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Trade Policy Review Body

TRADE POLICY REVIEW

Report by the Secretariat

CAMBODIA

This report, prepared for the first Trade Policy Review of Cambodia, has been drawn up by the WTO Secretariat on its own responsibility. The Secretariat has, as required by the Agreement establishing the Trade Policy Review Mechanism (Annex 3 of the Marrakesh Agreement Establishing the World Trade Organization), sought clarification from Cambodia on its trade policies and practices.

Any technical questions arising from this report may be addressed to Mario Kakabadse (tel.: 022 739 5172).

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SUMMARY

1. With macroeconomic stability firmly entrenched by the time of Cambodia's accession to the WTO in 2004, the country embarked on implementing far-reaching reforms to achieve rapid and sustained socio-economic development. International trade has been crucial to achieving this goal as it has been the driving force behind much of Cambodia's recent economic growth and poverty reduction, linking its economy more firmly to regional and global markets.

(1) ECONOMIC ENVIRONMENT

2. Cambodia's accession to the WTO in 2004 came in the middle of a decade of strong economic growth. Its economic and social achievements between 1998 and 2007 were particularly impressive: real GDP growth averaged close to 10%, 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 to the 1990s, and prudent fiscal policies underpinned macroeconomic stability. The 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.

3. The global recession caused the Cambodian economy to contract by an estimated 2% in 2009 and exposed Cambodia's long-standing structural vulnerabilities, notably that export-led growth remained narrowly based on garments and tourism, In 2010, however, driven by exports, the Cambodian economy achieved a stronger than expected recovery, with estimated GDP growth of 4.8%. Cambodia remains heavily dependent on exports of garments to the United States and the European Union, its main export markets. Imports are concentrated in manufactures, food, and fuel predominantly from Asia.

4. Despite a costly business environment, Cambodia's liberal investment regime has helped to attract increasingly large inflows of foreign direct investment from China and other Asian countries notably into the garment industry but also into infrastructure, tourism, and property. 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 diversify the sources of growth.

(2) TRADE POLICY FRAMEWORK

5. Cambodia became a member of the WTO on 13 October 2004 as the first LDC to join through the full accession process. It grants at least MFN treatment to all its trading partners. Cambodia is a beneficiary of the GSP schemes operated by developed countries. It has been a member of ASEAN since 1999.

6. The Government's trade development agenda, known as its Sector-Wide Approach (SWAp) to trade, aims to sustain growth by diversifying the country's still narrow economic base of garments and tourism. The Trade SWAp seeks to bring together activities in the trade area around a common monitoring framework. It is structured to deal with issues in three broad areas or strategic pillars: (i) reforms and cross-cutting issues for trade development (legal reforms, trade facilitation, TBT and SPS regulation and practice); (ii) product and service sector export development; and (iii) capacity building for trade development. The Trade SWAp, launched by the Government in 2008 in consultation with development partners, also serves as Cambodia's Aid-for-Trade (AfT) strategy and has served to strengthen Cambodia's ownership and management of AfT.

7. As a result of the WTO accession process, Cambodia adopted a work programme that laid out a set of legal and regulatory reforms to bring its business, investment, and trade regimes into line with international norms and provide transparency and predictability. It consists primarily of laws to achieve these goals and the subordinate legislation and administrative steps necessary to ensure their proper implementation and enforcement. Cambodia has made considerable progress by passing legislation on the general business environment, trade in goods, services, and the protection of intellectual property rights. The Government is in the process of drafting further laws and regulations to create a favourable environment for trade and investment. A commercial contract law and other important business-related laws are in draft, for example on commercial courts, e-commerce, telecommunications, and personal property leasing. Cambodia is also currently preparing a draft competition law and a law on trade remedies.

