

## CHAPTER 2

# Industrial Readjustment in Cambodia

Chap Sotharith

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## **CHAPTER 2**

### **INDUSTRIAL READJUSTMENT IN CAMBODIA**

*Chap Sotharith*

#### **INTRODUCTION**

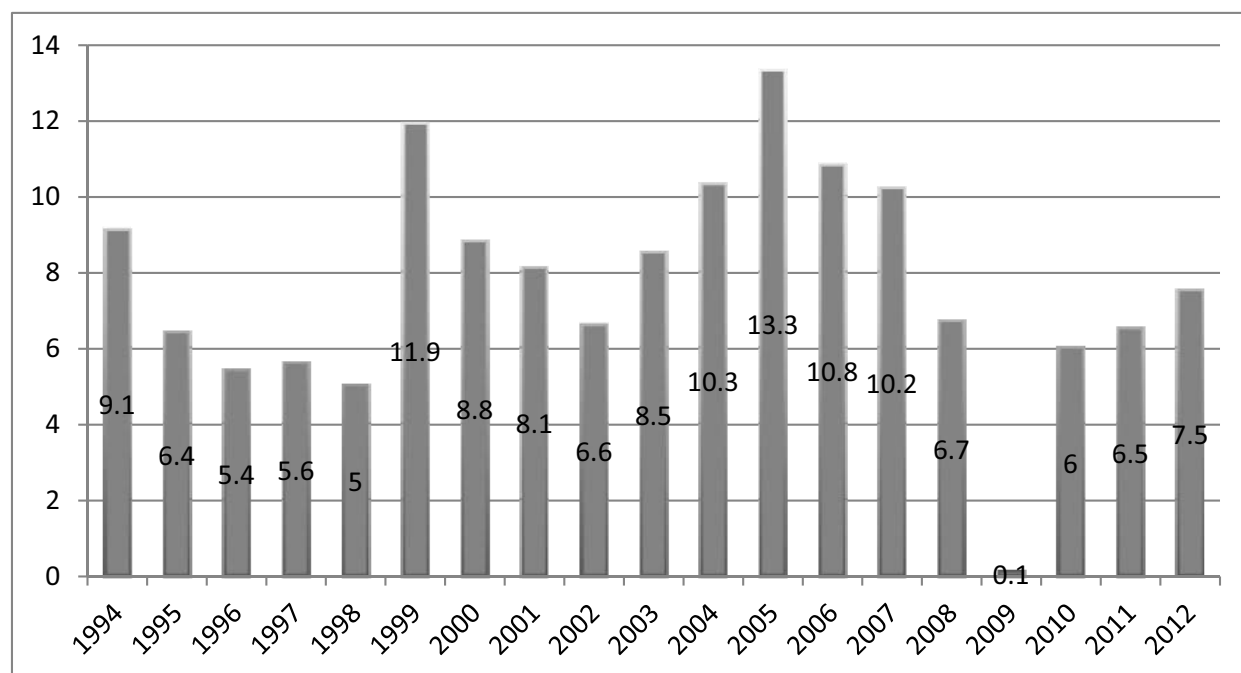
After overcoming protracted civil war and political strife, Cambodia has enjoyed national reconciliation and political stability after the general election in 1993. The country has transformed from a centrally planned economy to a free market economy. The Royal Government of the Kingdom of Cambodia has been implementing macroeconomic and structural reforms, and has achieved significant success in stabilising the macroeconomic foundation. The economy has grown rapidly since the first half of the 1990s, while inflation has been dramatically reduced.

In line with peace, stability and social order, Cambodia is now becoming increasingly integrated into the region after joining ASEAN and other regional and sub-regional mechanisms, with participation in activities including successfully hosting the ASEAN summit in 2002 in Phnom Penh. The country now as Chair of ASEAN will host the ASEAN Summit and related meetings this year. The Royal Government of Cambodia has signed trade agreements with many countries in Asia to promote access to outside markets. An important milestone in global economic integration was finally reached when Cambodia was admitted as the 148th member of

the WTO on 13 October 2004. With limited human resources and expertise in international trade, the WTO membership has imposed on Cambodia greater responsibility to adhere to strict protocols and standards. However, it has opened up tremendous opportunities for trade with the world at large on a competitive basis as well.

With an average growth of 8.4% per year from 1994-2008, Cambodia's economy is considered as one of the fastest growing in the world. However, after a double digit growth from 2004-2007, from early 2009 the Cambodian economy, had a growth of only 0.1%, as it was severely affected by the global financial crisis. During that time, the Royal Government set out a package of policies to reduce and mitigate the impacts of the Crisis on their economy (Figure 1).

**Figure 1. Cambodia Economy Growth Rate (1994-2012)**



Source: Government of Cambodia (2012 estimated by IMF).

Through the strict implementation of those policies, the Royal Government has led the Cambodian economy out of the crisis and has successfully addressed its negative impacts. The living standard of the people has been maintained as well as the macroeconomic stability, which are essential for ensuring social stability. The recovery path is “V” shaped, reflected through the following significant indicators:

First: After declining in 2009 due to the crisis, the growth rate increases to 5.5% in 2010. In 2011, the growth rate is expected to be more than 6%. In the medium term, Cambodia’s economy is projected to grow at around 6% to 7%. Inflation was around 3.5% in December 2010 over December 2009. In the medium term, inflation will continue to be low and stay below 5% although we have to be wary of spill over from regional inflation and hike in oil prices. Cambodia’s financial and banking sector remains strong and healthy; liquidity in the banking sector has increased, due to increase in credit allocation for economic activities.<sup>1</sup>

Second: Agriculture grew impressively during and after the crisis. In 2010, the sector grew by 4.5%. The paddy rice sub sector grew by 6.0% and other subsidiary crops by 8.4%. Since high priority has been given to this sector by the Royal Government, we expect that this sector will continue to grow at a fast rate in the future as well.

Third: Manufacturing and agro-industry sectors have also continued to grow. The garment sector, severely affected by the crisis, in 2009 grew by 28% in the first 11 months of 2010, generating total revenue of USD 3 billion. Reflecting the favourable impact of the rice production and export promotion policy announced in 2010, the official rice export increased by 45% in the first eleven months of 2010, over the

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<sup>1</sup> Samdach Techo Hun Sen’s Opening Speech at the 4th Cambodia Economic Forum, 16 February 2011.

corresponding period in 2009 (revenue USD 27.5 million). Investments in the food, beverage and tobacco industries have also substantially increased in response to the new policy. Fourth: The services sector remains strong. It grew by 4.6% in 2009 and 6.4% in 2010. The tourism sector has a high potential for growth. The tourist arrivals in Cambodia increased by 16% in 2010 (2.5 million tourist arrivals). In 2010, the total revenue from tourism was expected to increase by 14% (revenue USD 1.78 billion). During the post crisis period tourist arrivals in the region have continued to grow, particularly Chinese tourist arrivals.

## **1. HISTORICAL BACKGROUND**

Cambodia's economy is based mainly on agriculture. Industries have developed slowly due to many obstacles. Most of Cambodia's industrial establishments are in the form of small and medium-sized enterprises (SMEs). Industries started to develop in the 1960s after the country gained international recognition and pride. Later, the sector faced an uphill battle to survive due to war and political crises.<sup>2</sup>

The industrial sector accounted for only 5% of Cambodia's GDP in 1985, down from 19% in 1969. Industrial activity continued to be concentrated in the processing of agricultural commodities, mostly rice, fish, wood, and rubber. Manufacturing plants were small, and they employed an average of fewer than 200 workers. These plants aimed to produce enough consumer goods (soft drinks, cigarettes, and food items) and household products (soap, paper, and utensils) to satisfy local demand.<sup>3</sup>

In 1969 (or pre-war time) a census revealed 18 large industries countrywide (13

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<sup>2</sup> For more detail, see Chap (2011).

<sup>3</sup> US Library of Congress, <http://countrystudies.us/cambodia/66.htm>.

public and five public-private partnerships) and 33,000 privately owned SMEs. About half of the factories operating in 1969 were rice mills, or were engaged in rice processing.

In 1985 (post war time), 56 factories had been renovated and had been put back into operation. In the capital itself, about half of Phnom Penh's pre-war plants had reopened by 1985. Most industries were producing at far below capacity because of frequent power cuts, shortages of spare parts and raw materials, and the lack of both skilled workers and experienced managers. Industrial revival continued to be difficult and extremely slow because it was based mainly on the use of limited local resources.

