I. ECONOMIC ENVIRONMENT

(1) INTRODUCTION

1. Cambodia's accession to the WTO in 2004 came in the middle of a decade of strong economic growth. The economic and social achievements between 1998 and 2007 were the most impressive in Cambodia's history: real GDP growth averaged close to 10% over this period, the highest of any low-income country in Asia, resulting in an almost doubling of income per capita; the poverty incidence is estimated to have fallen steadily; consumer price inflation declined markedly compared with the 1990-98 period; and prudent fiscal policies underpinned macroeconomic stability. The recent discovery of oil and gas could be a significant boon for the country and, if properly managed, should provide the necessary resources to continue addressing a range of socio-economic issues.

2. However, after the decade of high growth and relative stability, the 2008-09 global recession exposed Cambodia's longstanding structural vulnerabilities, notably that growth and exports have remained narrowly based. The authorities are aware that diversified private-sector-led growth is important for raising Cambodia's growth potential. To this end, there have been initiatives during the review period to strengthen the investment climate, reduce the cost of doing business and improve Cambodia's international competitiveness, expand market access through trade agreements, and enhance agricultural development and rural infrastructure to help broaden the sources of growth.

(2) ECONOMIC AND POLICY DEVELOPMENTS AFFECTING TRADE

(i) Main economic developments

3. Cambodia enjoyed a decade of high growth and relative stability prior to the recent global crisis, enabling improvements in living standards and poverty reduction. Cambodia's exceptional growth performance between 1998 and 2007, at an annual average of 9.4%, relied on four drivers of GDP growth: rapid garment exports, strong tourism receipts, a construction boom, and robust crop growth in agriculture. Growth in output and trade was underpinned by an open trade regime and a favourable regime for foreign direct investment. After liberalizing its economy and its trade regime in the 1990s, Cambodia joined ASEAN in 1999 and was the first LDC to complete WTO accession negotiations.

4. However, the global crisis resulted in a growth collapse, exposing longstanding structural vulnerabilities. A downturn in three of the four drivers of growth, agriculture being the exception[1], caused growth to slip to under 7% in 2008 and to contract by an estimated 2% in 2009 (Table I.1). The narrow concentration of the sources of growth has made Cambodia vulnerable to external shocks and to the United States' economic cycle. Garment exports and tourism revenues were hit hard from the effects of the global financial crisis and in particular the severe economic recession in the United States. Several large projects, especially in the real estate and tourism sectors, were deferred. Actual foreign direct investment in Cambodia is estimated to have fallen from US$815 million in 2008 to US$530 million in 2009.

[1] The primary sector, the economy's fourth driver producing about 30% of GDP, maintained trend growth and served as a social safety net for many laid-off workers.

