

# CAMBODIA'S FUTURE JOBS: LINKING TO THE ECONOMY OF TOMORROW



# **CAMBODIA'S FUTURE JOBS:** LINKING TO THE ECONOMY OF TOMORROW

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# Contents

<b>Currency Equivalents</b>	<b>4</b>
<b>Abbreviations and Acronyms</b>	<b>4</b>
<b>Preface</b>	<b>5</b>
<b>Acknowledgements</b>	<b>6</b>
<b>List of boxes, figures and tables</b>	<b>7</b>
<b>Executive Summary</b>	<b>9</b>
<b>Introduction</b>	<b>11</b>
<b>Snapshot of Today's Jobs: Cambodia's Export-Oriented Development Strategy Has Uniquely Shaped its Jobs Structure</b>	<b>12</b>
Cambodia's economy supports many jobs	12
Although modern jobs are rapidly being created, the majority of jobs are still in traditional sectors	12
By many measures, job quality is improving but remains low	15
The current economic structure has served some populations better than others	19
<b>The Current Export Strategy May Not Deliver the Future Jobs to Which Cambodia Aspires</b>	<b>20</b>
Weak employment growth in FDI and domestic firms challenges better jobs	20
Labor productivity lags behind other countries and unit labor costs are high	22
Exports are concentrated in low-value activities	24
Low skill levels and returns to education underpin low labor productivity	25
Links with the domestic sector are weak	29
Macroeconomic risks also create jobs risks	30
<b>Policy for a Jobs Future Consistent with Cambodia's Vision 2050</b>	<b>31</b>
1. Diversify Exports and FDI into Higher Value-added Value Chains (or Segments of Value Chains)	32
2. Streamline Procedures and Reduce the Costs of Establishing and Expanding SMEs	33
3. Support Household Enterprises to Enhance Their Productivity	34
4. Support the Development of Links between FDI Firms and Domestic Input-supplying Firms	35
5. Build a Skills Development System that will Attract Higher-value FDI and Increase Productivity across the Economy	36
6. Promote Efficient Labor Mobility and Job Matching	37
7. Regain Macroeconomic Independence and Exchange Rate Flexibility	38
<b>A Vision of Cambodia's Future Jobs</b>	<b>40</b>
<b>References</b>	<b>41</b>

# Currency Equivalents

Exchange Rate Effective October 15, 2018

Currency Unit = Cambodian Riels (KHR)

USD 1 = KHR 4,076.47

# Abbreviations and Acronyms

CMT	Cut-Make-Trim
CSES	Cambodia Socio-Economic Survey
EAP	East Asia and Pacific
EGRA	Early Grade Reading Assessment
EU	European Union
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
GVC	Global Value Chain
ILO	International Labor Organization
ICT	Information and Communications Technology
IT	Information Technology
MNC	Multi-national Corporation
OECD	Organization for Economic Cooperation and Development
PPP	
R&D	Research and Development
SEZ	Special Economic Zone
SME	Small and Medium Enterprise
TVET	Technical and Vocational Education and Training
VAT	Value Added Tax
STEM	Science, Technology, Engineering and Math

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# Preface

*Cambodia's Future Jobs: Linking to the Economy of Tomorrow* summarizes an extensive analytical exercise that is described in full in the accompanying Technical Report. All of the material in this Main Report document, unless otherwise cited, is presented in detail in the Technical Report, including data sources, full citations, and a complete analysis and interpretation.

The Technical Report includes the following chapters:

**Chapter 1:** Introduction to Jobs in Cambodia

**Chapter 2:** Macroeconomic Policies Conducive For Creating Good Jobs

**Chapter 3:** Creating More and Better Jobs Through Private Sector Development

**Chapter 4:** Jobs and the Export Sector

**Chapter 5:** Workforce Skills for More, Better and More Inclusive Jobs

**Chapter 6:** Policy for Future Jobs Consistent with Cambodia's Vision 2050

Several background papers were also prepared to inform the report. They are cited in the chapters where their results are presented.

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# List of boxes, figures and tables

## BOXES

Box 1:	Jobs Definitions	11
Box 2:	The Impact of Minimum Wage in the Garment Sector	17
Box 3:	The Stages of Global Integration for Development and Jobs	20
Box 4:	Cambodia's Investment Climate Assessment	23
Box 5:	The Rise of the Sewbots? Maybe Not Quite Yet...	31
Box 6:	Policies to Move Up the Value Chain in Cambodia's Tourism Sector	33
Box 7:	Policy Implications for Inclusive Jobs	39

## FIGURES

Figure 1:	Labor Force Participation Rates in Cambodia and Comparator Countries	13
Figure 2:	Job Type Distribution, 2015	14
Figure 3:	Job Types, 2007 and 2015	14
Figure 4:	Composition of Household Employment, 2014	15
Figure 5:	Composition of Household Income, 2014	15
Figure 6:	Growth in Employment Share of Tasks, by Task Type, 2009-2015	16
Figure 7:	Hourly Earnings of Household Enterprise Workers and Wage Workers	18
Figure 8:	Gender Wage Gap	18
Figure 9:	Source of Employment, by age	19
Figure 10:	Employment Elasticity to Sales Growth for Apparel Firms	21
Figure 11:	The Lifecycle of a Firm	21
Figure 12:	Firm-level Productivity and Capital Intensity, 2016	22
Figure 13:	Productivity in Agriculture and Industry	22
Figure 14:	Average Wages and Unit Labor Costs in Apparel Firms	23
Figure 15:	Median Value-Added of Exports	24
Figure 16:	Total Labor Content Share of Apparel and Textiles in Gross Exports	24
Figure 17:	Rate of Return to Education	25
Figure 18:	Share of Employers Who Are Affected by An Inadequately Skilled Labor Force	26
Figure 19:	TVET Enrollment	26
Figure 20:	Percentage of Second Grade Students who Perform below Proficiency on Reading Assessments (EGRA)	26
Figure 21:	Net Effect of High-Skilled Emigration on the Share of High-skilled Workers in ASEAN Source Countries	27
Figure 22:	Inputs and Supplies Locally Sourced by Garment Firms	28
Figure 23:	Correlation between Wage Employment and the Number of Non-farm Enterprises	28
Figure 24:	Export Growth to the EU and EUR/USD Exchange Rate	29
Figure 25:	Seven Policies for More, Better, and More Inclusive Jobs in Cambodia	32

## TABLES

Table 1:	Employment by Main Occupation, 2004 and 2014	16
Table 2:	Ten Fastest Growing Occupations, 2009 and 2014	16



# Executive Summary

**Cambodia has succeeded in implementing an effective FDI-led development strategy.** Its 7 percent GDP growth rates have been accompanied by rapidly falling poverty rates. Over 1 million workers are now employed in the garment sector, and the share of jobs in industry continues to grow.