In early 1986, the major industrial plants in Phnom Penh included the Tuol Kok textile factory, the largest of six textile factories in the city (however, due to power shortages the factory remained idle three days a week,). There were also four power plants, a soft drink plant, a tobacco factory, a ferro-concrete factory and some other enterprises that produced consumer goods.<sup>4</sup>

In 1989, while Vietnam launched its "Doi Moi" reforms, Cambodia also started to adopt radical reforms of its economic management system and transition from a centrally planned economy (or socialist economy) to a market-oriented one. This was initiated by the recognition of private property in real estate, the reform of state-owned enterprises and the welcoming of FDI. The reforms laid the foundation for the industrialisation of Cambodia.

Starting from 1994, the Royal Government of Cambodia began privatising small and medium-sized state-owned enterprises, especially those that did not make a profit such as public transports (trucks and buses), engineering, rice mills, soft drinks, textiles,

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<sup>4</sup> Ibid.

and wine breweries. In 2009, the Cambodia Royal Railways was transferred to an Australian company named TOLL. So far, only a few strategic enterprises remain as 100% state-owned enterprises, including international ports, electricity, and water supply. Some remain as partly state-owned, for example national airlines and air traffic control (Chap 2011).

Statistics of industry establishments vary based on different sources. There were 375,095 establishments in Cambodia as of 9 February 2009 based on the preliminary results of the Nation-Wide Establishment Listing (EL2009) implemented by the National Institute of Statistics (NIS), Ministry of Planning (Ministry of Planning 2009). The EL2009 covered all areas in the country without exception and all establishments excluding individual proprietorships which belong to Agriculture, Forestry, and Fishery industries of International Standard Industrial Classifications (ISIC) version 4 and mobile establishments.

The EL report revealed that Cambodia has 375,095 establishments and the number of establishments per 1,000 persons is 28.0, as compared to other countries viz. Japan, Indonesia and Laos had 5.9 million, 22.7 million, 209,000 establishments and 46.3, 102.3, 37.4 establishments per 1000 persons respectively. Among these four countries, Cambodia has relatively fewer establishments for its population size (Ministry of Planning 2009).

According to EL 2009 Report, the biggest province in terms of the number of establishments was Phnom Penh with 55,802 establishments or 14.9% of the total number of establishments in Cambodia, followed by Kampong Cham (43,787 or 11.7%), Kandal (38,791 or 10.3%), Takeo (27,431 or 7.3%), and Prey Veng (26,563 or 7.1%). These five provinces are located in the southern part of the country and are

plain areas, accounting for more than 50% of the total Cambodian population. The development of Phnom Penh as the capital of Cambodia can be said to contribute to a huge number of establishments, reflected in the increased number of retail shops and restaurants, etc. as well as in the construction of high-rise buildings and in the formulation of a special economic zone. In Kampong Cham, there are six large-scale industries: rubber, starchy food, animal feed, footwear, timber, and wearing apparel manufacturing. In Takeo, there are five large-scale industries: rice milling, pure drinking water, wearing apparel, brick producing, and water supply. In addition, construction material is a huge industry. In Prey Veng, wearing apparel is a large-scale industry.

Meanwhile, the smallest province was Kep with 789 establishments or 0.2% of the nation's total number of establishment, perhaps reflecting the fact that its area is the smallest amongst all provinces, followed by Mondul Kiri (1,637 or 0.4%), Pailin (1,904 or 0.5%), Stung Treng (2,656 or 0.7%), and Oddar Meanchey (3,683 or 1.0%). These five provinces are located in the northern or eastern part of the country except Kep. Although Kep was the smallest, there are three large-scale industries: hotel, salt producing, and fish sauces. In Pailin, there were five large-scale industries: casinos, guesthouses, restaurants, quarrying, and selling construction materials. In addition, electricity supply is a huge industry. However, the number of casinos, guesthouses, and restaurants are decreasing (Ministry of Planning 2009).



**Table 1. Brief Finding in National Wide Listing of Enterprises in Cambodia.**

Number of Provinces	24
Number of Districts	185
Number of Communes	1,621
Number of Villages	14,066
Number of Establishments	375,095
Number of Establishments per km <sup>2</sup>	2.1
Number of Establishments per 1,000 Persons	28.0
Population per Establishment	35.7
Number of Establishments per 1,000 Households	132.4
Number of Households per Establishment	7.6

*Source:* National Institute of Statistics.

In 2010, according to the Ministry of Industry, Mine and Energy's Annual Report (2010), there 74 new factories were established creating 51,723 new jobs. The total number of factories registered by MINE in 2010 was 599 factories (MIME 2011). The report showed that there were 37,422 SMEs with an increase of 5.24% when compared with 2009. The value of SMEs production was Riel 3,951,397 million (USD 987 million) with an increase of 23.52%.

## **2. INDUSTRIAL READJUSTMENT**

### **2.1. Industrial Development**

Cambodia has experienced rapid industrial growth with a double digit growth in some years between 2000 and 2008. Even though the sector declined drastically, due to the global and regional financial crises in 2009, it started to bounce back quickly. Compared to other sectors, the industrial sector recorded its highest development rate at around 9% from 2011 to 2013. The most promising sectors are garment and

manufacturing. The growth rate is shown in Table 2 (RGC 2012).

**Table 2. Growth Rate of GDP by Economic Activities (Constant Price of 2000, %)**

	2011	2012	2013	2014
<b>Agriculture</b>	<b>4.1</b>	<b>4.2</b>	<b>3.8</b>	<b>3.7</b>
Crop	4.1	4.4	4.3	4.2
Animal Raising	5.0	4.9	5.0	5.0
Fisheries	4.3	3.9	2.4	2.4
Forestry	1.1	1.1	1.1	1.1
<b>Industry</b>	<b>9.2</b>	<b>9.4</b>	<b>9.8</b>	<b>9.3</b>
Mining	8.5	7.3	8.8	8.9
Manufacturing	9.9	9.6	10.0	9.2
Garment and Textiles	11.6	11.2	11.2	10.0
Wood Paper and Printing	1.6	2.2	3.5	3.6
Rubber	8.8	8.3	9.7	9.9
Other Productions	5.6	4.4	6.2	6.3
Electricity Gas and Water	6.5	6.6	7.6	7.7
Construction	6.7	9.3	10.1	10.2
<b>Services</b>	<b>5.7</b>	<b>5.7</b>	<b>7.1</b>	<b>7.3</b>
Trade	5.8	4.9	6.3	6.4
Hotel & Restaurant	10.7	9.4	9.4	9.5
Transport & Telecommunication	4.2	4.4	5.8	5.9
Finances	7.9	7.8	8.5	8.6
Public Administration	4.6	4.0	3.9	4.0
Real Estates	5.1	5.9	8.2	8.2
Other Services	4.3	4.9	7.0	7.4
Tax on Production less subsidies	3.6	9.1	6.6	8.2
Subsidies	40.3	9.1	6.6	8.2
Financial Service Charge	13.9	7.8	8.5	8.6
<b>Gross Domestic Product (GDP)</b>	<b>6.0</b>	<b>6.5</b>	<b>7.0</b>	<b>7.0</b>

*Source:* Royal Government of Cambodia (2012).

## 2.2. Industry Development Policy in Cambodia

Cambodia industrial policy was developed in a “Top Down” Approach (Figure 2). In a democratic regime, Cambodia leadership started to formulate its policy framework from Party Political Platform 2004. In 2003 General Election, Cambodia People Party won a landslide victory and it was possible that the CPP could lead the Government

alone. However, in order to strengthen the Government, FUNCINPEC party was invited to join the coalition.