Table I.1
Selected economic indicators, 2004-10

	2004	2005	2006	2007	2008	2009[a]	2010[a]
Income and growth							
GDP per capita at current market price (US$)	401.3	466.2	534.9	626.0	739.4	732.9	791.2
GDP growth (%, constant 2000 prices)	10.3	13.3	10.8	10.2	6.7	-2.0	4.8
Agriculture[b]	-0.9	15.7	5.5	5.0	5.7	5.4	4.0
Manufacturing	17.7	9.7	17.4	8.9	3.1	-5.3	1.8
Services	13.2	13.1	10.1	10.1	9.0	2.3	3.3
Savings and investment (current market prices, % of GDP)							
Gross domestic investment	18.6	21.4	22.7	26.5	22.6	22.7	..
Gross national savings	16.3	17.2	21.7	22.6	10.3	17.9	..
Prices and interest rates							
Inflation (CPI, %age change, annual average)	3.9	6.3	6.1	7.6	25.1	-0.4	4.0
Inflation (CPI, %age change, end-year)	5.3	8.4	4.2	14.0	12.5	5.3	3.1
Deposit rate (%)	1.79	1.92	1.84	1.90	1.91	1.66	1.26
Lending rate (foreign currency) (%)	17.62	17.33	16.40	16.18	16.01	15.81	15.63
Government finance (% of GDP)							
Revenue	10.4	10.6	11.4	12.1	13.3	11.8	12.6
Current revenue	10.3	10.0	10.1	12.0	13.1	11.7	12.5
Tax revenue	7.7	7.7	8.0	10.2	11.2	10.1	10.6
Expenditure	14.2	13.2	14.1	14.7	15.9	17.5	17.8
Current expenditure	8.4	7.9	8.2	8.5	9.4	10.7	10.8
Current fiscal balance	1.9	2.1	1.9	3.5	3.7	1.0	1.6
Overall balance	-3.8	-2.6	-2.7	-2.6	-2.7	-5.7	-5.3
External sector (% of GDP, unless otherwise indicated)							
Current account	-8.2	-9.8	-7.9	-8.0	-13.3	-11.6	-10.9
Net merchandise trade	-12.8	-16.1	-14.8	-15.6	-17.4	-15.7	14.9
Merchandise exports	48.5	46.2	50.8	47.3	45.5	40.3	41.1
Merchandise imports	61.3	62.3	65.6	62.9	62.9	56.0	56.0
Services balance	5.4	7.6	6.8	7.3	5.9	5.8	5.6
Services exports	15.1	17.8	17.8	17.9	15.9	15.6	14.5
Services imports	9.6	10.2	11.1	10.6	10.0	9.8	8.9
Financial account	4.1	4.9	2.9	7.9	13.4	5.8	5.6
Foreign direct investment	2.3	6.0	6.5	10.0	7.7	4.9	4.9
Balance of payments	1.1	1.2	2.7	4.9	5.0	-0.0	1.3
Terms of trade (2005 = 100)	100.9	100.0	99.7	98.8	99.6	..	..
Merchandise exports (annual %age change)	24.0	12.4	27.0	10.7	15.2	-10.9	11.7
Merchandise imports (annual %age change)	22.5	19.8	21.8	13.8	19.8	-10.4	9.5
Service exports (annual %age change)	46.9	38.9	15.9	19.4	6.3	-1.2	1.7
Service imports (annual %age change)	18.6	24.9	25.1	13.9	12.3	-1.7	0.1
Foreign exchange reserves (US$ million)	708.9	834.0	1,096.7	1,615.6	2,163.5	2,259.9	2,550.0
in months of imports	2.1	2.0	2.2	2.8	3.2	3.7	3.6
Total external debt stocks (US$ million; end-period)	2,991.7	3,350.2	3,698.0	4,313.1	4,395.5	4,357.6	5,033.2
Debt service ratio[c]	1.0	0.9	0.7	0.7	0.7	0.8	0.8
Memorandum items							
Current GDP (riels billion)	21,438.3	25,754.3	29,849.5	35,042.2	41,968.4	43,080.0	47,680.0
Current GDP (US$ million)	5,337.8	6,293.0	7,274.5	8,639.2	10,351.8	10,407.6	11,393.3
Rs/US$ (annual average)	4,016.3	4,092.5	4,103.3	4,056.2	4,054.2	4,139.3	4,184.9
Population (millions)	13.3	13.5	13.6	13.8	14.0	14.2	14.4

.. Not available.

a Estimates.
b Including forestry and fishing.
c As a percentage of exports of goods and services.

Source: Data provided by authorities; IMF (2010), *International Financial Statistics,* September; IMF (2009), *Country Report No. 11/45,* February.

5. The crisis and its impact on Cambodia's real sector exposed both structural and competitiveness weaknesses in the economy. For example, garment exports from Cambodia contracted by more than other countries in the region (such as Bangladesh) – indicative of a possible decline in the competitiveness of this sector. Growth and exports have remained narrowly based, offering limited benefits to the rural poor, which constitute Cambodia's vast majority. In 2010, however, driven by exports, the Cambodian economy achieved a stronger than expected recovery with estimated GDP growth of 4.8%, according to the IMF. The strength of the recovery was driven by two of Cambodia's traditional growth drivers, indicating that a broadening export-led recovery was under way. First, garment exports registered a 24% increase in 2010, after shrinking by 20% during the 2008-09 crisis and, second, tourism rebounded strongly with a 16% increase in tourist arrivals (to 2.5 million tourists) and a 14% increase in tourism receipts (to US$1.8 billion).

6. Cambodia's economy is continuing to recover from the 2008-09 downturn but annual growth is not expected to return to the highs of around 10% recorded in the years preceding the crisis. However, real GDP growth is expected to remain strong in 2011, at around 6%, as are Cambodia's garment and footwear exports, due partly to the EU's relaxed rule of origin on preferential tariffs for LDC exports to EU markets, effective 1 January 2011. Agriculture is becoming an increasingly important source of economic growth in line with official plans to boost exports of milled rice as the government seeks to develop other sources of economic growth.