**Cambodia's exposure to the global economy combined with the government's outward-looking economic policies have yielded good results.** First, by opening its borders to international trade and investment, Cambodia attracted FDI, particularly in the garment sector, because of its low trade barriers, stable government, and relatively hassle-free business practices. Second, the spike in international commodity prices was a boon to a still largely agricultural economy, thus alleviating pressure to make a quick transition out of agriculture. Third, a further reduction of trade costs and the existence of an abundance of highly mobile, low-skilled, and, thus, low-cost, labor provided a further impetus to investments in the garment sector and a continuation of the structural transformation process.

**Although Cambodia's current economic model is still delivering good new jobs, its success may be slowing down.** The garment sector that has been the main driver of Cambodia's jobs and growth is showing some weaknesses. Job creation is slower than in the same sector in other countries. Its labor productivity has stagnated, and unit labor costs are higher than those in competitor countries, thereby negatively affecting Cambodia's competitiveness. The potential loss of trade preference with the EU and the US in the near term will also impede the country's competitiveness in key export markets. The garment sector has few links with domestically owned small and medium-sized enterprises (SMEs) as it relies less on local sourcing than do garment firms in other countries—such as Vietnam, Turkey or India—or other export-oriented industries in Cambodia. The labor force does not have the skills to attract higher-value FDI, nor do they have the means to acquire those skills.

**Moreover, a large share of Cambodia's current jobs may not be of the kind that the country will aspire to create in the future.** More than half of all jobs are still in

family farming or household enterprises, which are lagging behind the rest of the economy in terms of productivity and growth. Fully 94 percent of jobs are in low-skilled occupations, with managers and professionals accounting for less than 5 percent of all jobs. While wages have increased in recent years, particularly for those near the bottom of the income distribution, more than half of jobs operate outside of the modern economy. Family farming and household enterprises primarily trade amongst themselves, which limits their growth and profits. The economy provides markedly fewer opportunities for women and older workers than it does for men and younger workers.

**The current model is further at risk due to several emerging mega-trends that will alter how external forces shape Cambodia's jobs picture in the future.**

Changing consumption patterns resulting from a growing consumer class within Cambodia and across Asia will change the composition of both domestic and export demand. New trade agreements and technologies will further shift global trade patterns. Automation has the potential to create more, better, and more inclusive jobs, but also to make others disappear. The advent of new technologies means that workers will require a more complex set of skills than in the past.

**Cambodia can manage these trends by taking the steps necessary to move into the next stage of FDI-led development: diversification and densification.**

This would mean pursuing higher-value FDI and fostering links between exporting firms and domestic input-supplying firms. However, this will only be possible if Cambodia lays the foundations by reforming its own policies to attract and retain more, better, and more inclusive jobs.

**We propose seven jobs-specific policies that, in conjunction with broader sectoral development strategies, have the potential to generate better jobs in Cambodia in the future.** These policies are in alignment with the principles and recommendations of the Royal Government of Cambodia's Rectangular Strategy-Phase IV. We present these seven policy actions in one document to show how they can improve the quality and increase the inclusiveness of Cambodia's jobs. The specific policy recommendations are as follows:

**First, diversify exports and FDI into higher value-added value chains or segments of value chains.** Most current jobs are in low-value segments of global value chains (GVCs) in which Cambodia's exports sectors have the lowest median value-added among those of their peer countries. Simplifying processes, providing incentives to foreign investors, and creating quality assurance facilities will encourage the diversification of exports and FDI into higher value-added value chains (or segments of value chains). Signing, finalizing, and enforcing international trade and investment agreements with key trade partners will also be vital to mitigating the risk of losing special access to markets such as the European Union.

**Second, streamline procedures and reduce the costs of establishing and expanding SMEs, which have considerable potential to create jobs.** It is harder for firms to expand in Cambodia than in other countries. Young firms in Cambodia—defined as those that have been operating for less than five years—create little employment, even though this stage is critical for a firm's growth. Establishing a range of institutions that can support entrepreneurs during the various stages of a firm's development, including ideation, incubation, and acceleration, will help SMEs to grow and create jobs at the various stages of their lifecycles. There is also a need to reduce the costs that they incur in doing business as well as to enhance their access to finance to be able to compete on both the domestic and international markets.

**Third, help household enterprises enhance their productivity and create better jobs.** Nearly one in five jobs in Cambodia are in household enterprises, and this share is projected to grow as a consequence of more rapid urbanization. Thus, it will be necessary for policymakers to have a much stronger focus on this often-forgotten segment of the economy to enable these very small enterprises to increase their revenues and, hence, to create better jobs. Information technology can help household enterprises to improve their basic business practices and to access broader markets.

**Fourth, support the development of links between exporting FDI firms and domestic input-supplying firms.** Government policies can provide foreign firms with incentives to source their inputs from local SMEs. At the same time, the government can help SMEs to understand and meet the quality standards of FDI firms and provide them with financing to upgrade their production processes.

**Fifth, build a skills development system that will attract higher-value FDI and increase productivity across the economy.** While a solid education system is the foundation of any future workforce, today's workforce in Cambodia is getting by with only 6.3 years of education on average, while having few opportunities to upgrade their skills. This points to the need for a dual strategy. First, it would be advisable to reform today's education system to help the next generation of workers to acquire the broad range of skills needed to work in a knowledge-intensive economy. Second, policymakers should consider developing a strategy (including incentives) for engaging enterprises in the design, financing, and support of a modernized technical and vocational education and training system (TVET).

**Sixth, promote efficient labor mobility and job matching.** A mis-match between skills and jobs stifles productivity and frustrates workers' sense of well-being. Helping people to find and acquire the right jobs will reduce these inefficiencies. First, policymakers should systematically produce and disseminate information about jobs inside and outside of Cambodia to help students, jobseekers, education and training institutes, and employers to make skills development choices that are aligned with rapidly evolving market demand. Second, they should continue opening formal international migration channels while supporting programs that encourage circular migration.