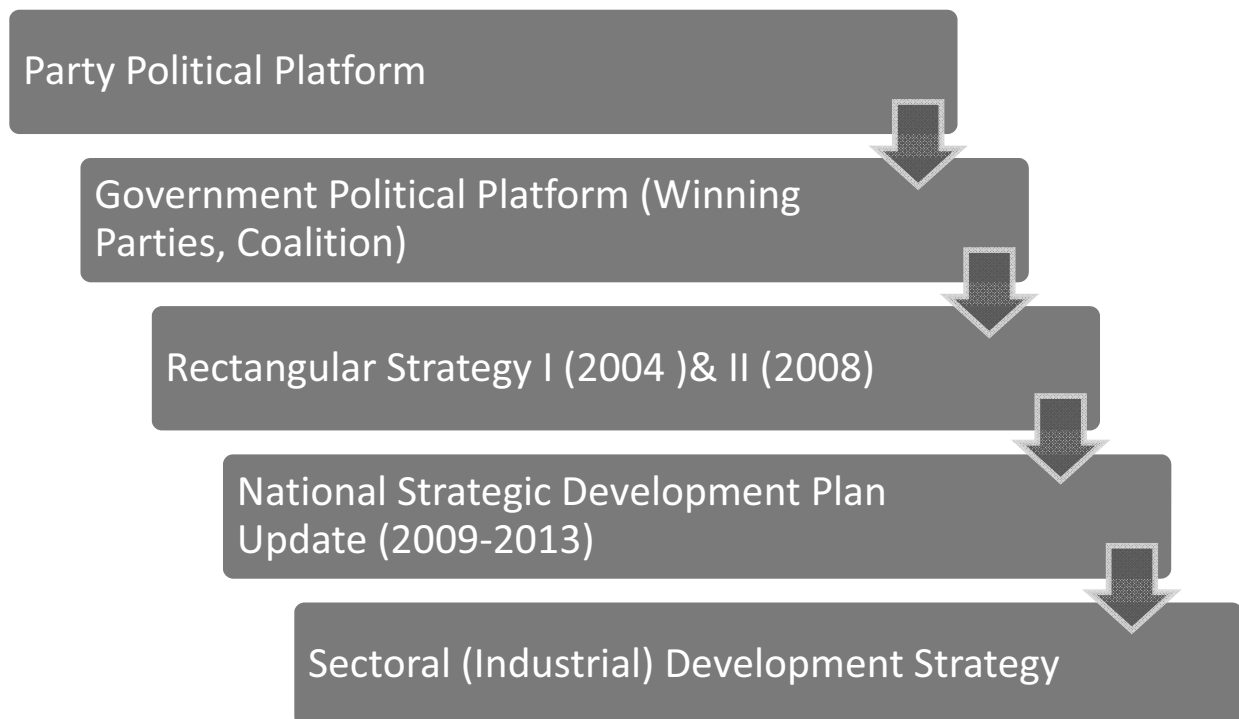
In 2004, a 73 point Political Platform was reached by ruling political parties of Cambodia (a coalition of CPP and FUNCINPEC). In the Platform, industrial development policy was illustrated from Point 40 to Point 44. A key strategy of the industrial policy is to expand the economic interaction between agriculture and industry by promoting agro-industry into an essential core of Cambodian industry in order to improve the industrial structure so that it will not rely too much on textiles (Point 40).<sup>5</sup> In this regard, the Royal Government will encourage processing industries that provide an opportunity to use Cambodian comparative advantage to compete on regional and international markets, especially in industries that process natural agricultural products and in laborintensive industries. Toward this goal, the Royal Government will continue to aim at improving the investment environment, increasing technology transfer, and increasing professionalism training, including by establishing industrial zones and export processing zones supplied with quality physical infrastructure and services, establishing national standards institutions and national laboratories, and strengthening the legal framework in order to ensure efficiency and transparency in the enforcement of laws and regulations. The Royal Government will review the draft of the Law on Industrial Zones, considering points related to the enforcement of labor law in that area. The Royal Government will continue to prioritize promotion of non-metal mining, which includes limestone, clay, and kaolin and which can supply raw materials to cement, tile, ceramic, and brick factories; the processed timber and timber products industry; electronics assembly; machine

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<sup>5</sup> Royal Government of Cambodia (2004) The 73 Point Political Platform.

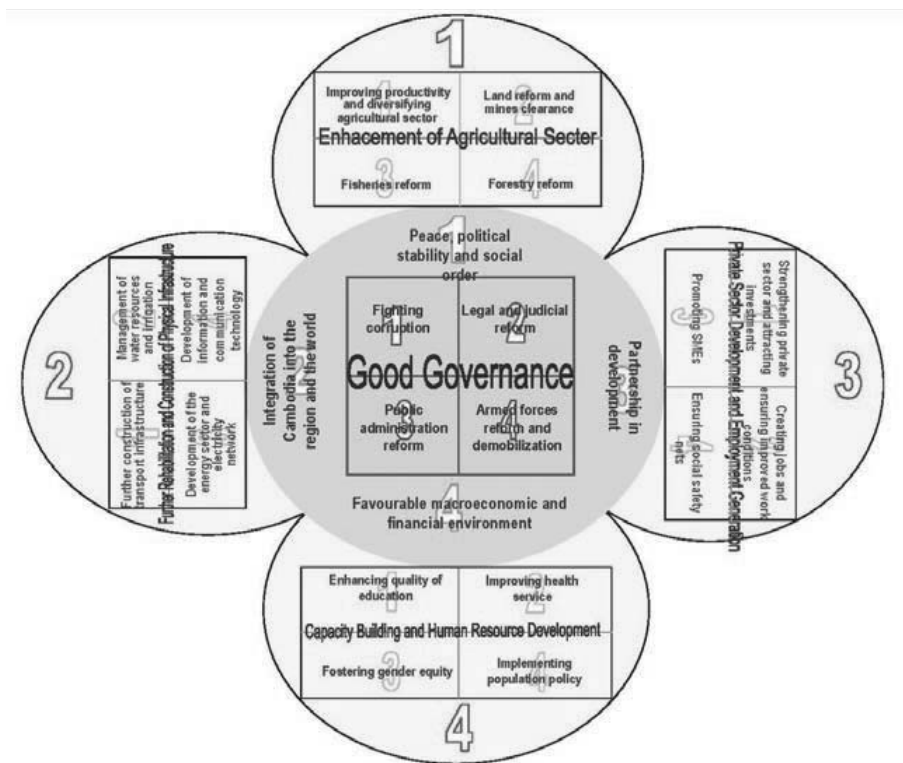
processing of fish and meat; and factories that process other farm products such as hemp, tobacco, cashew nuts, coffee, palm oil, rubber, sugar cane, potatoes, fruits and vegetables, etc Point 43 of the Political Platform further illustrated that in order to achieve these priorities, the Royal Government will continue to encourage investment by focusing on resolving governance problems, facilitating administrative procedures, and reducing the number of inspections. Special attention will be given to promoting small and medium industry as well as domestic industry so that this field is capable of producing some products to meet domestic demand instead of imports, especially to serve the tourism market, and in the future these products may be exported. These factors also require the implementation of programs to increase the quality of professional training and tertiary education by uniting theory with practice and real production activities, as well as programs targeted at growing a spirit of entrepreneurship and practical competence in learners so that they know how to start a business, farm, or enterprise, and this will create employment for citizens. The Royal Government will strengthen enforcement of the Law on Social Security and the Labor Law within the industrial zones. Point 44 stipulated that the Royal Government will continue to encourage research and exploration into petroleum and gas so that this field can contribute to national economic growth and development according to Cambodia's potential. At the same time, the Royal Government will try to solve the problem of overlapping maritime boundaries as soon as possible in order to protect national sovereignty and territorial integrity.

**Figure 2. How Industrial Development Strategy Formulated**



In 2004, the Rectangular Strategy initiated by Prime Minister Hun Sen with its motto “For Growth, Employment, Equity and Efficiency” was launched (Figure 3). According to the Strategy, the Royal Government of Cambodia has laid out ambitious goals. First, Cambodia has to ensure sustainable economic growth of around 7% per year on broader and more competitive economic basis. Second poverty incidence should be reduced at the rate of more than 1% per annum. In order to achieve these goals, Cambodia has to promote industrial development. The Strategy was the foundation of National Strategic Development Plan, which included the industrial development policy (Rectangular 2 and 3).

**Figure 3. Rectangular Strategy**



Industrial development is promoted by the investment policy of the Royal Government of Cambodia. The policy encourages local production and international trade by opening the free market to all investors and partnerships to invest in the country without any discrimination or restriction. The condition being that land ownership belongs to natural persons holding Cambodian citizenship or by legal entities in which more than 51% of the equity capital is directly held by natural persons or legal entities with Cambodian citizenship.

In the Rectangular Strategy for Growth, Employment, Equity and Efficiency, the Royal Government of Cambodia has laid out ambitious goals. First, Cambodia has to ensure sustainable economic growth of around 7% per year on a broader and more competitive economic basis. Second, poverty incidence should be reduced at the rate of

more than 1% per annum. In order to achieve these goals, Cambodia has to promote industrial development.

Following the implementation of favourable policies for trade development and foreign direct investment (FDI), the Cambodian industry has grown rapidly. Manufacturing in Cambodia in the past was carried out mostly on a very small scale, where food processing, brick making and timber processing were the main activities. Cambodia, nevertheless, went through a great deal of structural changes in the past decade or so after declaring a market economy (JICA 2002:45).

The Royal Government of Cambodia has indentified the energy sector as a priority in the current National Strategic Development Plan (NSDP). Oil and gas development, has the potential to improve domestic social and economic development by increasing job opportunities and incomes which contribute to poverty reduction and more importantly help to improve the well-being of Cambodians.

