

# Cambodia

Based on a rebound in tourism and clothing exports, recovery in 2010 was also supported by a good year in agriculture. However, there are indications that poverty has increased in recent years. The pace of economic growth is expected to pick up in the forecast period. Inflation will also rise. A new effort to promote rice production and exports goes some way to addressing the need to diversify sources of growth and reduce rural poverty.

## Economic performance

A bounceback in tourism and clothing exports, coupled with increased production of paddy rice, drove a 6.3% recovery in GDP last year (Figure 3.23.1) from a sharp slowdown in 2009 caused by the global economic crisis.

The primary sector, producing about a third of GDP, grew by an estimated 4.2% in 2010. Paddy rice output rose by about 5% to 7.9 million tons, mainly a result of favorable weather and better access by farmers to fertilizers and higher quality seeds. Livestock production increased by about 5.5%, whereas forestry and logging and fisheries output registered only slight growth.

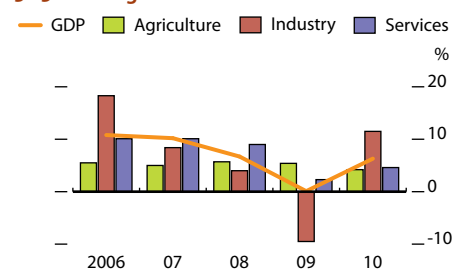
Recovery in global travel saw tourist arrivals rise by about 16% to 2.5 million, and tourism receipts by 14.5% to \$1.78 billion (Figure 3.23.2). The sharpest gains were in arrivals from Asia, including Viet Nam (up 48% to 466,700), the Republic of Korea (up 47% to 289,700), and the People's Republic of China (PRC—up 39% to 177,700). This rebound in tourism contributed to estimated growth of 4.3% for services.

Industry was the main contributor to GDP growth in 2010, expanding by an estimated 11.6% (it had contracted in 2009). External demand for Cambodian garments, principally from the United States (US) and the European Union (EU), rebounded. Data from the US Department of Commerce showed that US garment imports from Cambodia rose by 19% in US dollar terms in 2010 (Figure 3.23.3). Construction activity remained sluggish, reflecting a fall in foreign investment in property during the global crisis and slow pickup in residential building.

Increased deposits of foreign currency at banks drove a 20.0% year-on-year increase in M2 money supply in December 2010. Bank lending to the private sector picked up from 6.5% year on year at end-2009 to 27% 12 months later, reflecting the economic recovery. The riel appreciated by 2.4% against the US dollar over 2010.

A less expansionary fiscal stance saw the overall budget deficit trimmed to an estimated 6.0% of GDP, from 6.4% in 2009. Domestic revenue bounced back to the equivalent of 12.7% of GDP, higher than the

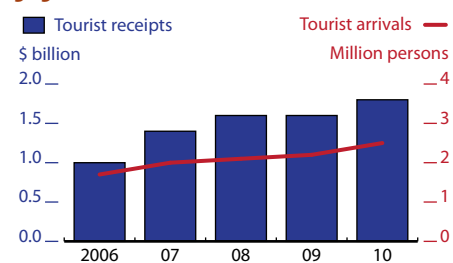
3.23.1 GDP growth



Sources: National Institute of Statistics; ADB estimates.

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3.23.2 Tourism indicators



Source: Ministry of Tourism.

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budget plan of 12.3% and the 2009 outturn of 11.9%. Given that revenue collection is still relatively low, the government aims to raise it by 0.5 percentage points of GDP a year over the medium term.

Government expenditure amounted to an estimated 18.6% of GDP, somewhat above the 17.6% budget target but lower than the 2009 peak of 20.5%. The higher than target spending was due principally to externally financed capital works. The deficit was largely financed by grants and concessional loans, with the drawdown of government bank deposits estimated at 0.5% of GDP, much lower than the 2009 outturn of 2%.

Consistent with a modest recovery in domestic demand, inflation in 2010 averaged 4.0% (Figure 3.23.4), a turnaround from 2009 when the consumer price index fell slightly in year-average terms.

In the external accounts, merchandise exports rose by an estimated 20.8% in US dollar terms, largely reflecting growth in garment exports to the US. Imports rose by an estimated 15.9%, mainly on increases in oil and in raw materials for garments. Overall, the 2010 current account deficit (excluding official transfers) narrowed slightly to an estimated 11.0% of GDP.

Foreign direct investment inflows rose by about 50% to \$801 million, reflecting strong growth in agriculture and garments. Special economic zones are attracting investments in light industry, especially those in Phnom Penh, Sihanoukville, and Svay Rieng. Donor inflows remained buoyant, and gross international reserves increased by 12% over the year to \$2.65 billion, equivalent to 4.7 months of imports of goods (Figure 3.23.5).