7. With GDP per capita at around US$790 in 2010, Cambodia remains a very poor country. The poverty rate was estimated to have decreased moderately from 47% in 1993 to 35% in 2004 and to an estimated 30% in 2007, with rural poor comprising 90% of the total.[2] Further reductions in the poverty level have been problematic since then due to the unexpectedly sharp rise in consumer prices, notably for foodstuffs, in 2008 and the effects of the global economic crisis. The Government has adopted the Updated National Strategic Development Plan (NSDP) to extend its development targets until 2013. The updated plan targets economic growth of 6% a year and per capita income of nearly US$1,000 by 2013. Maintaining high, broad-based economic growth and a pro-poor policy is crucial to realizing the goal of reducing the poverty rate to 19.5% by 2015 as targeted in Cambodia's Millennium Development Goals.

(ii) Main macroeconomic policies

8. Cambodia's macroeconomic framework is based on a continuation of the prudent monetary and exchange rate and fiscal policies that have enabled it to achieve its impressive economic track record.

(a) Monetary and exchange rate policies

9. Over the past 20 years, consumer price inflation has fallen sharply from an average of 56% over 1990-98 to an average of 3.5% over 1998-2007. Inflation then started rising again[3], with the spike in food and energy prices, although this was happening nearly everywhere. Moving into 2009, inflation decelerated to 5.3% from high levels, as world food and oil prices fell, and weakening domestic demand further subdued price pressures. Despite price hikes in other countries in the region and a rapid economic recovery, Cambodia's consumer price inflation dwindled to 3.1% in 2010.

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[2] Poverty is defined as the percentage of the population with per capita consumption below the national poverty line, which was 2,470 riels per capita per day in 2007 or about US$0.61 at the prevailing exchange rate (Ministry of Planning, 2010, p. 8).

[3] Inflation accelerated from 6.4% in September 2007 to a peak of 25.7% in May 2008, driven largely by the surge in oil and food prices.

10. In recent years, the riel has been stable *vis-à-vis* the dollar, in nominal terms, leading to some depreciation *vis-à-vis* other currencies. Fluctuations of the riel in real terms have a diffused impact given the *de facto* high dollarization of the economy, and the U.S. dollar remains the currency of choice in Cambodia for trade and investment. According to the IMF, Cambodia has become Asia's most dollarized economy (over 90% of total bank deposits are held in U.S. dollars)[4], which reflects Cambodia's unbalanced and narrow growth, driven by the dollarized urban export and tourism centres as well as FDI and aid inflows. The effectiveness of monetary policy remains limited owing to this extensive dollarization which, according to some observers, is likely to have enhanced Cambodia's trade (in particular the surge in garment exports to the United States since 1995).[5]

(b) Fiscal policy

11. In a substantially dollarized economy, fiscal policy is the main macroeconomic policy instrument. A major problem for Cambodia over the past decade has been the poor rate of revenue generation although efforts are under way to broaden the tax base through an increase of the road tax on vehicles and the introduction of a tax on property. An outstanding feature of Cambodia's tax base is the high share of trade-related taxes (customs duties and excise duties and VAT on imports) in total tax revenue. Although these taxes have been declining, from 69.5% of total tax revenue in 2004 to 56.3% in 2010, they still account for over half of the total revenue, with fuel and vehicle imports alone accounting for a combined 60% of total customs revenue (see Table III.2).

12. According to the IMF, Cambodia's revenue mobilization remains among the weakest in the region with a tax revenue to GDP ratio of between 10% and 11%, which has seriously limited Cambodia’s ability to address priority development needs. Cambodia will therefore continue to depend on foreign grants and loans to finance its deficit, which reached the equivalent of 5.3% of GDP in 2010.

13. The Government is committed to further improving customs administration and tax collection in order to secure fiscal sustainability and mobilize resources for Cambodia's heavy development needs. In this regard, reducing the scope for evasion is significant. For example, the Customs Valuation Agreement applies to petroleum imports as of 1 January 2011 and the IMF estimates that replacing the reference price for taxes on petroleum imports to the current transaction level could result in a gain of about 1% of GDP, assuming that the resulting increase in domestic retail prices over those in neighbouring countries does not erode the tax base.[6] This would require that greater incentives for smuggling are effectively curbed by improvements in customs control. Smuggling continues to erode the tax base, given Cambodia's stretched and porous border, but the authorities assert that anti-smuggling efforts have been stepped up in recent months.

14. In the longer term, the fiscal picture could change markedly if substantial revenues begin to flow from the production of oil and natural gas, which constitutes a major opportunity and challenge for Cambodia's medium- to long-term development.

(iii) Trade competitiveness

15. During the review period (2004-10), the Government continued to adopt laws and regulations both to enhance private sector activity and to fulfil its WTO commitments. While on paper the legal

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[4] Measured as the ratio of foreign currency deposits to broad money, dollarization has risen steadily, from about 60% in the late 1990s to about 80% in 2010 (compared with 50% in Laos and 20% in Viet Nam) (IMF, 2010, p. 14).