The key strategy of the Royal Government of Cambodia is to increase the economic linkage between agriculture and industry, with its industry policies, to improve the industrial sector and lessen its dependence on the only prime sector, the textile industry. The government continues to provide the necessary physical infrastructure and highly qualified support services to enhance the investment climate, promote transfer of technology, increase professional training, and establish industrial zones or special economic zones (SEZs). The legal framework is also being strengthened to ensure efficiency and transparency in the implementation of laws and regulations.

Along with rebuilding the country from the ground zero up, Cambodia also commenced rebuilding its economy in defence against the return of the Khmer Rouge

regime. The following is a chronological outline of the changes in Cambodia's industrialisation:

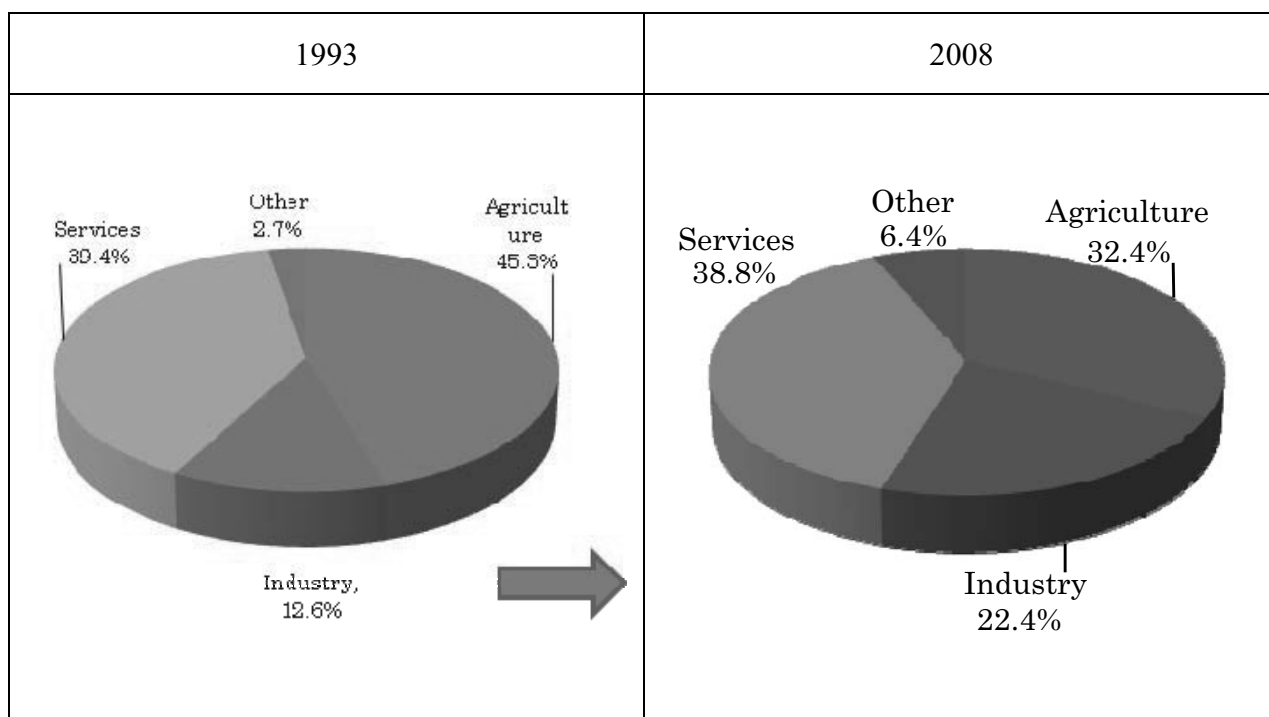
- (i) Starting from 1989: Radical reform was launched to accept private ownership of land and real estate. Privatisation and acquisition of state-owned enterprises was introduced and FDI was openly welcomed.
- (ii) Starting from 1993: There was a complete changeover from a centrally planned economy to a market economy. The economy became highly dependent on the external assistance provided by international aid agencies.
- (iii) After 1995: The economy showed a steep growth led by labour-intensive industries, especially garment manufacturing and tourism-related industries.
- (iv) After 1997: The economy was affected by political unrest and the fallout from the Asian financial crisis. However, Cambodia could overcome this with positive growth, and the industry in the country survived mainly due to a strong demand in the garment sector.
- (v) After 1999: Integration into the regional economy took place by its admission to ASEAN. FDI in the manufacturing sector started to flow in.
- (vi) After 2003: Integration into global trade took place by its admission to the WTO. The garment sector still dominated the industry and Cambodia's trade continued to grow rapidly.

Industrialisation in Cambodia has been achieved through several changes in economic policies, especially the reform from a centrally planned economy to a free market economy in 1993.

Since 1993, industries have grown rapidly due to attractive FDI policies, As a result, the GDP grew from 12.6% in 1993 to 22.4% in 2008 (Figure 4).



**Figure 4. Changing in Industrial Structure 1993-2008**



Source: Chap (2011).

The outward-oriented industrial development strategy is given priority for four reasons. First, the small size of the domestic market in terms of population and purchasing power limits the opportunities for efficient production. Second, Cambodia does not have sufficient financial resources or managerial expertise to fully utilize its natural resource base. Third, access to technological innovations that underpin increased efficiency and wider consumer choice can only come from integration with regional and global economies. Fourth, no country has a comparative advantage in producing everything, and all countries can therefore benefit from cooperating and trading with others (Sau 2007).

### **2.3. Industrial Development Action Plan (1998-2003)**

The Industrial Development Action Plan (1998-2003) of the Royal Government of

Cambodia has two goals: the development of export-oriented industries, and the development of import-substituting production of selected consumer goods. These goals are to be achieved by promoting: (i) labour-intensive industries, (ii) natural resource-based industries, (iii) SMEs, (iv) agro-industries, (v) technology transfer and upgrading the quality of industrial products, (vi) establishment of industrial zones, and (vii) development of import-substituting production of selected consumer goods (MIME 1997).

#### **2.4. The Strategic Framework of the General Department of Industry 2010-2015**

The General Department of Industry (GDI) drafted a concept paper called “The Strategic Framework of the General Department of Industry 2010-2015” to list the performance of the industry sector , challenges ahead, vision and strategic agenda, and core areas of intervention and the transformation of GDI by 2015 (Meng 2010).

The concept paper was prepared for the internal use of the General Department and it has not yet been adopted as the Government’s Strategy. It indicated that GDI, as a leading authority of the Ministry of Industry Mines and Energy, responsible for the industry sector, has a core mandate to implement the RGC’s Development Policy and Strategy in the industry and SME sectors, articulated in the Rectangular Strategy Phase II. Under this policy and strategy, poverty reduction is one of the most important objectives of the RGC. To contribute to achieving this objective, GDI plays a very important role in driving the development of a dynamic industry sector promoting efficiency, equity, employment and growth. Therefore, in recognition of this role, GDI’s corporate vision under Strategy 2015 will be “A highly productive Cambodia with better competitiveness” and its mission will be to enable

enterprise development in the productive sector in Cambodia (Meng 2010:3).

In pursuing this vision, GDI will focus all its activities and operation on two key strategic plans for industry sector development: (i) Cambodia's comparative advantages and human development with industry growth, and (ii) eco-friendly and socially responsible industry growth.

### **3. CHALLENGES IN INDUSTRIAL READJUSTMENT**

#### **3.1. Lack of Long Term Strategic Plan in Industrialisation**

Cambodia only has the Industrial Development Action Plan (1998-2003) for implementation of industrial policy. This document is considered outdated and a new strategic plan should be formulated. Therefore, it can be concluded that the country has not yet formulated a long-term strategic plan for industrialisation consisting of vision, industrial readjustment and addressing issues such as good governance in various sub-sectors such as industrial diversification, industrial standards, energy and electrification, mining, oil and gas management, supporting SMEs, industrial zonings and others.

So far, there are several government agencies involved in long term planning of industry development namely, Ministry of Industry, Mines and Energy, Ministry of Planning, Supreme National Economic Council (SNEC), and Council for Development of Cambodia.