Current levels of public debt are considered manageable. External public debt is estimated at \$3.5 billion and domestic debt is very small. The PRC accounted for about 58% of total bilateral loan disbursements in 2010.

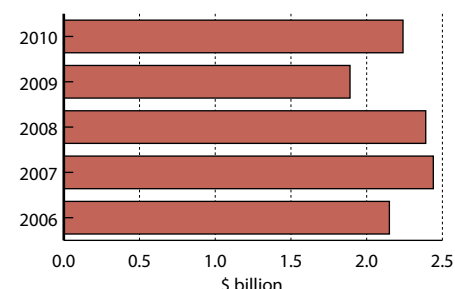
Latest available data show that 30% of the population lived in poverty in 2007, with the majority of the poor and vulnerable in rural areas. There are indications that poverty has increased since 2007 as a result of sharply higher food prices in 2008 and the economic slowdown in 2009. In response, the government has drafted a social protection strategy, expected to be launched in 2011. Immediate priorities of this strategy involve the expansion of targeted programs such as free health care for the poor, and the pilot testing of programs including conditional cash transfers and labor-intensive public works.

The government last year adopted an ambitious plan to increase paddy rice production and promote the milling of rice for export, which should benefit the 70% of the population that earns a living from rice. Targeting 1 million tons of milled rice exports by 2015 (compared with just 13,000 tons in 2009, according to the official estimate), the plan includes steps to expand irrigation facilities; improve the use of water, seed, fertilizer, and equipment; provide credit to farmers; encourage the private sector in rice processing and export; and reduce transport costs.

Longer-term measures in the rice plan will focus on improving farm yields and export competitiveness, for example by building roads, railways, and ports, and by improving land management.

Reflecting the gradual expansion of the private sector, the number of licensed enterprises grew to 38,023 at end-2010 from 36,116 in 2009. The government is eager to encourage new firms and new industries, but

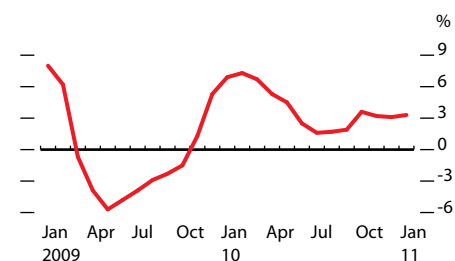
### 3.23.3 United States imports of textiles and clothing from Cambodia



Source: US Department of Commerce.

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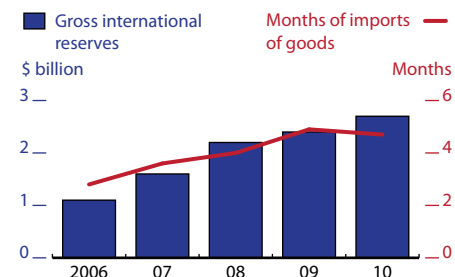
### 3.23.4 Inflation



Source: National Institute of Statistics.

[Click here for figure data](#)

### 3.23.5 Gross international reserves and import cover



Source: National Bank of Cambodia.

[Click here for figure data](#)

developing the private sector is constrained by infrastructure deficiencies, including the high cost of electricity and lack of access to affordable finance, especially for small and domestically focused firms.

The government adopted an anticorruption law in 2010 which, if well implemented, could significantly reduce the costs of doing business, strengthen the country's competitiveness, and improve public sector governance. A stock market is scheduled to open in 2011, with three selected state-owned enterprises planned for listing.

## Economic prospects

Assuming global economic growth in line with the *Asian Development Outlook 2011* assumptions, as well as favorable weather for agricultural production, GDP is projected to expand by 6.5% in 2011 and 6.8% in 2012 (Figure 3.23.6).

Growth in industry is projected at 10.8% in 2011, based largely on external demand for Cambodian garments from the US and EU. US garment imports from Cambodia in January jumped by 41% to \$214 million. A relaxation of EU rules of origin under the Generalized System of Preferences from January this year gave Cambodian garments duty-free access to the EU, regardless of the origin of the fabric. Cambodian milled rice also received preferential access to the EU. Consequently, milled rice exports to that market rose by 228% to 10,495 tons in the first 2 months of this year from the prior-year period.

Construction is projected to expand by a modest 3% this year. The government in 2010 liberalized restrictions on foreign ownership of apartments, which is expected to help stimulate some additional demand. Offshore oil and gas production is expected to come on stream in late 2012.

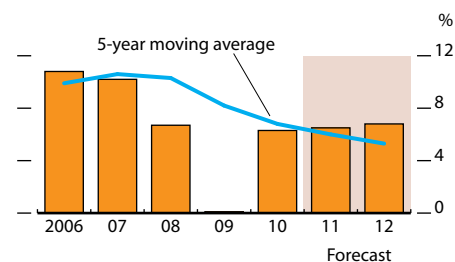
Growth in services looks set to pick up to about 5% this year. Tourist arrivals rose by 18% in January 2011 from the prior-year period, while trade and transport and communications are likely to continue expanding, as domestic consumption and the business outlook improve. Agricultural production is seen increasing by 4.3%, supported by the government's commitment to promote rice production and exports.