(3) TRADE POLICY DEVELOPMENTS

8. The customs tariff is Cambodia's main trade policy instrument. It is also a major source of government revenue, amounting to 16.9% of total tax revenue in 2010. Overall, trade-related taxes, comprising customs duties, VAT, and excise taxes on imports as well as export taxes and additional duties, accounted for over 56% of total tax revenue in 2010, down from almost 70% in 2004. The heavy dependence on trade-related taxes is gradually declining, reducing Cambodia's fiscal vulnerability in line with the Government's medium-term revenue strategy to progressively reduce reliance on customs revenue by strengthening the domestic tax revenue base, which remains low by regional standards, at around 8% of GDP. Regarding tariff exemptions, revenue forgone during the review period has been significantly higher than the amount of customs duties collected.

9. In reforming its tariff structure, Cambodia had reduced the number of tariff bands from 12 to 4 before joining the WTO, and the highest tariff rates of 40%, 50%, 90% and 120% were abolished. The tariff comprises four tiers: zero, 7%, 15% and 35%. The tariff rate of 35% protects several semi-processed goods and consumer goods, such as processed meat and dairy products, processed vegetables and fruits, beverages and tobacco, footwear, and motor vehicles. Over 53.4% of tariff lines are duty free or subject to the minimum 7% tariff rate, compared with 44% in 2001. A standard deviation of 9.2% in 2011 indicates that there is still some dispersion of tariff rates. The average MFN applied rate on agricultural products (WTO definition), at 14.5%, remains higher than for industrial goods (11.3%). Cambodia has an escalating tariff structure with rates rising with each stage of processing. Cambodia has reduced its overall tariff lines from around 10,700 at the time of accession to almost 8,300 in 2011, based on the HS 2007 nomenclature.

10. Cambodia has bound 100% of tariff lines. The overall average bound duty rate is 20.1% while the average applied rate of duty is 11.7%. During the review period due to various reasons, there were a number of tariff lines whose applied rates were higher than their corresponding bound rates. In February 2011, the Government approved the modification of customs duty rates on these items to comply with the committed bound rates. Other duties and charges were bound at zero.

11. Cambodia has been reforming its customs regime to streamline and improve the effectiveness of customs operations and to facilitate trade. The 2007 Customs Law prepared the way for the adoption of several regulations, *inter alia*, to fulfil commitments to ASEAN to move to the Common Effective Preferential Tariff (CEPT) scheme, to adhere to the 1999 Revised Kyoto Convention, and to implement the WTO Agreement on Customs Valuation. As of January 2011, according to the authorities, all imports comply with WTO valuation methods. Cambodia notified the WTO in 2010 that it no longer has any laws or regulations on PSI.

12. The Government has streamlined import and export procedures. As a result, the number of days required to process document for imports and exports, as well as export costs per container, have declined**.** The authorities maintain that with the introduction of the ASYCUDA system, over 90% of import declarations are cleared within 24 hours (from the filing of the goods declaration to the release of goods).

13. The 2007 prohibited and restricted goods list identifies tariff lines that are subject to import prohibition or licensing, mainly for the protection of human health, consumer interests, national security, and to protect the environment. In principle, licensing is automatic and does not restrict quantity or value of imports. Cambodia intends to comply with WTO provisions in the application of preferential and non-preferential rules of origin and is currently preparating relevant regulations, which are at an early stage of development. In 2009, with donor assistance, Cambodia began the task of drafting trade remedies legislation. The current draft, in the form of a single draft law encompassing anti-dumping and countervailing measures and safeguards, is under review by an inter-ministerial drafting group.

14. Cambodia levies export taxes on certain unprocessed raw materials and products to encourage local processing, encourage exports of finished products, and protect human health. Cambodia's export duties are applied on an MFN basis and its ASEAN partners are not exempt. Export taxes accounted for approximately 2% of the revenue collected by Customs in 2000 and less than 0.5% in 2010. Export prohibitions are maintained mainly for reasons of health, ecological balance, security, archaeological value or the maintenance of adequate domestic supply. Export permits or authorizations are required for a number of items, including processed wood products and sand. Cambodia has no export subsidies.