#### **3.2. Development of Special Economic Zones**

Special Economic Zones are very important for industrial development. Due to a high

demand of industrial establishments, the Cambodian government has approved a total of 21 SEZs, located along the border with Thailand and Vietnam (Koh Kong, Poipet, Bavet, and Phnom Den), at Sihanoukville, and at Phnom Penh. Of the 21 zones, six have commenced operations (Table 3). Aiming to attract more investors, the SEZs offer a one-stop service for imports and exports, with government officials stationed on-site providing administrative services. Applications to establish factories within the SEZs are dealt with on-site, as all require administrative clearances and permits.<sup>6</sup>

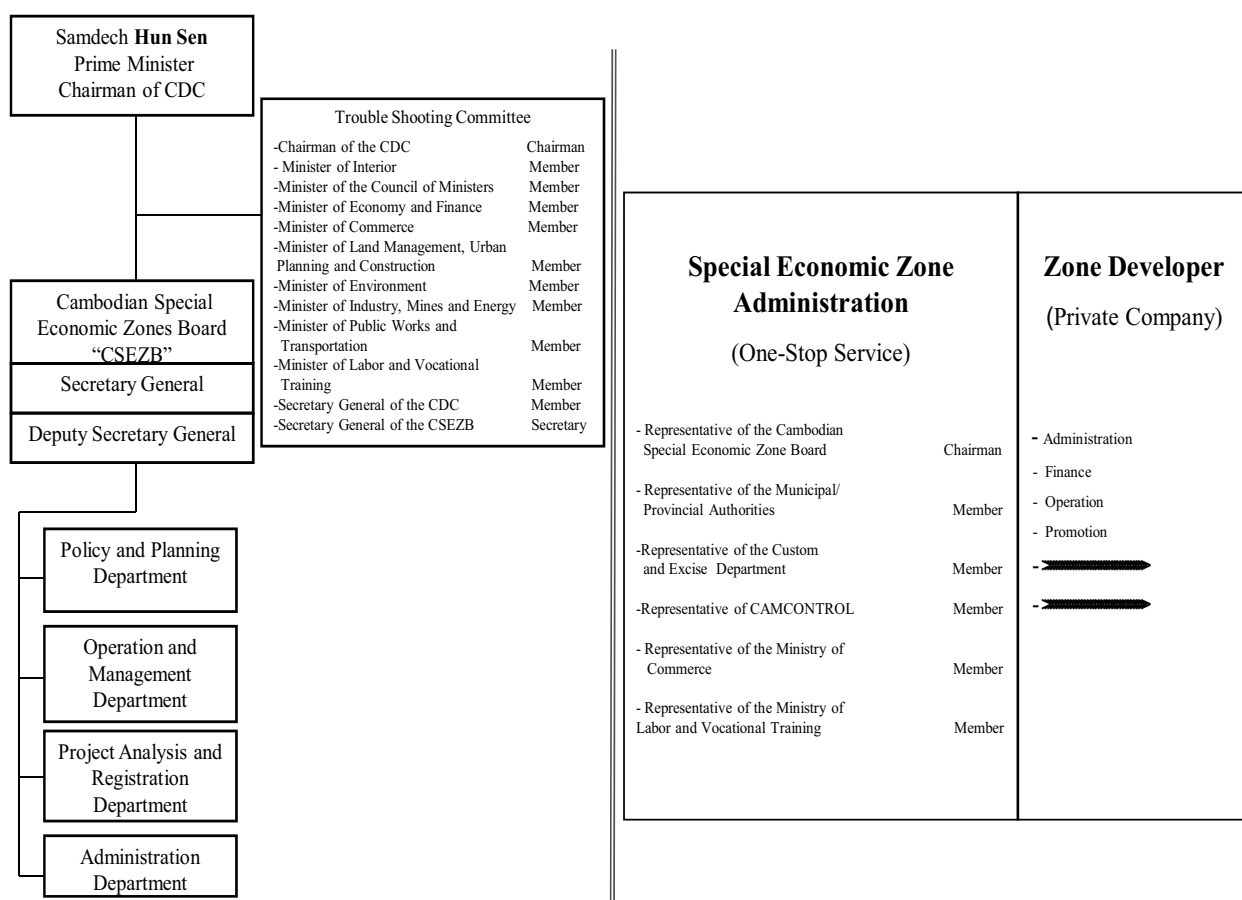
To date, only about 30% of the total SEZs listed in table 2 are operational or partly in operation (Chap 2011).

There are many challenges for SEZ development in Cambodia. The challenges include land speculation, lack of funding and lack of technical expertise. Some of the investors or agents, after receiving licenses, are very slow in implementation due to several reasons such as land speculation and lack of fund. Some SEZs, especially those developed by some local companies, were poorly planned without proper roads, sewage system and waste disposal facilities. Though the owners invested very little (just dirt roads and divided plots of land), they sold or rented the land at very high prices. According to the interview, it was found that the SEZs are not provided with special incentives such as tax or VAT incentives.

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<sup>6</sup> <http://www.investincambodia.com/default.htm>.

**Figure 5. Management Structure of CDC and at Each SEZ**



Source: Council for Development of Cambodia (CDC).

**Table 3. List of Special Economic Zones in Cambodia**

No.	Name	Locations	Area (ha)	Ownership	Capital (\$ mil)	Status
1	Koh Kong SEZ	Koh Kong	336	Mr. Ly Yong Phat (Cambodian)	n/a	Licensed in 2002, Operational
2	Suoy Chheng SEZ	Koh Kong	100	Mrs. Kao Suoy Chheng (Cambodian)	14	Licensed in 2002. Not yet operational
3	N.C SEZ	Koh Kong	150	Mr. Kong Triv (Cambodian)	14	Licensed in 2002. Not yet operational
4	Stung Hav SEZ	Sihanoukville	192	Ms. Lim Chhiv Ho (Cambodian)	14	Licensed in 2002. Not yet operational
5	N.L.C SEZ	Sray Rieng	105	Ms. Leang Vouch Chheng (Cambodian)	13	Licensed in 2005. Not yet operational
6	Manhattan (Svay Rieng) SEZ	Sray Rieng	571	Mr. Clement Yang (Taiwan)	15	Licensed in 2005. Operational
7	Poipet O'Neang SEZ	Banteay Meanchey	467	Mrs. Van Ny (Cambodian)	15	Licensed in 2005. Operational
8	Doung Chhiv Phnom Den SEZ	Takeo	79	Mr. Doung Chhiv (Cambodian)	28	Licensed in 2006. Not yet operational
9	Phnom Penh SEZ	Phnom Penh	350	Ms. Lim Chhiv Ho (Cambodian)	68	Licensed in 2006. Operational
10	Kampot SEZ	Kampot	145	Mr. Vinh Huor (Cambodian)	15	Licensed in 2006. Not yet operational
11	Sihanoukville SEZ 1	Sihanoukville	178	Mr. Lav Meng Khin (Cambodia)	100	Licensed in 2006. Not yet operational
12	Tai Seng Bavet SEZ	Svay Rieng	99	Mr. Ly Hong Shin (Cambodian)	37	Licensed in 2007. Operational
13	Oknha Mong SEZ	Koh Kong	100	Mr. Mong Rithy (Cambodian)	40	Licensed in 2007. Not yet operational
14	Goldfame Pak Shun SEZ	Kandal	80	Mr. Chan Ji Kvong (Korean)	34	Licensed in 2007. Operational
15	Thary Kampong Cham SEZ	Kompong Cham	142	Chhorn Thary (Cambodian)	69	Licensed in 2007. Operational
16	Sihanoukville SEZ 2	Sihanoukville	1688	Mr. Lav Meng Khin (Cambodian)	n/a	Licensed in 2007. Operational
17	D&M Bavet SEZ	Svay Rieng	117	Ms. Men Pheakdey (Cambodian)	52	Licensed in 2007. Not yet operational
18	Kiri Sakor Koh Kong SEZ	Koh Kong	1750	Mr. Ly Yong Phat (Cambodia)	110	Licensed in 2008. Not yet operational
19	Sihanoukville Port SEZ	Sihanoukville	70	Mr. Lu Kim Chhun (Cambodian)	34	Government owned. Licensed in 2008. Not yet operational
20	Kampong Saom SEZ	Sihanoukville	255	Mr. Kith Meng (Cambodian)	190	Licensed in 2009. Not yet operational
21	Pacific SEZ	Svay Rieng	107	Mr. Chea Eavmeng, Mr. Gau Hieckhuor, Mrs. Yin Phanny	70	Licensed in 2009. Not yet operational

Source: [http://www.investincambodia.com/economic\\_zones/sezs.htm](http://www.investincambodia.com/economic_zones/sezs.htm), accessed on 07 July 2010.

### 3.3. Lack of Energy and High Price of Electricity

Industrialisation cannot be successfully achieved without building a good source of energy and provision of an affordable and reliable electricity supply is critical for the

future of business in Cambodia. Reliable, affordable electricity is a prerequisite to economic success and the welfare of the people. Without it, businesses have two choices: buy a generator or shutdown production every time there is a power cut. At present, the sale of generators in Cambodia is a thriving business.