[5] IMF (2002), p. 29. See also ADB (2008).

[6] IMF (2010), p. 12.

framework for greater private sector development is taking shape, more needs to be done to implement laws and regulations and to create an environment to attract higher levels of employment-generating investment. As evidenced by a number of surveys, Investment Climate assessments and Doing Business indicators, the business environment remains challenging in many aspects. Available infrastructure in key backbone services – electricity, advanced telecommunications, and transportation infrastructure – is also poor and, where these depend on public investment, it will take Cambodia as an LDC time to redress underinvestment.

16. Access to finance is also limited, despite the recent rapid economic growth. The incidence of labour disputes has recently increased significantly. Dispute resolution mechanisms remain weak. Regulations are either absent (or not enforced), or costly (with significant informal payments). Poor governance is also noted in natural resource management, with continued issues of weak management of common pool resources and encroachment on private land.

17. Despite increasing investor interest, Cambodia continues to rank poorly on global surveys of competitiveness and corruption. The World Bank suggests that regulatory uncertainty and excessive red tape, remaining distortions in the trade regime, electricity costs, inadequate skills of the labour force, and corruption are major obstacles to private sector growth and development of export competitiveness.[7] The World Bank identifies poor product quality, an inadequate SPS policy framework, limited access to technology and business development services, underdeveloped links between the rural and modern sectors of the economy, and relatively costly logistics as constraints to export diversification. A common thread in many value-chain studies is Cambodia's weak competition policy framework, broadly defined to include remaining distortions at, and behind, the border.

18. According to the World Economic Forum[8], Cambodia's competitiveness ranking is low, at 110 of 133 countries surveyed. Foreign investors in general have also been deterred by red tape and high utility costs, all of which detract from the advantages of low labour costs. In 2009, Cambodia also remained low in Transparency International’s corruption index, ranking 158 out of 180 countries assessed. Business people, both local and foreign, have identified corruption, particularly within the judiciary, as the single biggest deterrent to investment in Cambodia.[9] The long-awaited anti-corruption legislation, approved by the National Assembly in March 2010, was implemented later in the year. Cambodia is not a signatory to the OECD Anti-Bribery Convention, but has endorsed the ADB/OECD Anti-Corruption Action Plan for Asia and the Pacific. In 2007, the Government signed a regional anti-corruption pact with eight other ASEAN countries, and in September of the same year, signed the UN Convention Against Corruption.

19. The Government has reviewed the global environment for Cambodian exports and concluded that tariff advantages are unlikely to drive future export growth. It derived from this the need to diversify exports and export markets and identified 19 products and services with potential for export diversification, 12 of which are in the agriculture, forestry and fisheries sector. The most important is rice, for which the Government has prepared an ambitious plan to make Cambodia the world's third largest exporter of rice (regarded as the country's "white gold"), behind Thailand and Viet Nam, by 2015. The other products are: rubber, cassava, fishery, fruits and vegetables, wood products, soybeans, silk, livestock, cashew nuts, corn, and beer. In the industrial sector, wood products, light manufacturing assembly, footwear, and garments are listed, and in the services sector, tourism, labour services sector, transport, and business and web-based services.

[7] World Bank and International Finance corporation (2009).
[8] WEF (2010).
[9] See also World Bank (2010a).

20. The Government has identified a number of shared challenges for Cambodian sectors with export potential. Factors that continue to constrain export diversification include: high production and infrastructure costs, low competitiveness and low productivity; limited value added in many sectors, due to high import dependency for raw materials and intermediate inputs; poor quality and limited differentiation of products, limited access to technology, and small design and R&D capacity; in many sectors, enterprises have difficulties meeting exacting quality standards of various foreign markets as well as meeting time delivery requirements of foreign buyers; a legal and institutional framework for business export development that remains underdeveloped, although improving; and, in terms of licences, despite progress in some areas – such as the one-stop services at the Cambodia Investment Board (CIB) or at Special Economic Zones (SEZs) – the regulatory burden remains significant for small and medium firms, which often opt to do business in the informal sector.