15. At the time of Cambodia’s accession to the WTO, 11 state-owned companies were engaged in importation and exportation of products such as rice, rubber, fertilizer, fishery products, pharmaceutical products, and agricultural equipment. Following a programme of divestment, the Green Trade Company is the only remaining state-owned enterprise involved in food import and export.

16. Cambodia is trying to increasing exports via geographically defined special economic zones (SEZs), with the goal of attracting foreign direct investment. The Government is preparing a Law on Special Economic Zones and notes that the draft law contains no export-performance measures or local-content requirements. So far, Cambodia has approved 22 SEZs, of which 14 have been established and 5 are operational, mainly in the garments, shoes, bicycles, food processing and electrical equipment industries.

17. In acceding to the WTO, Cambodia drew up an action plan to upgrade its standards, technical regulations, metrology, and conformity assessment capacity, as well as establish a TBT enquiry point. The 2007 Law on Standards of Cambodia is the legal basis for all measures related to standards and technical regulations; the authorities acknowledge that there may be a need to re-examine and revise parts the law. The 2007 law established the Institute of Standards of Cambodia (ISC), which serves as the secretariat of the National Standards Council and is responsible for developing and issuing standards. Currently, there are 71 Cambodian standards, mainly on foods, electrical appliances, and tools. Cambodia’s policy and practical approach is to adopt international standards as Cambodian standards or technical regulations where appropriate for its economic situation.

18. Cambodia's drive for full SPS compliance has been a priority during the review period. A continuing challenge for effective SPS management is the need for relevant ministries and agencies, in implementing their legal mandates, to minimize duplication, reduce unnecessary inspections, and improve reporting

mechanisms for food safety. The problem of agency duplication of functions and inspections through the proliferation of subordinate legislation may have had detrimental effects on Cambodia's SPS policy, reporting, and enforcement systems. However, the authorities contend that since the establishment of a 2010 regulation (on the Implementation of an Institutional Arrangement of Food Safety based on a farm-to-table approach), the definition of responsibilities has been clarified between the agencies involved.

19. Several ministries, agencies, and institutions are concerned with intellectual property policy and enforcement**.** In a significant step toward consolidating IPR policy-making, enforcement, and technical assistance, the Council of Ministers created the National Committee for Intellectual Property Management in 2008. It is responsible for developing national policy on intellectual property, strengthening interagency cooperation, preparing and disseminating new laws and regulations, and acting as a clearinghouse for technical assistance relating to intellectual property. Cambodia has passed or is preparing a number of laws and regulations on matters such as patents, trade marks, copyright, geographical indications, and plant variety protection. Cambodia benefits from an extended time-limit (until July 2013) for the full implementation of the TRIPS Agreement.

20. Although no legal framework relating to competition policy is in place, in 2010 the Ministry of Commerce finalized the terms of reference of a competition working group to oversee the drafting of a competition law.

(4) SECTORAL POLICY DEVELOPMENTS

21. Agriculture remains Cambodia's most important economic sector in terms of its contribution to both income and employment for most of the country's rural population, which accounts for about 85% of the total. Agricultural GDP growth averaged 5.8% per annum, in real terms, during 2004-10, but despite this relatively strong performance, its contribution to GDP has gradually declined, from 40% in the mid-1990s to around 33% in 2010, although it remains the primary source of employment for at least 70% of the population. Raising productivity in the labour-intensive agriculture sector remains a concern in Cambodia.

22. Exports of agricultural products are of little significance, according to official figures, accounting for under 6% of exports. This is due partly to supply inconsistency, difficulties in meeting SPS requirements, and poor trade-related institutional support. Most exports of Cambodian agricultural products are unofficial and are exported in a non-processed state to neighbouring countries, reflecting the very low value added of the sector. Agricultural export subsidies are bound at zero. Cambodia does not maintain or apply any export subsidies for agricultural products. Regarding domestic support, Cambodia does not use either amber box or blue box measures. Expenditures for green box measures (for 2007 and 2008) mainly took the form of payments for relief from natural disasters.