In order to develop the energy sector, significant progress has been made in increasing the available supply of electricity and the expansion of the electricity network. The Energy Sector Development Plan 2005-2024 has been prepared (MIME 2009) for developing the energy sector for meeting the increased demand of households and industrial establishments.

Lack of energy and high price of electricity is one of the main challenges for industrial development and readjustment. At present, only 12.30% of the rural population or about 15% of the country's 14 million people have access to electricity.<sup>7</sup>

Cambodia's power sector was rehabilitated since 1995 under the State-owned Electricite du Cambodge (EDC). EDC's capacity output in 2007 was only 194.8 MW and 1,071 GWh. It is estimated that in 2024 Cambodia would need 3,045.33 MW and 16,244.61 GWh of electricity. The annual energy consumption per capita of Cambodia is 103 kWh. Though the country has a huge potential for generating electric power from many hydro sources, of more than 10,000 MW, it has not yet utilized all of these resources. The country has only 22 small isolated power generators with a few small and medium sized hydro-electric dams. Big hydro electric dams are under construction and feasibility study. The supply of electricity can only meet about 50% of the demand, especially in provinces and rural areas.

Phnom Penh, which accounts for 85% of Cambodia's electricity consumption, will

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<sup>7</sup> Minister of Industry, Mine and Energy, Suy Sem's Speech on 23 March 2011, in MIME (2011).

be at the heart of the proposed grid. The grid will be connected to western Cambodia by 2012 to supply electricity to Siem Reap, Battambang and Banteay Meanchey.<sup>8</sup> National electricity consumption has increased by 12% per year and consumption in Phnom Penh has risen by 20% annually.

So far, industrial development in Cambodia is facing constraints from the high price of electricity and lack of electricity supply in many parts of the country. Electricity is only available in the capital and provincial towns. In order to “top up” the supply, Cambodia has imported electricity from Thailand Laos and Vietnam. In most areas, especially remote rural areas, people use diesel generators, car batteries, kerosene lamps, and candles.<sup>9</sup>

The average price of electricity in Cambodia is USD 0.18 per kilowatt/hour, and prices are as high as USD 0.90 per kilowatt/hour in remote rural areas compared to around 5.4 cents per kilowatt in Vietnam. Therefore, electricity prices in Cambodia are considered as the highest in the ASEAN region. The price of power is a major deterrent to foreign investors and undermines Cambodia’s ability to compete with neighbouring countries such as Thailand and Vietnam.<sup>10</sup>

Unreliable electricity supply and high energy costs remain a major concern for businesses in Phnom Penh, where power outages are increasingly frequent in most areas of the city. The estimated current capacity for power production for the city was 190 megawatts; however, the demand is around 230 megawatts. The supplier solves this problem by cutting off the electricity supply to some areas on the outskirts of the

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<sup>8</sup> Web of Cambodia “Power Plan Development in Cambodia,” at [http://www.web-cambodia.com/en/article/Power\\_Plans\\_Development\\_in\\_Cambodia-36047.html](http://www.web-cambodia.com/en/article/Power_Plans_Development_in_Cambodia-36047.html) accessed on 30 December 2011.

<sup>9</sup> <http://www.investincambodia.com/power.htm>.

<sup>10</sup> <http://www.investincambodia.com/power.htm>.



city for one or two hours a day, which naturally causes problems for consumers.

In 2009 however, the city's shortage of electricity could ease when the municipality begins purchasing 200 megawatts of extra power from Vietnam. The electricity will be imported via a new power line running from Vietnam through Svay Rieng and Kandal provinces to Phnom Penh.

As Cambodia has just started to build the national grid, many provincial towns and cities still use their own power generation plants and distribution networks, with little interconnection. The power plants are small and are mainly fuelled by imported diesel, and this is reflected in the prices.

Cambodia has imported electricity from Vietnam at high voltage 220 kV with a capacity of 200 MW in 2009. The country also imported from Thailand at 115 kV starting November 2007 for the northern grid up to 80 MW. Cambodia also imported electricity from Lao to Stung Treng Province at 115 kV with a capacity of up to 20 MW in 2011. With the ADB assistance, Cambodia, Lao PDR and Vietnam will have a power Interconnection at high voltage 500 kV, by 2018.

In order to supply electricity to provinces and rural areas, Cambodia has implemented projects of provincial and rural electrification. So far, the Royal Government has completed the rehabilitation of 8 provincial towns supported by ADB (USD 18.6 million) and AFD (€3.75 million), grid extension & rural electrification program with the assistance of SDR27.9 million from the World Bank and USD 5.75 million from GEF, and renewable energy master plan study and 2 micro hydro development by JICA.

Rural Electrification includes the following targets:

- 100% of the villages will have access to electricity services by 2020

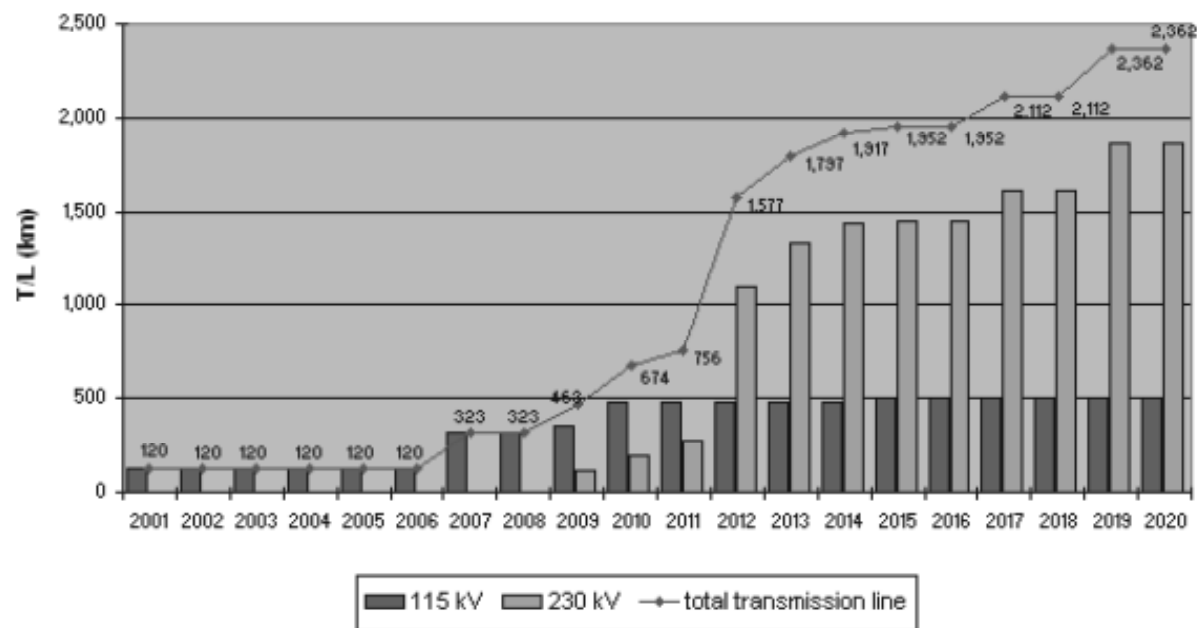
- 70% of the rural population will have access to quality electricity services by 2030.

Although significant progress has been made, the energy sector also faces many daunting challenges, which include:

- How to ensure efficiency and sustainability of production, supply, and proper maintenance in the power infrastructure across the whole country.
- How to lower the current high cost of electricity generation not only to support private sector development but also to make it affordable for the poor.
- How to attract private sector investment and participation to expand the power infrastructure and meet the growing demand for electricity, particularly in the rural communities.