(iv) Current account

21. Cambodia's balance of payments remains stable but vulnerable to external shocks due to its relatively low level of gross international reserves compared with imports. Cambodia has been running a sizeable current account deficit due to rapid growth in investment, averaging around 9% of GDP between 2004 and 2009, although in 2009 the weak economy prompted a major fall in imports, which narrowed the current account deficit, after it peaked at 13.3% in 2008, and stymied inflation. The widening of the current account deficit in 2010 (to -10.9% of GDP) was driven mainly by the trade deficit, as both imports and exports recovered strongly and global oil prices increased. As export and tourism growth continues to firm up, the Cambodian authorities expect the current account deficit to be reduced in 2011.

22. Large inflows of private investment, remittances, and foreign assistance have so far enabled the authorities to maintain increasing international reserves. Gross official reserves stayed broadly stable in 2010, at around US$2.5 billion or 3.6 months of imports; the relatively low import coverage makes Cambodia's external balance vulnerable to shocks and below what are considered to be prudential levels (around ten months) in many countries. The global financial crisis also affected capital inflows, in particular foreign direct investments to the construction sector. With fewer international banks provides financing for direct investment in 2009, FDI contracted by an estimated US$285 million.

23. Cambodia's trade sector (goods and services) is heavily correlated with the business cycle of the developed economies such as the United States and European Union. The Government estimated exports of goods contracted by 11% in 2009, with export of garments falling by 23%. Tourist arrivals (or export of services), contracted marginally by 0.8% in 2009 due to a decline in global travel. As the global outlook improves in 2010, the trade sector is expected to improve with export of goods to increase by 11.7% (garment experts by 7%). However, a full recovery in garment exports may not occur until 2012.

(3) DEVELOPMENTS IN TRADE AND FDI

24. Cambodia's exports have been growing relatively rapidly, driving growth over the last decade. Starting from 16% of GDP in 1993, exports of goods and services accounted for nearly 56% of GDP in 2010 based on balance of payments (BOP) statistics. Growth in exports has been one of the main drivers of Cambodia’s strong economic performance. Garments and tourism account for most of the exports and there has been little diversification towards other goods and services. Even within garments, there has been little diversification beyond low-end garments and the U.S. market, which, for a historical reason related to increased access to quotas under the Multi-Fibre Arrangement, is the main export market. In parallel, imports of goods and services, according to BOP figures, increased

from 32% to 65% of GDP during the same time period, partly due to the increase of the trade deficit in the energy and manufacturing sectors owing to the expansion in economic activity and to high oil prices.

(i) Merchandise trade

25. The garment industry dominates foreign trade, overshadowing contributions from other subsectors such as rubber and rice. From 1997, the traditional exports, e.g. logs, sawn timber, and rubber, were increasingly superseded by sales of garments, which accounted for 44% of domestic exports (excluding re-exports[10]) in that year and for about 90% in 2005 and 80% in 2010. Cambodia has a rather narrow export profile in terms of what it exports but managed to reduce its dependence on the U.S. market during the review period.

(a) Exports

26. According to Cambodia's customs-based trade statistics[11], Cambodia's export revenue has recorded fairly strong growth in recent years, increasing from US$2.4 billion in 2005 to US$3.8 billion in 2010 (Chart I.1 and Table AI.1). Garment exports accounted for between 80% and 90% of total exports during the five-year period. There had been concerns that export revenue would decline sharply in 2005, following the expiry at end 2004 of the WTO's global system of quotas on trade in textiles and garments. However, partly because the United States and the EU imposed restrictive safeguards on imports of garments from China, Cambodia's garments exports remained strong. The rubber industry increased its share of exports slightly in 2010 to 2.1%, partly reflecting increased investment in recent years, but it still struggles to compete with neighbours such as Malaysia and Thailand. Another major traditional export, forestry products, recorded declines in recent years to negligible levels.

27. Until the mid 1990s, Cambodia's main export markets were other Southeast Asian economies with Singapore and Thailand alone accounting for over 50% of exports in 1995. However, following Cambodia's bilateral trade agreements with the United States, the United States became the leading market for Cambodian exports (Chart I.2 and Tables AI.3). In 2005, the U.S. accounted for two-thirds of Cambodian exports, this share declined to half of the total in 2010, while Canada, the EU and Asia all increased their share of Cambodian exports.

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[10] Re-exports used to represent a significant feature of external trade, prompted by the differences in import tariffs between Cambodia and its neighbours, and included cigarettes, motorcycles, beer, and electrical equipment (re-exported to Viet Nam) and gold (principally re-exported to Thailand). In the late 1990s, however, re-exports declined sharply: they accounted for 62% of total exports in 1995, but only an estimated 5% of the total in 2009.