23. Under the motto "Rice – White Gold", the Government adopted a new rice policy in 2010 based on an ambitious five-year plan aimed at expanding the production and export of rice. As a result of the 'Everything but Arms' initiative, exports of milled rice to the EU have been exempt from import duties and quotas since 2009. This preferential measure, together with the removal of licence requirements for milled rice exporters, and a doubling of the Rural Development Bank capital, has helped increase exports. Given the country's recent success in achieving surplus rice production, including for export, the Government is intent on expanding its production and export capacity and becoming a major export nation.

24. The manufacturing sector, which contributed between 14% and 19% of GDP during the review period, remains heavily dependent on labour-intensive garment

production. From the mid 1990s, the manufacture of clothing, mostly for export, grew rapidly and, by 2010, 319,000 workers were engaged in the sector. The garment industry accounts for two thirds of the manufacturing sector (12% of GDP) and 80% of Cambodia's export revenue. Historically, improving labour standards and working conditions have generally helped garments exporters to maintain export contracts and stave off the competitive threat from other low-cost manufacturers in the region. However, the outlook for Cambodian garment exports is clouded by structural changes in the market and to lagging competitiveness. Unit prices for Cambodian garments continue to decrease as a result of aggressive competition, particularly from China, Viet Nam, and Bangladesh. Furthermore, growth margins in the garment industry have narrowed with the expiry, at the end of 2008, of safeguard measures imposed on China by the United States and the EU.

25. Services comprise nearly 40% of the Cambodian economy and their importance should increase as Cambodia develops, although in recent years the share of services in total output has remained stagnant. Because of the importance of tourism, one of the main drivers of Cambodian growth in the past decade, Cambodia is a net exporter of services. Tourism has emerged as a major source of foreign exchange earnings since stability returned to Cambodia; the main attraction is the Khmer archeological treasures in the Siem Reap region. Foreign visitors now number over 2.5 million per year, more than ten times the number of international arrivals in 1995. Tourism is regarded as one of the most important immediate and long-term sources of foreign exchange; it, brings in over US$1.7 billion per year and generates, directly and indirectly, employment opportunities for an estimated 300,000 people.

26. Cambodia is also keen to develop crucial infrastructure services – including financial services, telecommunications and transport – although continuing inefficiencies and shortages constrain the availability of high quality services at reasonable cost. Cambodia adopted a relatively liberal regime for trade in services as part of its accession to the WTO. It undertook market-access commitments across the broad range of services sectors, including 74 subsectors in its schedule, many with full subsector commitments, and others with partial commitments and transition periods, such as in the telecommunications sector.

(5) OUTLOOK

27. Cambodia's economic performance since 2004, together with the authorities' commitment to reform, should lead it toward sustained growth and poverty alleviation. However, with GDP per capita at an estimated US$790 in 2010, Cambodia remains a poor country. The Government targets economic growth of 6% a year and per capita income of nearly US$1,000 by 2013. Maintaining solid, broad-based economic growth and a pro-poor policy is crucial to realizing the goal of reducing the poverty rate, as targeted, to 19.5% by 2015 (from 30% in 2007), in accordance with Cambodia's Millennium Development Goals.

28. Although annual GDP growth is not expected to return to the highs of around 10% recorded before 2008, it is expected to remain strong in 2011, at around 6%, as are Cambodia's main exports, due partly to the relaxed rule of origin of the European Union on preferential tariffs for LDC exports to EU markets, which became effective on 1 January 2011. Agriculture is expected to become 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. In the longer run, the intensity of efforts to strengthen and simplify the legal and institutional framework for coherent policy making and to promote export and market diversification will largely determine the pace and sustainability of Cambodia's economic growth.