Government spending is forecast to grow marginally faster than revenue in 2011, owing to increases in capital outlays, and the budget deficit is expected to be 6.2% of GDP. External financing (concessional loans and grants from bilateral and multilateral lenders) will cover most of the deficit, leaving a shortfall equivalent to 0.9% of GDP (compared to an estimated 0.5% of GDP in 2010) to be financed by drawdowns on government bank deposits at the central bank.

Upward pressure on prices will be generated by the strengthening domestic demand, generally expansionary fiscal policy, and higher global prices for food and fuel. Inflation is forecast to average 5.5% (Figure 3.23.7).

The planned increase in domestic financing of the budget, coupled with the quickening of economic growth and inflation, suggests the need for a gradual tightening of monetary policy during the forecast period. However, the high degree of dollarization of the economy (amounting to as much as 95% of currency in circulation) limits the effectiveness of monetary policy.

### 3.23.6 GDP growth



Source: Asian Development Outlook database.

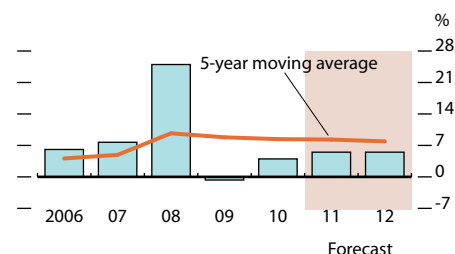
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### 3.23.1 Selected economic indicators (%)

	2011	2012
GDP growth	6.5	6.8
Inflation	5.5	5.5
Current account balance (share of GDP)	-10.7	-10.2

Source: ADB estimates.

### 3.23.7 Annual inflation



Source: Asian Development Outlook database.

[Click here for figure data](#)

The trade deficit is expected to remain substantial, in part a result of the higher cost of imported oil in 2011. On the positive side, a rise in tourism receipts will contribute to a surplus in services trade. The current account deficit (excluding official transfers) is forecast at 10.7% in 2011 and 10.2% in 2012 (Figure 3.23.8). Gross international reserves are projected to rise to \$2.84 billion in 2011.

Risks to the forecasts center on external events, such as unexpected global economic weakness or higher than assumed oil prices, which could hurt the prospects for Cambodia's tourism and clothing exports and push up inflation. Tourism could also be affected by any intensified conflict on the border with Thailand or by renewed political strife in Thailand. Lack of progress on fiscal consolidation, with low tax revenue and absence of government debt securities, may lead to problems in funding the fiscal deficit. The relatively low involvement of Japan in Cambodia's trade, tourism, and foreign investment suggests a modest effect on the economy from the earthquake in Japan in March 2011.

## Development challenges

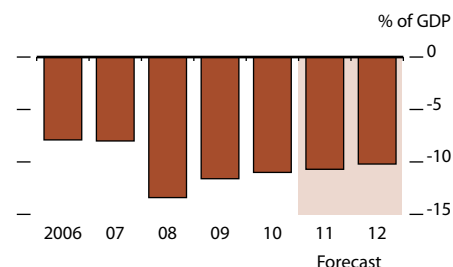
The impact of the global recession on the economy highlighted the need for Cambodia to reduce vulnerability to external shocks by accelerating economic diversification and improving competitiveness of industries.

Sources of growth in recent years—garments, tourism, and construction—were all hit hard by the global downturn. A stronger agriculture sector would not only diversify sources of growth but also help to extend development to rural areas where 90% of the poor live. Food exports to Asian markets such as the PRC would reduce the heavy reliance on the US and EU clothing markets—hence the government's efforts to promote rice production and milled rice exports.

The clothing and tourism industries are hampered by high costs for electricity, until Cambodia builds its generation and distribution capacities, and for trade, which involves numerous bureaucratic procedures and unofficial fees. These industries need to raise the quality of their products and services and develop skills to support higher-value-added activities.

Cooperation is increasing with neighboring countries to enable Cambodia to tap into growing markets through increased connectivity. The country lies at the heart of the Greater Mekong Subregion southern economic corridor extending from Thailand to Viet Nam through highways and railway links that form part of the Singapore–Kunming rail project. To meet competition in these markets and to strengthen value chains in agriculture, manufacturing, and tourism, Cambodia needs to intensify efforts to reduce transport and logistics costs, especially at ports and border crossings.

3.23.8 Current account balance



Source: Asian Development Outlook database

[Click here for figure data](#)