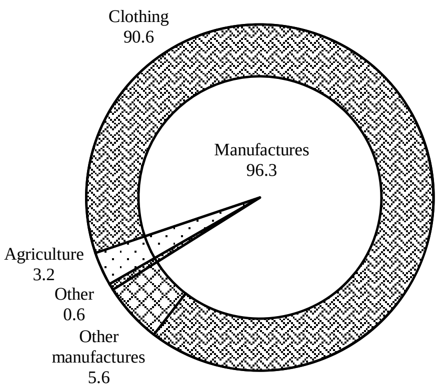
[11] The total value of exports varies considerably between national sources and the IMF. In addition, a considerable amount of unregistered cross-border trade with Viet Nam and Thailand makes it difficult to determine the exact volume of trade going on. Figures cited in this section exclude exports of so-called printed matter, consisting mainly of trade in bank notes. BOP figures are considerably higher than customs-based trade statistics as BOP data adjust customs figures to reflect trade in printed matter, estimates of under-reporting, informal trade, and border trade.

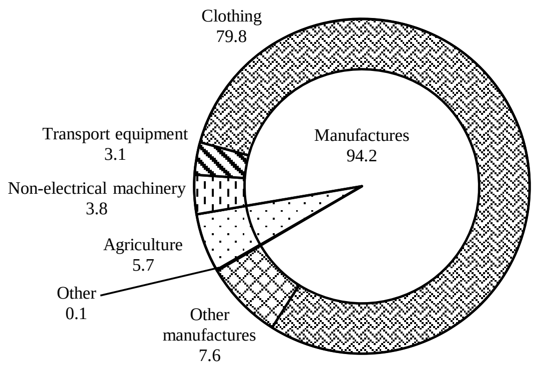
Chart I.1
Product composition of merchandise trade (SITC Rev.3), 2005 and 2010

Per cent

2005 | **2010**

(a) Exports (f.o.b.)

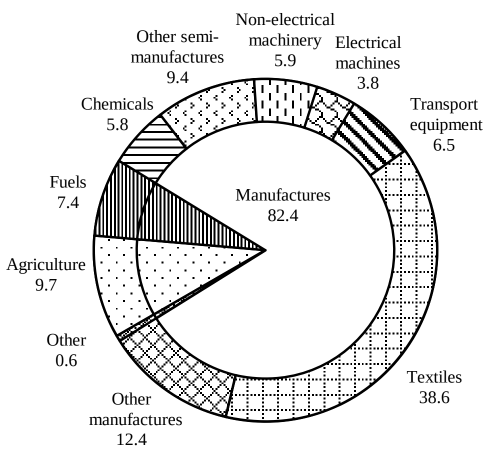


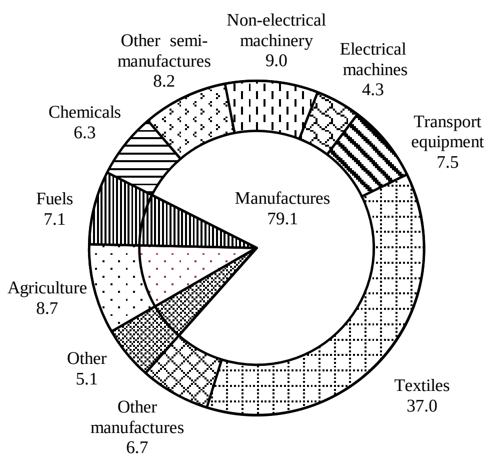


Total: US$2,434.6 million

Total: US$3,808.7 million

(b) Imports (c.i.f.)





Total: US$2,546.3 million

Total: US$4,876.0 million

Note: Exlcuding trade in bank notes.

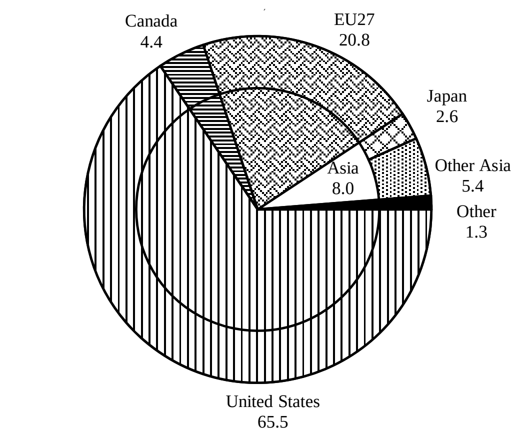
***Source*: WTO calculations, based on data provided by the authorities.**