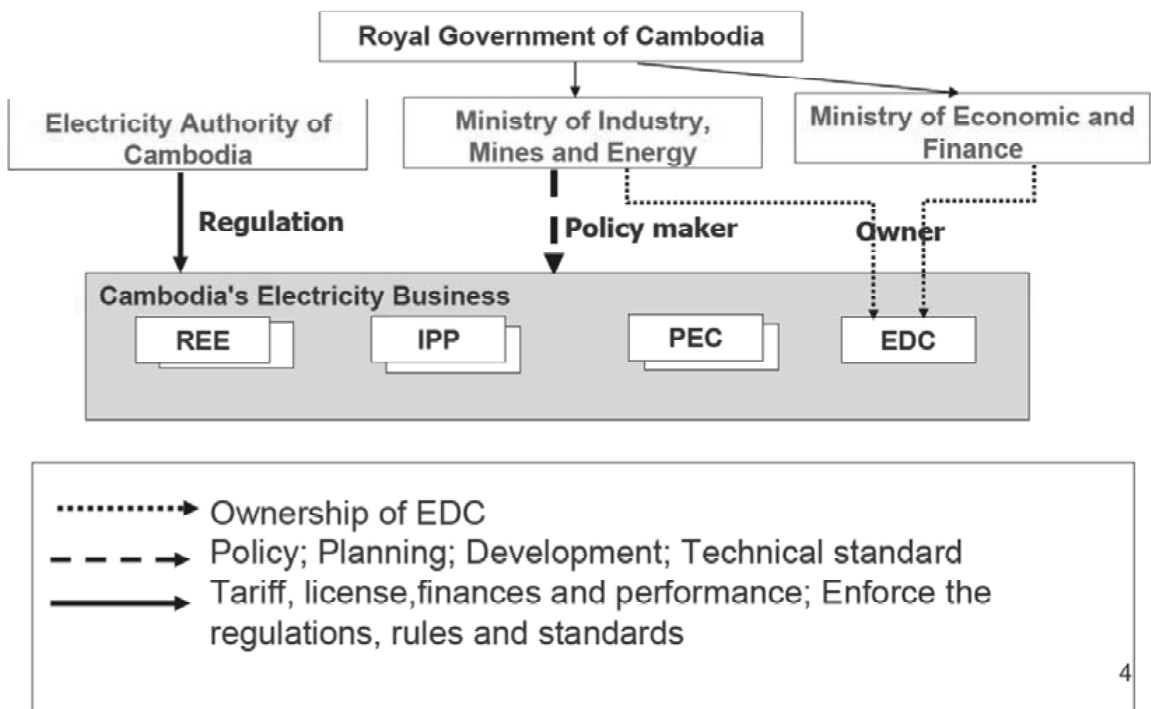
The lack of rural and provincial electricity is a bottleneck for industrial development, especially in reducing development gaps in various regions in Cambodia.

Figure 6. Transmission Expansion Plan (2001-2020)



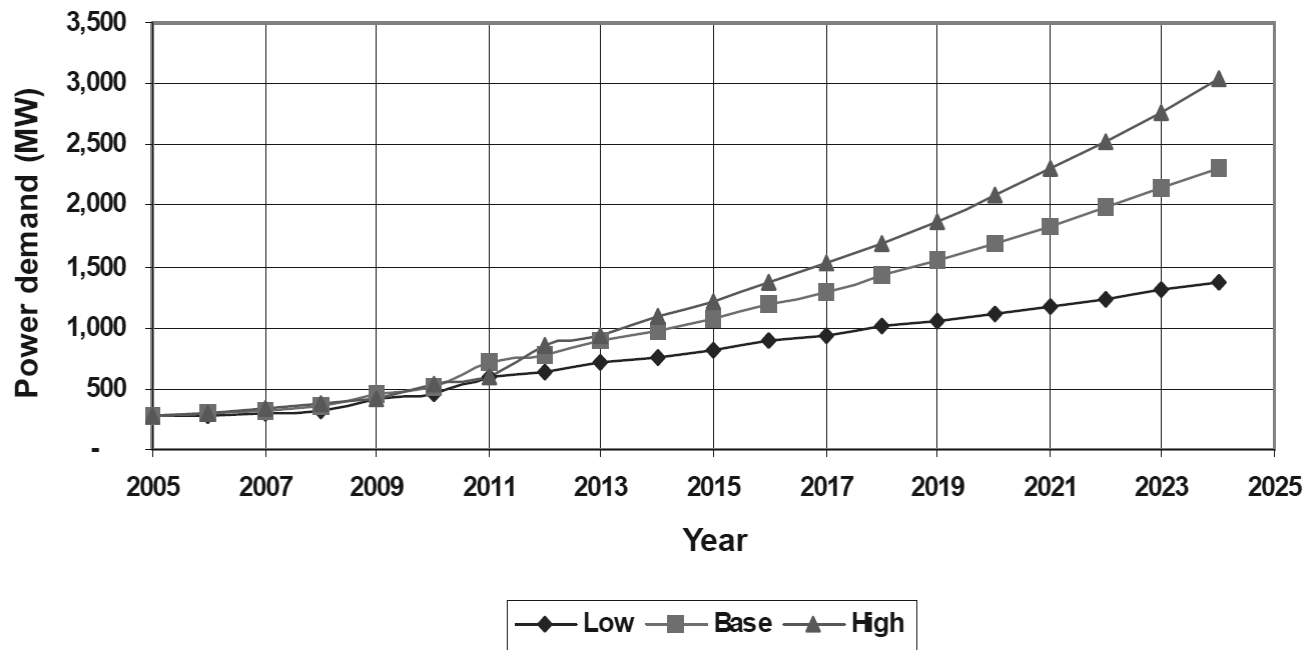
Source: Ministry of Industry, Mine and Energy.

Figure 7. Current Structure of Electricity Sector



Source: Ministry of Industry, Mine and Energy.

**Figure 8. Power Demand in Cambodia**



*Source:* Ministry of Industry, Mine and Energy.

### **3.4. Management in Extractive Industries**

For mineral resources, Cambodia offers one of the few under-explored (greenfields) areas in the world. Since the beginning of the decade, the interest in Cambodian mineral exploration has grown substantially, in particular, from international investors from Australian, China, South Korea and Vietnam. The country’s mineral resources represent a natural asset that can be transformed into the source of substantial new wealth and that can improve the quality of life for all Cambodians by generating well-paying and skilled employment, both directly and indirectly through spin-off industries.

At present, the Ministry of Industry, Mine and Energy has issued 77 licenses for mining exploration and extracting (MIME 2011). The mining industries have been subjected to complaints and criticism from environmentalists and local people as it affects the environment and their livelihood. Many investors are slow in starting their

exploration due to several reasons such as speculation and lack of funding.

The management of the extractive industry is facing challenges such as lack of laws and regulations related to mining and extracting industries, limited human resources and technical know-how to manage and control the sector.

According to an interview, it is found that the sector is facing difficulties due to unclear policies on management of mineral resources and on production and export of mineral ores. According to the Government's policy, export of mineral ores is not allowed. The Government has encouraged the establishment of factories to process mining products such as iron, gold, aluminium and others mineral products. Some investors faced difficulty in exporting primary ores due to restriction from the Government. They complained that it was very difficult to build factories in the country because it is very risky that though they have invested a lot of money in exploration they may find that the volume of mineral ores is insufficient to supply to the processing factories. On the other hand, the cost of building a factory is very high and the factory may face shortage of raw materials. Not to mention other obstacles such as lack of electricity and lack of access roads and other public facilities and infrastructure.

### **3.5. Small and Medium Enterprise Development**

SME is the core of industrial development. In recent past decades, the SME sector enjoyed a strong and high growth and prosperity and contributed to a high growth rate of the economy. However, with the global crisis in 2008-2009, the sector is severely affected.

The SME Development in Cambodia is facing many challenges. In regard to the

regulatory and legal framework, the first key area is the need for streamlining and reducing the cost of company registration. Currently, this represents one of the highest cost and time expenditures in the region. A second priority, is establishing a regulatory review process and a recourse mechanism. This would focus on the numerous and overlapping licenses issued by most ministries, a situation that imposes a severe burden on SMEs. Third, the need for establishing a commercial legal framework is highlighted as an important part of the strategy. As of mid-2005, the commercial legal framework remained incomplete.

The second key area in the strategy is improving access to finance. Access to finance is a critical issue for all businesses and remains a problem particularly for SMEs. Among the other issues the strategy addresses: (i) collateral and land titling, (ii) leasing, (iii) credit information sharing, (iv) simplified accounting for SMEs, and (v) non-bank financial institutions. Addressing these issues is seen as critical for improving SME access to credit.

Finally, the third key area is improving support activities for SMEs. In the delivery of support services, there is a role for the government to play in addition to that played by the private sector. Where public goods and services are involved or there is market failure, the government should take the initiative, either by itself or in partnership with the private sector. Where private sector Business Development Services (BDS) markets do not exist, the Inter-Ministerial SME Sub-Committee has a role to work with donors and business associations to stimulate demand and develop private sector supply. In particular, support activities should focus on improving access to markets, upgrading technology and human resources, and developing linkage.

The SME Development Framework will require significant efforts by the

Government. It will also require the cooperation and coordination of donors, business associations, and other stakeholders. Moreover, the framework should be periodically reviewed and revised to reflect changing conditions and priorities for Cambodian SMEs.