**Seventh, regain macroeconomic independence and exchange rate flexibility.** US dollar fluctuations significantly impact Cambodia's trade and commodities sectors, which are responsible for most of the country's jobs. As Cambodia begins to export to a broader range of countries, macroeconomic and fiscal stability will help shield existing jobs from factors related to the US dollar.

**If Cambodia can successfully transition to the next stage of an FDI-driven development strategy, this is likely to produce more and better jobs.** Achieving this goal will be a complex challenge and will require strong leadership by a coordinating body tasked with championing the jobs issue and guiding the many actors from different sectors toward a shared future jobs vision. While the world is changing fast, Cambodia still has an opportunity to make this transition and improve the quality of jobs for all of its citizens.



## Introduction

**Cambodia's economic growth and jobs transformation has been significant by global standards and has largely been driven by the government's embrace of an export-driven development strategy.** Over the period 2000 to 2015, Cambodia's exports of goods and services—mainly garments and tourism—grew by nearly 20 percent annually and were the driving force behind the country's (average) annual GDP growth rate of 7.9 percent over the same period.<sup>1</sup> The economy's integration into the global economy was the result of the government's strategy of attracting foreign investment into industries that played to Cambodia's comparative advantages: an abundant, low-skilled, and highly mobile labor force and a stable government that was eager to facilitate the movement of foreign capital and goods.

**This export-oriented strategy has created more, better, and more inclusive jobs in Cambodia than existed at the beginning of the reform period.** Since the late 1990s, 3.6 million net jobs have been created in services and industry (compared to 0.7 million agricultural jobs), with nearly 1 million of those new jobs being in the garment sector. Most of the jobs in the garment sector pay at least the minimum wage and offer a range of additional monetary and non-monetary benefits, unlike most jobs in the domestic economy. Furthermore, they are highly inclusive jobs, in that they draw vast numbers of low-skilled young women to the urban centers where the garment factories are located (Box 1).

**These jobs underpinned Cambodia's rapid poverty reduction.** Between 2004 and 2012, the poverty incidence under Cambodia's national poverty line declined from 50 percent to 18 percent of the population. Inequality,

measured by the Gini coefficient, fell from 32 to 28 between 2008 and 2012, largely due to the poorest 40 percent of the population having higher increases in consumption than the top 60 percent. Although Cambodia reached lower-middle-income status in 2015, the vast majority of families still hover near the poverty line and are at daily risk of falling into poverty in the event of an adverse shock.

**Two factors suggest that the current economic development strategy may not continue to deliver the quality of jobs to which the Cambodian government aspires. First, the current export-driven development strategy may not be performing as well it could.** Although Cambodia's apparel sector has continued to add jobs (at least up to 2015), the sector is *under*-producing jobs relative to global norms. Also, unit labor costs exceed levels in competing textile-producing countries, offered wages are below aspirational wages, and foreign firms are not using local suppliers of goods or services. While attracting FDI to low-value-added industries was an appropriate jobs strategy during the period when Cambodia was first entering the global economy, it may no longer be the best strategy for creating more, better, and more inclusive jobs going forward. The potential loss of special access for Cambodia's exports in important markets such as the European Union would further undermine key exporting industries and make it harder to attract FDI.

**Second, domestic, regional, and global mega-trends are changing what will be produced and how it will be produced, thus creating new job opportunities in some areas while destroying jobs in others.** Incomes are rising in Cambodia and Asia, and consumption is both increasing and diversifying into higher value-added goods and, especially, services. Urbanization is creating a larger consumer class that wishes to purchase goods and services

### Box 1: Jobs Definitions

**For the purposes of this report, a “job” will be defined as any income-earning activity that is not illegal.** Thus, a job may be as simple as the employment of a full-time worker, in a factory, who is earning a wage or as complex as the range of income-earning activities carried out by a household in various sectors at different times of the year.

**A “good” job is a subjective concept that depends on the economic structure, culture, and aspirations of a country, its industry, and its people.** In the case of Cambodia at this time, the report will assume that a good job is characterized by high productivity, a wage commensurate with productivity levels, safe work conditions, and job security.

**An “inclusive” job can be defined as one that is open to any Cambodian citizen** regardless of gender, age, or ability, as well as one that integrates different segments of the economy into a single market.

<sup>1</sup> Cambodia's export expansion was only eclipsed by one other country in the world (Equatorial Guinea) and was far ahead of star exporters, including Vietnam (15.5 percent) and Bangladesh (15.3 percent) (World Bank 2017b)

that were previously self-produced. Demographic trends are shrinking the size of the workforce in Cambodia's neighboring countries (China, Thailand, Vietnam, and developed East Asia) while creating new industries to serve a growing and aging consumer class. Trade patterns are shifting due to new trade pacts, and China is becoming a lead country in GVCs. Technology is changing the nature of work across economies, from the smallest micro-enterprises to the largest sophisticated factories, and this is resulting in the creation of jobs that require more skills than ever before.<sup>2</sup>

**This report identifies the policy reforms that will be needed to overcome these challenges and to create more, better, and more inclusive jobs in the future.**

We begin by reviewing the structure, source, and quality of today's jobs, arguing that Cambodia's export-oriented strategy has been an important catalyst for creating new and better jobs.<sup>3</sup> We then discuss the limitations of the current economic strategy for creating and upgrading jobs and go on to describe the opportunities that the mega-trends are likely to provide. Finally, we propose two strategies to enhance the quality and inclusiveness of Cambodia's jobs. First, we argue that Cambodia needs to move towards Stage II of FDI-driven development, wherein it should promote global integration by attracting higher-quality FDI and creating an enabling environment and incentives to encourage foreign-owned firms to develop closer links with the domestic private sector. Second, we recommend seven specific reforms that need to occur within Cambodia to attract new FDI to diversify the economy and to fully benefit from the job opportunities that it will offer. This report is the synthesis of a detailed and comprehensive analysis presented in the Technical Report.