Chart I.2
Direction of merchandise trade, 2005 and 2010

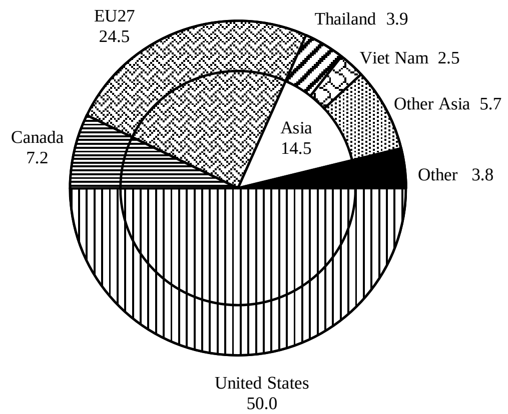
Per cent

2005 | **2010**

(a) Exports (f.o.b.)

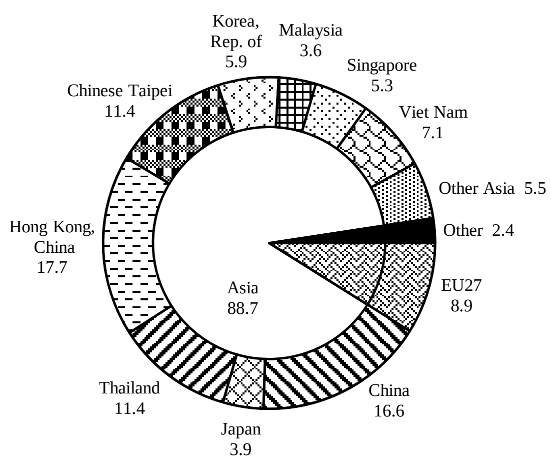


Total: US$2,434.6 million

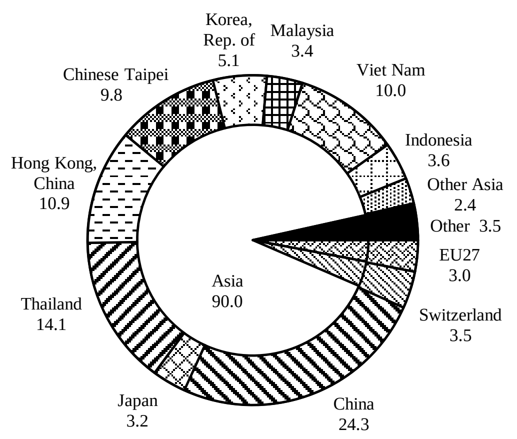


Total: US$3,808.7 million

(b) Imports (c.i.f.)



Total: US$2,546.3 million



Total: US$4,876.0 million

Note: Excluding trade in bank notes.

***Source*: WTO calculations, based on data provided by the authorities.**

(b) Imports

28. As with Cambodia's exports, many of its imports are not registered due to smuggling. The domestic garment and tourism industries both rely extensively on imports and, generally, the country remains dependent on imports for a wide range of manufactured products and consumer goods. Based on customs data, Cambodia's import bill nearly doubled between 2005 and 2010, from US$2.5 billion to US$4.9 billion (Chart I.1 and Table AI.2). During the review period, the import structure changed little, with manufactures (including textiles and textiles articles, machinery and transport equipment, chemicals, and electrical components) accounting for 80% of imports and primary products (mainly food and oil) accounting for about 17%.

29. Similarly, the main import sources have changed little since 2005 with Asia accounting for around 90% of imports, led by China (which now provides 24% of Cambodia's imports); Thailand; Hong Kong, China; Viet Nam; and Chinese Taipei (Table AI.4).

(ii) Services trade

30. Although services payments have been pushed up by trade-related services costs, the services account has remained in surplus, owing to healthy revenue growth in tourism. Tourism receipts contracted marginally (by 0.8%) in 2009 due to a decline in global travel (Table I.2). The balance in the service sector was largely in surplus (about 6% of GDP), owing to the sharp increase in receipts from tourism. The services surplus is expected to grow in the near term as tourism recovers. However, there will be an increase in demand for imported trade-related services, such as insurance and freight.

Table I.2
Trade in services, 2004-10
(US$ million and %)

	2004	2005	2006	2007	2008	2009	2010
Services balance (US$ million)	290.0	475.6	492.3	632.1	609.4	606.4	633.0
Receipts (US$ million)	804.9	1,118.1	1,296.3	1,547.5	1,645.1	1,624.9	1,652.6
	(% of total receipts)						
Transportation	13.0	11.4	12.9	13.6	14.5	11.8	8.7
Travel	76.0	75.1	74.3	73.3	74.1	72.9	75.6
Other	12.0	13.6	12.8	13.1	11.4	15.3	15.7
Payments (US$ million)	514.4	642.6	804.0	915.4	1,035.8	1,018.4	1,019.5
	(% of total payments)						
Transportation	68.0	56.1	54.7	55.9	58.7	52.9	50.2
Travel	9.3	15.1	15.2	13.4	9.3	10.2	11.1
Other	32.7	28.9	30.1	30.7	32.0	37.0	38.8

Source: Data provided by the Cambodian authorities.