The development of SMEs in Cambodia is facing many challenges:

- The electricity tariff remains high compared to neighbouring countries, and is a big obstacle in strengthening Cambodia's competitiveness as well as attracting investments and improving livelihoods. Access to electricity in rural areas is still limited.
- The shortages of technicians and skilled workers are a major obstacle to accelerating SMEs in both urban and rural areas.
- There is a lack of support from the government in human resources development, market information and market access, and technological innovation.

**Table 4. Status of Licensed Factory & Handicraft in 2010**

Capital/Province	Beginning balance			Newly register			Close down			Total number at Ending		
	SME			SME			SME			SME		
	Large	License	Register	Large	License	Register	Large	License	Register	Large	License	Register
Phnom Penh	371	0	542	37	0	248	15	0	0	393	-	790
Kandal	111	372	729	17	0	76	5	0	9	123	372	796
Takeo	4	39	50	0	3	17	0	0	0	4	42	67
Prey Veng	0	75	194	0	0	84	0	3	0	-	72	278
Svay Rieng	8	7	112	1	6	82	0	0	0	9	13	194
Kompot	5	43	884	0	10	114	0	0	0	5	53	988
Kep	0	2	29	0	0	14	0	0	0	-	2	43
Shihanouk Ville	17	26	99	0	0	0	0	0	0	17	26	99
Koh Kong	2	10	192	0	0	14	0	0	0	2	10	206
Pursat	0	58	1,940	0	4	12	0	0	0	-	62	1,952
Pailin	0	6	0	0	0	35	0	0	0	-	6	35
Battambang	4	396	403	2	9	25	0	0	0	6	405	428
Banteay Mean Chey	2	78	241	0	0	75	0	0	0	2	78	316
Oudor Mean Chey	0	6	89	0	1	0	0	0	11	-	7	78
Preah Vihea	0	3	0	0	0	25	0	1	0	-	2	25
Siem Reap	0	108	1,716	1	6	370	0	40	85	1	74	2,001
Kompong Thom	1	95	89	1	1	86	0	0	0	2	96	175
Kompong Cham	7	66	42	2	58	0	0	0	5	9	124	37
Kompong Speu	17	21	4,623	1	12	888	0	0	0	18	33	5,511
Kompong Chhnang	7	44	980	1	0	12	0	9	0	8	35	992
Kratie	0	4	286	0	7	131	0	0	0	-	11	417
Stung Treng	0	1	27	1	2	0	0	0	0	1	3	27
Ratanakiri	0	4	0	1	2	3	0	0	0	1	6	3
Mondolkiri	0	2	39	0	1	9	0	0	0	-	3	48
<b>TOTAL</b>	<b>556</b>	<b>1,466</b>	<b>13,306</b>	<b>65</b>	<b>122</b>	<b>2,320</b>	<b>20</b>	<b>53</b>	<b>110</b>	<b>601</b>	<b>1,535</b>	<b>15,516</b>

Source: GD of Industry, MIME.



### **3.6. Poor Infrastructure**

One of the main constraints, in industrial readjustment in Cambodia is poor infrastructure. Industrialization cannot be accomplished without adequate and good quality of infrastructure. Cambodia is still in poor infrastructure including highways, railways, ports, air-port, warehouses, and other facilities.

## **4. CONCLUSION**

Industrial development strategy in Cambodia is in place through National Strategic Development Plan (2009-2013) but it not sufficient. The country needs a long term strategy that is equipped with clear vision, mission and action plan. The Strategy should not be only involved with industry itself but it should be involved with many related sector (or cross-cutting sector approach) such as policy related to FDI, environment, agriculture, trade, infrastructure, energy and vocational training.

Cambodia's industrial readjustment has been done to cope with the changing environment of the domestic, regional economic integration and the world market. Cambodia has benefit from its potential and external factors such as Official Development Assistance (ODA) and increased trade and FDI. Though it is in the early stage of development, Cambodia's industry has become the core of future economic development.

Cambodia's industrial readjustment has two goals: the development of export-oriented industries and the development of import-substituting production of selected consumer goods. These goals are to be achieved by promoting labour-intensive industries, natural resource-based industries, SMEs, the agro-industry,

technology transfers and upgrades in the quality of industrial products, establishment of industrial zones, and development of selected import-substitution production.

In the process of industrial readjustment, the country is facing many daunting challenges including lack of long-term strategic plans, Special Economic Zones, lack of Energy, management of extracting industries, supporting framework for SMEs development and poor infrastructure.

In an internationally competitive environment, it is not a question of survival of the size of economies, biggest or smallest, but the fastest. Only those who keep pace with the rapidly changing industrial trends survive and others fall apart. Industrial policy should keep the stakeholders abreast of the changes and the institutional and policy direction should enable them to keep pace with those changes.

## **5. RECOMMENDATIONS**

There are three sets of recommendations:

### **5.1. General Recommendation**

Cambodia is seeing the emergence of many new opportunities but we can seize them only if we are willing to work hard. Central agencies such as the Ministry of Economy and Finance, National Bank of Cambodia, Ministry of Commerce and other relevant Ministries/Institutions must double their efforts to prepare and implement the much needed reforms aimed at improving institutional functions and coordination, encouraging domestic and foreign trade, facilitating business as well as introducing incentives for the successful implementation of industrial development policy,

especially for supporting capital mobilization, knowledge creation and skill training. These underscore the importance of the key reform pillars of the Royal Government including public financial management reform, trade facilitation reform and financial development.

Cambodia should recognise the need to improve the implementation capacity of sector level institutions and coordination among the concerned agencies. For example, the development and regulation and industrial standards require coordination and close cooperation between the Ministry of Industry, Mines and Energy and other relevant Ministries/Institutions of the Royal Government. It also requires strengthening of the research capacity and skill training. Coordination and close cooperation between the Ministry of Education, Youth and Sports, Ministry of Labour and Vocational Training, Ministry of Social Affairs, Veterans, and Youth Rehabilitation and other relevant Ministries/ Institutions will be required to accomplish this task.

Private sector, which is the key player in the market economy, will have to closely partner with the Royal Government to enhance the competitiveness of Cambodia through promotion of creative ideas, innovation, and research and development. Linking education and training to the labour market conditions within the framework of the new governance architecture will be a key aspect of the implementation of industrial development policy.

## **5.2. Specific Recommendations**

For the Government

1. A Long Term Strategic Plan for Industrialisation and Industrial Policy should be formulated to boost industrial development. The industrialisation policy

should include a master plan for regional hubs of industrial corridors for the future country's industrial zoning. Special promotion of industrial zones at different provinces is recommended. The Plan should also be incorporated with the context of ASEAN Economic Community which will be finalized by 2012.

2. The government should formulate a technology transfer policy to promote technical skill and encourage the FDI companies to invest in R&D in Cambodia.
3. The government should strengthen standards and quality control to restrict the import of poor-quality products, while at the same time promoting the quality of local products to improve competitiveness.
4. Investment and trade promotion should be conducted more in Cambodia, and also abroad, so that the government can attract FDIs for producing intermediate goods in the country. Special incentives should be provided in SEZs for selected industries such as electronics and food processing that use local raw materials for manufacturing and exports.
5. Licensing of investment projects related to industries should be focused on job creation, reducing disparity and technology transfer.
6. Promotion of selected industries that provides Cambodia a special comparative advantage should be done urgently. For example, since Cambodia is an agro-based country, processing industries should be encouraged.
7. Clear policies on production, exporting of mineral ores should be formulated and human resources should be well trained in the management of extracting

industries including mining and petroleum-related industries so as to reap the benefits of these booming and promising industries.

8. Regional cooperation in different mechanisms, such as Greater Mekong Sub-region (GMS), ASEAN-Mekong Basin Development Cooperation (AMBDC) and ASEAN Economic Community (AEC), which will be realized by 2015, should be integrated into actions by the Royal Government of Cambodia, especially in priority areas, such as Initiative for ASEAN Integration (IAI), and regional infrastructure connectivity.

#### For the Private Sector

1. The private sector should work together more closely to promote professional associations, entrepreneurship, and innovation.
2. The private sector should find foreign partners to work with in order to share experiences and gain technical knowledge from them. The partners should work together with honesty, shared interests and mutual respect.

#### For Development Partners

1. Development partners should provide scholarships to Cambodian students for study in select industries that the country needs to develop, such as oil and gas, mines, energy, and telecommunication.
2. Official Development Assistance (ODA) should be provided to increase industrial productivities and to promote the quality of local products. The concepts of “one village, one product” should be further realised.

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