**The analytical findings and policy directions of this report are intended to contribute to policymaking in two ways.** First, it provides a focus on jobs. The government's *Rectangular Strategy for Growth, Employment, Equity and Efficiency: Building the Foundation Toward Realizing the Cambodia Vision 2050 - Phase IV* is comprehensive by design and addresses a wide range of policy objectives. Most of the strategic sides of the respective strategic rectangles are sector-specific.<sup>4</sup> In contrast, this report draws from across the strategy to pull together a range of policies that collectively will create more, better, and more inclusive jobs. Second, while specific job strategies, particularly the *National Employment Policy: 2015-2025*, provide general directions, in this report, we attempt to provide more detailed

policy options. The mapping of the policies recommended in this document and those contained in the Phase IV of the *Rectangular Strategy* is shown in the policy matrix at the end of this review, which also suggests the agencies that might lead the reform process.

## Snapshot of Today's Jobs: Cambodia's Export-Oriented Development Strategy Has Uniquely Shaped its Jobs Structure

### Cambodia's economy supports many jobs

**There are 8.2 million jobs in Cambodia, and 160,000 new workers enter the labor force every year.** About 80 percent of Cambodians aged 15 or older are working, which is among the highest rate globally and is far higher than the expected labor force participation rate for a country at Cambodia's level of development (Figure 1a). This is partly attributable to Cambodia's very high female labor force participation rates (Figure 1b), which fluctuate between 73 and 80 percent compared with a regional average of 61 percent and a global average of 50 percent. This is perhaps not surprising given the predominance of traditionally "female" industries in Cambodia's economy, specifically garments and tourism. The size of the labor force is expected to continue growing until 2044 because Cambodia is one of the few countries with a young population in an aging region.

### Although modern jobs are rapidly being created, the majority of jobs are still in traditional sectors

**As of 2015, while 4 in every 10 jobs were in non-farm public and private wage employment, the other 6 were in family farming, farm wage labor, and non-farm household enterprises** (Figure 2). This is a very different picture than less than a decade before when 8 in 10 jobs were in traditional sectors defined as having employees who work in low-skilled (micro or small) firms that do not abide by labor legislation (Figure 3). A sizeable share of jobs in non-farm wage work can also likely be classified as "traditional." This report refers to traditional jobs as

<sup>2</sup> In this report, we only list the mega-trends that are relevant to the jobs discussion. A longer and broader list is presented in Phase IV of the *Rectangular Strategy*.

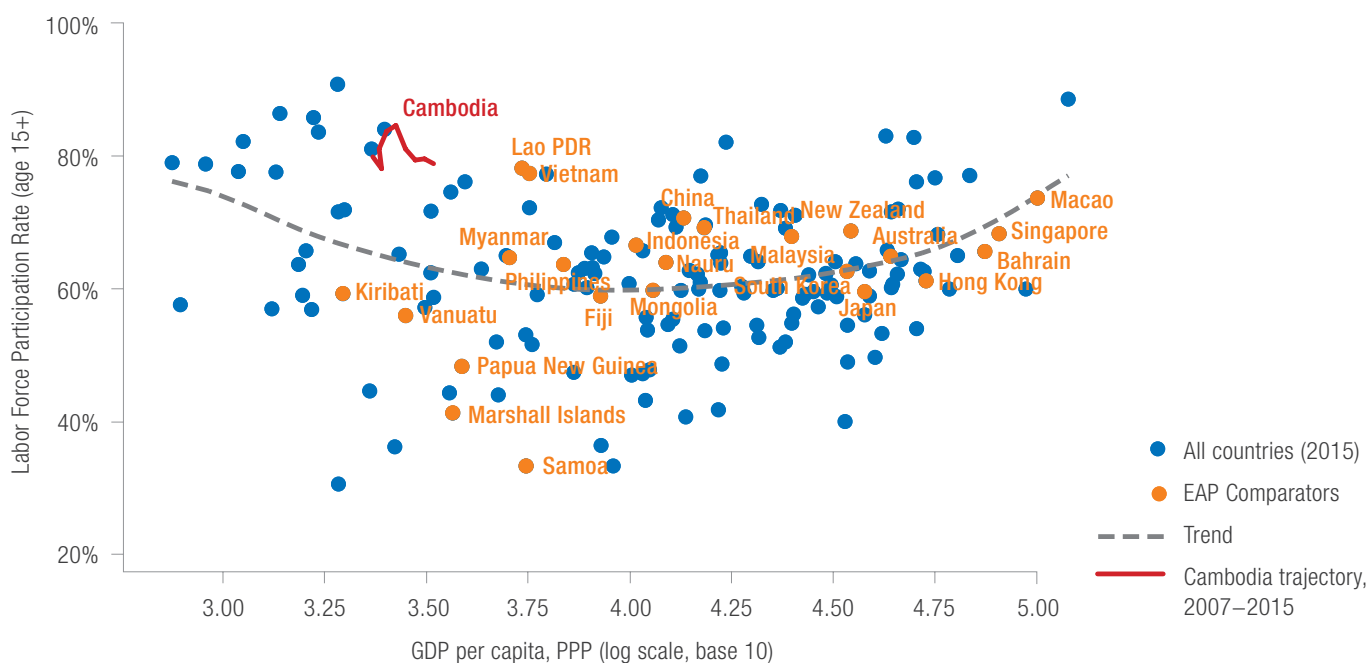
<sup>3</sup> This report does not explore the jobs situation in agriculture or policy options for creating better agricultural jobs. Since the nature of agricultural jobs is quite distinct from more market-based jobs, they merit a separate analysis.

<sup>4</sup> The *Rectangular Strategy* is depicted as four strategic "rectangles" that encompass four aspects of development—human resources, economic diversification, private sector and job development, and inclusive and sustainable development—and each "side" of each rectangle is a (generally) sector-specific priority within the respective rectangle. Each side of the rectangle is underpinned by several policies. The four rectangles surround four "environment" concepts, and the core of the model is governance reform. The human resource development strategic rectangle is the priority for Phase IV.