(iii) Foreign direct investment (FDI)

31. Investors were attracted to the construction and tourism industries in 1993, with Cambodia's cultural heritage perceived to have strong potential. A second wave of investors between 1996 and 1998 focused on the logging sector, while the bilateral trade agreement with the United States signed in 1996 encouraged substantial FDI in the garment sector. Prior to the discovery of petroleum and gas reserves, the majority of investment was concentrated within the three main sectors, garments, construction, and tourism, which together represented more than 80% of total capital registered. Investment approved by the Council for the Development of Cambodia (CDC) declined during

1999-2004; potential investment totalled US$201 million in 2004, while actual investment was US$131 million.

32. The amount of approved (potential) investment subsequently increased significantly, rising from US$589 million to US$2.4 billion in 2006 and US$7.2 billion in in 2008. According to figures provided by the National Bank of Cambodia, actual investment increased more moderately from US$381 in 2005 to more than US$800 million in 2007 and 2008 and declined thereafter (Table I.3). The total stock of FDI has reached the equivalent of about 50% of GDP.

Table I.3
Foreign direct investment, 2004-10
(US$ million)

	2004	2005	2006	2007	2008	2009	2010
FDI (implemented)	131	381	483	867	815	530	553
Approved projects (fixed assets)	201	589	2,390	1,382	7,169	2,229	2,496
FDI stock	2,090	2,471	2,954	3,821	4,637	5,167	5,720

Note: Revised figures based on the National Bank of Cambodia's source (for FDI and FDI stock).

Source: NBC.

33. FDI in manufacturing is largely concentrated in the garment industry, with investors from China accounting for over 90% of investment approvals over the past five years. The enthusiasm of Chinese investors in expanding in the Cambodian garment industry has alleviated concerns that the abolition of the MFA would result in significant export losses. In recent years, FDI has also begun expanding into other labour-intensive export lines, such as shoes, toys, and wood products. As FDI-driven exports in these sectors increase over time, it is possible that significant inroads can be made in addressing under-employment and poverty in Cambodia.

34. China is Cambodia's largest investor, followed by the Republic of Korea, Malaysia, the United States, Chinese Taipei, Thailand, Russia, and Singapore. Most Chinese investment is in the garment industry. Recently, two Chinese companies applied to invest in oil refining; and there has been Chinese interest in investing in hydroelectricity, railways, and oil and gas exploration.

(4) OUTLOOK

35. Cambodia's economic recovery is under way. Real GDP growth is projected to reach 6% in 2011, driven by a rebound in exports (particularly garments) and tourism, and the uninterrupted growth of agricultural production. Growth prospects depend largely on the performance of the agriculture sector, which has weathered the global crisis well, but crop production might be negatively affected by the sporadic droughts in some parts of the country. Even if these developments were to materialize, they would be offset by a surge in exports of milled rice. The sector has benefited from the recent adoption of paddy production and rice export policy.

36. The merchandise trade deficit will remain substantial in the short term, owing to Cambodia's reliance on imported capital goods. Even after economic growth recovers in the United States, Cambodia's leading export market, garment manufacturers may struggle to compete with more efficient producers. High overheads, poor infrastructure and stiff competition from other garment manufacturers, such as Bangladesh, are casting a shadow over Cambodia's long-term garment prospects. Agriculture offers potential to diversify the export base: there is room to substantially boost rice exports as rice yields are among the lowest in the region due in part to limited use of improved seeds and fertilizer and the need for better water management.

37. In the medium term, there is a clear need to diversify the economy, which is overly dependent on the garment, tourist, and construction industries. Both the garment and tourist industries were undermined by the global economic slowdown, resulting in serious export and job losses, although recovery has been impressive. The construction sector was weakened by the bursting of the property bubble, which undermined the banking system by boosting non-performing loans, prompting the IMF to urge the central bank to strengthen the supervision of Cambodia's financial system. Initiatives to improve the business environment and address infrastructure bottlenecks are critical. The recently promulgated Anti-Corruption Law could help reduce the cost of doing business, thereby improving Cambodia's international competitiveness, given that Cambodia ranks low in number of governance indicators.