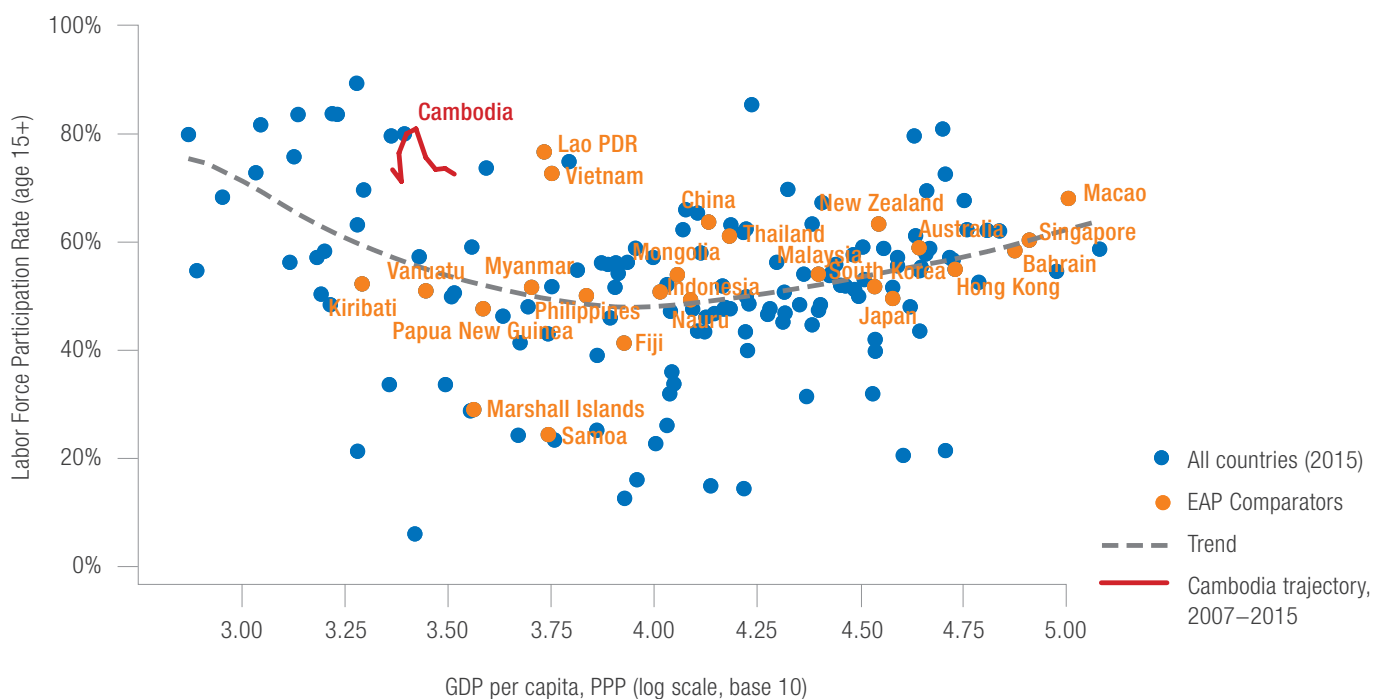


**Figure 1:**  
Labor Force Participation Rates in Cambodia and Comparator Countries

**(a) Total Labor Force Participation Rate**



**(b) Female Labor Force Participation Rate**



**Source:** Author's estimates using CSES 2007-2015 and the WDI online database.

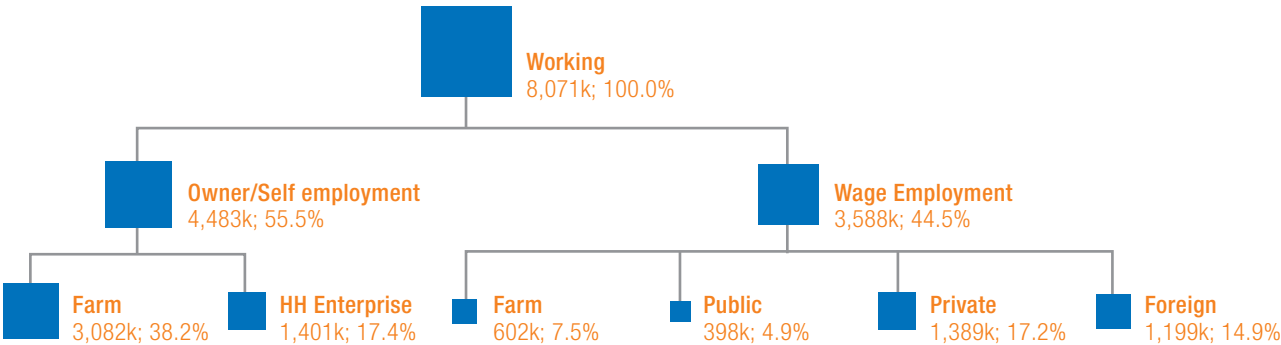
work in non-wage family farms and non-farm household enterprises. It refers to modern jobs as wage-paying jobs in non-farm industries. While the data do not allow us to estimate the number of these workers in Cambodia, in Vietnam, for example, these workers comprise half of all (non-public sector) wage employees (Cunningham and Pimhidzai 2018).

**Cambodia’s a rapid swing toward modern jobs is due to the growth in non-farm wage employment, driven by exporting and foreign-owned firms in the garment industry** (Figure 3). The export-oriented textile, leather, and footwear sectors alone added more than 600,000 jobs (net) between 2007 and 2011, representing more than 40 percent of total net employment growth. The increase in private sector wage employment has been apparent in rural areas (from 12 percent to 26 percent of all rural jobs) as well as in urban areas (from 20 to 38 percent). However, the growth in employment in export firms has been disproportionately driven by a small number of very large firms. Large exporters constitute 10 percent of all exporting firms but are responsible for 88 percent of all (direct) exporting jobs. Indeed, large firms (those employing

more than 500 workers) across the entire economy are the source of 25 percent of wage jobs even though they only comprise 0.4 percent of firms. In contrast, small enterprises (those with 0 to 9 workers) constitute 97.8 percent of all firms but provide only 50 percent of all wage jobs. Foreign-owned firms also have a higher average number of workers per firm than domestically owned firms. For example, foreign-owned firms in the apparel industry employ 850,000 workers, or an average of 2,800 workers per foreign-owned apparel firm compared with 115 workers per domestically owned apparel firm.

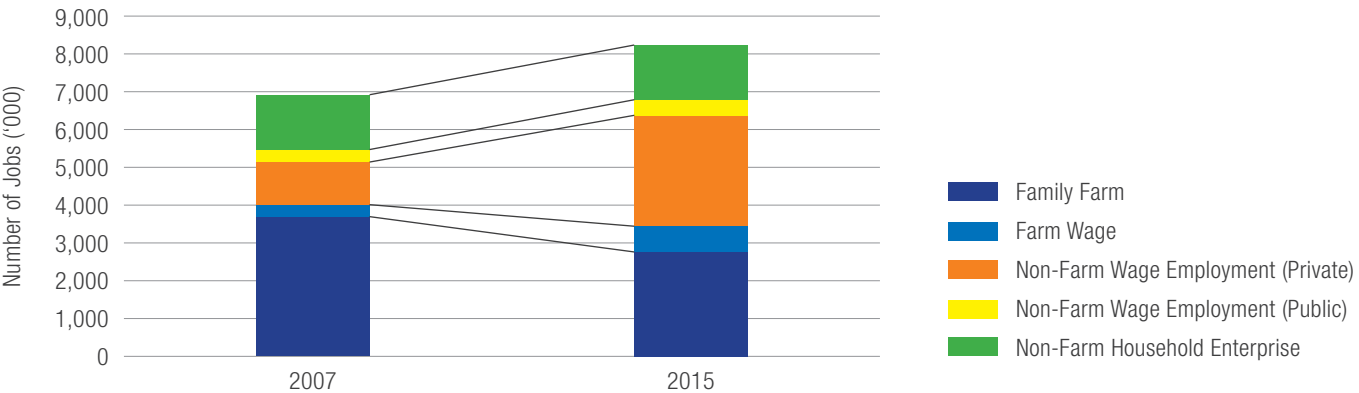
**While most job growth has been in manufacturing and services, half of Cambodia’s jobs are still in family-owned firms and farms.** About 3 million workers report family farming as their main source of income, and another 1.4 million primarily depend on household enterprises. While the number of family farmers has fallen significantly in recent years, the number of household enterprise owners is holding steady. The jobs picture can be complex in rural households, where members tend to hold an array of different jobs (Figure 4). For example, many non-farm household enterprises in rural areas also depend

**Figure 2:** Job Type Distribution, 2015



Source: CSES 2015.

**Figure 3:** Job Types, 2007 and 2015



Source: World Bank staff estimates using CSES 2014. Working age population estimate from UNPOP.

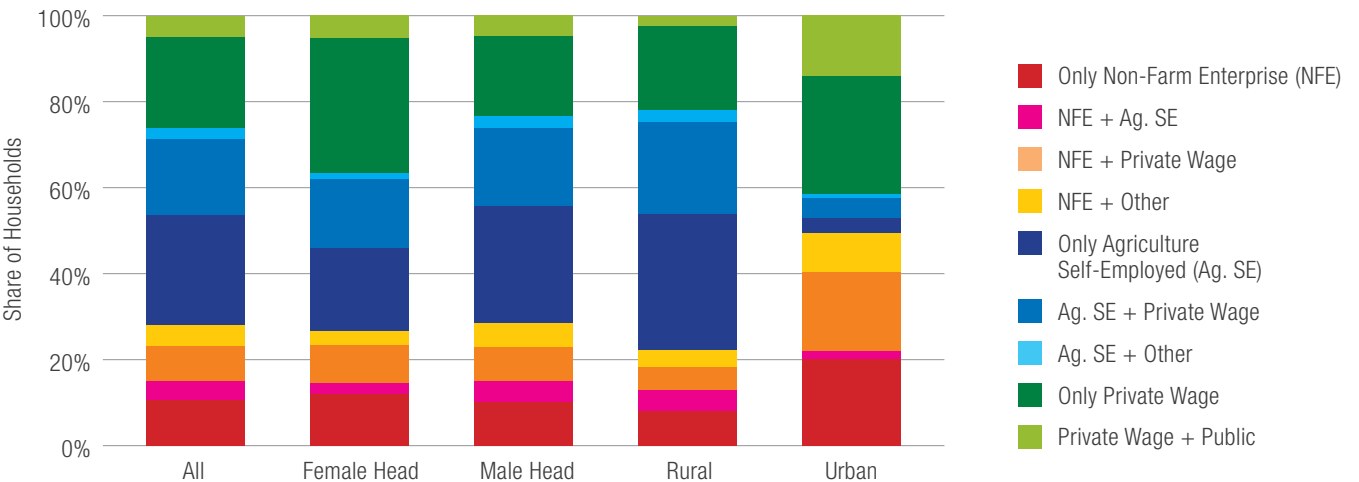
on income earned from agriculture, private wages, or other sources. On average, rural households earn most of their income from off-farm jobs, with only 24 percent derived from agriculture (Figure 5).

### By many measures, job quality is improving but remains low

**The Cambodian labor market primarily provides low-quality jobs, but there are some signs that this is changing.** More than 66 percent of jobs are in agricultural, forestry, fisheries, or elementary occupations (such as security guards, office cleaners, and tuk-tuk drivers). In contrast, fewer than 5 percent of jobs are high-

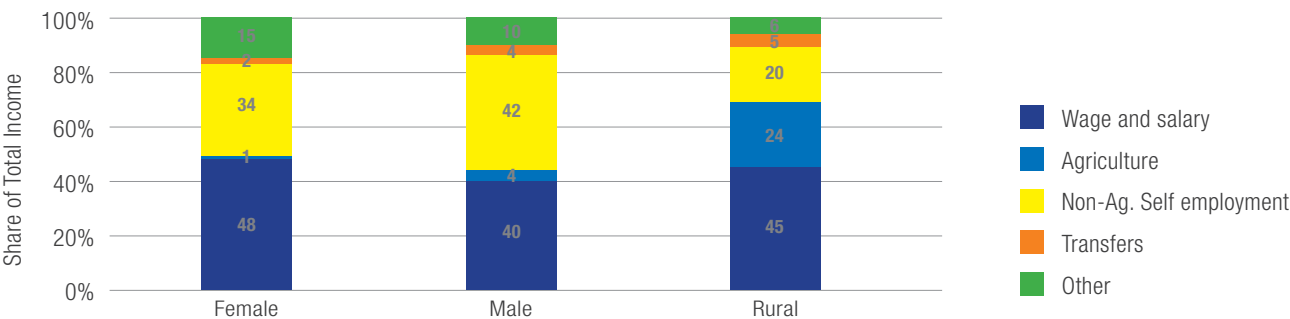
value managers, professionals, technicians, and associate professionals (Table 1). However, trends suggest that job quality is improving. The fastest growing jobs are in semi-skilled occupations such as construction and manufacturing (especially garments) and in semi-skilled white-collar jobs (Table 2).<sup>5</sup> More importantly, within occupational categories there is a shift away from subsistence occupations and towards market occupations that require similar skills. For example, a decline in the number of street and market sales assistants is being accompanied by a rise in the employment shares of shop sales assistants. Similarly, subsistence agricultural is declining as wage employment in agriculture increases.

**Figure 4:** Composition of Household Employment, 2014



Source: World Bank staff estimates using CSES 2014.

**Figure 5:** Composition of Household Income, 2014



Source: CSES 2015.

<sup>5</sup> Men are increasingly moving into both these types of occupations whereas women are only increasing in the latter category.

**Although Cambodia’s job growth so far has been driven by low-knowledge jobs, the country’s occupational profile is showing signs of becoming more knowledge-intensive.** Even in the short period between 2009 and 2015, there has been a significant increase in knowledge-intensive jobs in Cambodia, while growth in manual tasks has been stagnant or negative (Figure 6). Although the number of knowledge-intensive jobs is still low, trends suggest that this is beginning to change.

**Real wages have been increasing, with those at the bottom of the wage distribution gaining more than others.** Average real wages grew by over 54 percent between 2009 and 2015. By 2015, only 2 percent of Cambodian jobs paid wages below the international poverty line. Furthermore, the lowest wages increased at a faster rate than the highest wages, resulting in a decline in wage inequality.

**Table 1:** Employment by Main Occupation, 2004 and 2014

	2004	2014
Armed forces	0.9%	0.8%
Managers	1.3%	0.8%
Professionals	3.8%	2.6%
Technicians and associate professionals	0.6%	1.1%
Clerical support workers	0.2%	3.9%
Service and sales workers	13.6%	15.3%
Skilled agricultural, forestry, and fishery workers	58.7%	37.8%
Craft and related workers	6.1%	20.3%
Plant and machine operators and assemblers	6.1%	3.9%
Elementary occupations	8.4%	13.4%
<b>Total</b>	100.0%	100.0%

**Source:** World Bank staff estimates using CSES 2004-14.

**Table 2:** Ten Fastest Growing Occupations, 2009 and 2014

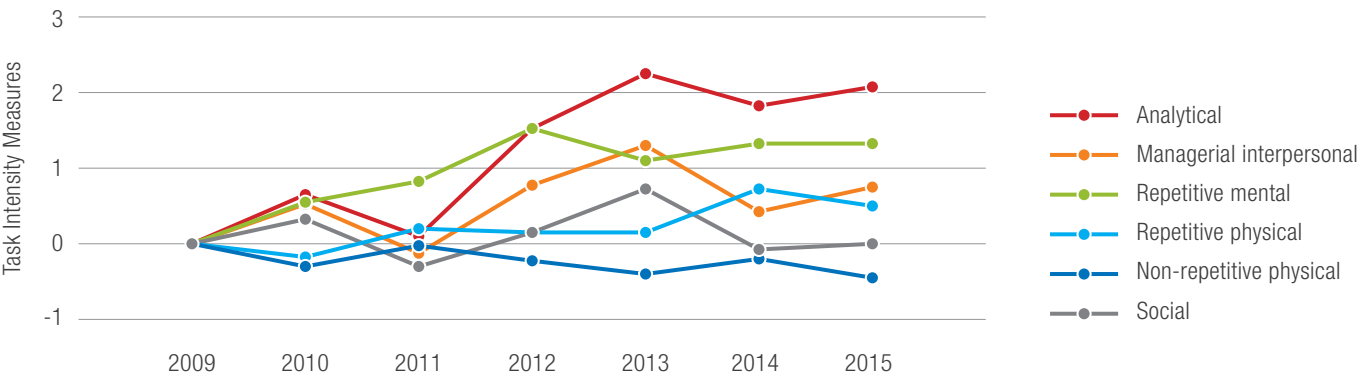
	2009	2014
Garment and related trades workers	+4.4%	+10.2%
Building frame and related trades workers	+0.5%	+2.8%
General office clerks	+0.8%	+2.6%
Agricultural, forestry, and fishery laborers	+6.3%	+6.9%
Shop salespersons	+5.0%	+6.0%
Waiters and bartenders	+0.3%	+0.8%
Building finishers and related trades workers	+0.2%	+0.8%
Tellers, money collectors and related clerks	+0.2%	+0.7%
Hotel and office cleaners and helpers and building caretakers	+0.1%	+0.3%
Moto-taxi and tuktuk drivers	+1.2%	+1.5%

**Source:** World Bank staff estimates using CSES 2009-14

**Note:** Occupations in the three-digit ISCO that have an employment share of at least 0.1 percent.

**Figure 6:** Growth in Employment Share of Tasks, by Task Type, 2009-2015

*Cognitive tasks have gained the largest employment share over the period*



**Source:** World Bank staff estimates using CSES 2009-15, and O\*NET database on skills associated with different occupations.

**Note:** Aggregate task intensity measures follow the classification used in Autor and Acemoglu (2011). Task intensity scores are standardized by the mean and standard distribution of the scores in non-subsistence occupations weighted by the labor share of those occupations in 2009. Sample restricted to non-subsistence occupations in all years.

## Box 2: The Impact of Minimum Wage in the Garment Sector

**Cambodia has an unusual minimum wage scheme. It is only applicable to the garment and footwear sectors, the country's two largest manufacturing exports of the country.** The minimum wage legislation was put in effect in 1997. It was initially set at USD 40 per month and was gradually increased eight times, reaching USD 170 per month by January 2018. Although the nominal minimum wage increased by over 380 percent in the period, the real value of the minimum wage was below its 1997 level until the increase in January 2015 (see ILO 2016 for a detailed review).

**In addition to the minimum wage set by the government, employers in the garment and footwear sector are required to pay mandatory allowances to their workers.** These consist of allowances for: (i) transportation and accommodation (USD 7 per month); (ii) attendance (USD 10 per month); (iii) overtime meals (USD 0.5 per day); and (iv) a seniority bonus (USD 2 to 11 per month) after two years of employment,.

**A recent study examined the impact of minimum wage changes in Cambodia's garment sector between January 2009 to January 2015 on the labor participation, working hours, and total earnings of garment and non-garment workers.** It found that the minimum wage increases:

- Did not affect the participation rates of garment workers, non-garment wage workers, or non-wage workers.
- Raised average hourly real wage earnings for wage earners in the garment sector (by 2.8 percent) but reduced average hourly real wage earnings for those outside the garment sector (by 1.4 percent). These changes are of modest magnitudes relative to the size of the minimum wage increases during this period, which were 20 to 33 percent increments. Why? Most workers in the garment sector already earned above the increased minimum wage. Average wages for garment workers still increased as these wages were anchored to the minimum wage, but the increase was less than the proportional increases. An increase in the minimum wage raises the wages not only of the lowest paid workers but also of workers higher up the earnings distribution. In fact, the gains for the higher-earning garment workers were slightly larger than the gains for the lower-earning garment workers.
- Did not affect total household wage earnings. Instead, households reduced their working hours to maintain their same household earnings.

**However, the moderately positive impact of minimum wage hikes that were observed in the study may not be sustained in the future.** During the study period, the overwhelming majority of garment sector workers were already earning more than the subsequent increase. If minimum wages increase faster than productivity (and wage) increases among the lowest paid workers, future hikes may have a different impact than past increases. Empirical evidence from countries in East Asia and Latin America has consistently shown that, when the minimum wage is close to the market wage, it begins to have a positive impact on the earnings of minimum wage earners while causing more job losses. It is not possible to predict the level at which the minimum wage might begin to have a negative impact. Instead, it will be necessary to begin to monitor the impact of minimum wage increases and for policymakers, trade unions, and employers to determine the degree of labor market distortions that are an acceptable trade-off.

**Sources:** Shrestha (2019), de Carpio (2014), and Cunningham (2007).

**Considering job quality from the perspective of employers, labor productivity is growing even though it is under-performing on many measures.** Between 1993 and 2015, labor productivity in Cambodia grew by 3.6 percent. Exports partly drove this gain, with output per worker having grown by 11.6 percent between 2004 and 2011. Among large firms, particularly domestic firms, these productivity increases have been robust.

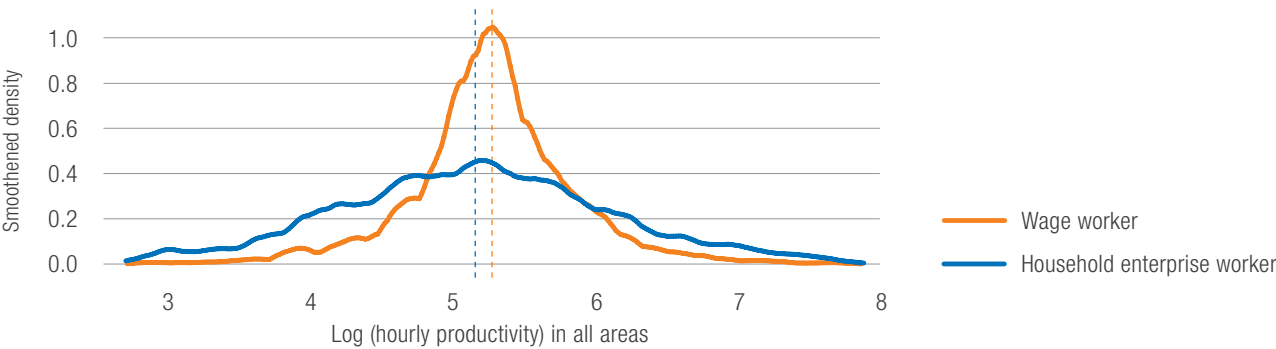
**Household enterprises are an important source of job creations, but their workers are more likely than wage workers to earn below the garment and footwear sector's minimum wage.** The share of household enterprises in total jobs (17 percent) is projected to grow as a result of rapid urbanization. About one quarter of all rural households and one half of all urban households operate a non-farm enterprise. The average earnings of household enterprises are higher than the average wages of

wage earners, but since they work longer hours, their hourly earnings fall below those earned in a wage job in a private firm (Figure 8). In addition, the share of workers earning below the monthly minimum wage is higher for household enterprise workers than for wage workers in the private sector (37 percent in household enterprises compared to 30 percent for wage workers).

**While operating a household enterprise often entails longer working hours and earning more variable income than holding a wage job does, it can offer non-monetary benefits.** For instance, women with a child

under the age of 5 are more likely to operate a household enterprise. This suggests that, although they end up working more hours in a day than they would in a wage job, the work is flexible enough for them to provide childcare while working. Similarly, a large sample survey in Vietnam found that household entrepreneurs regarded the independence and the opportunity to balance work and life as positive reasons to operate a household enterprise (Pasquier et al. 2018).<sup>6</sup> These household enterprise owners reported that these jobs paid better than agriculture jobs, provided a quality of life that is not feasible in formal wage jobs, and were far more accessible than more lucrative public sector jobs.

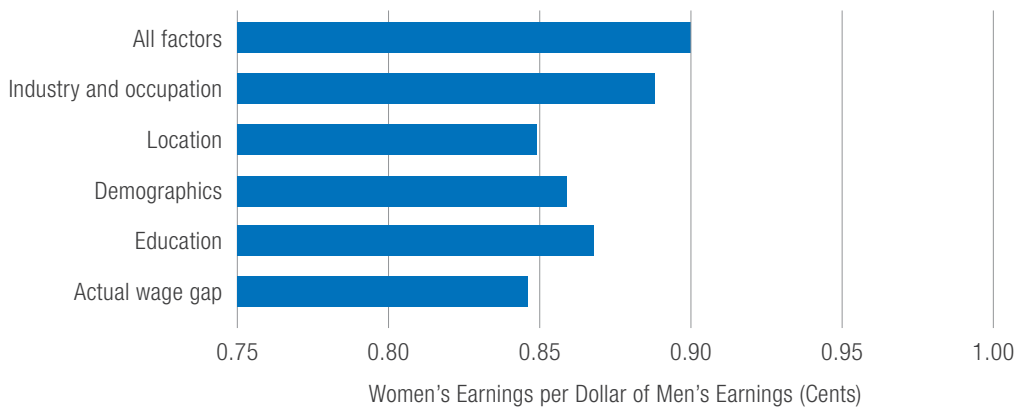
**Figure 7:**   
Hourly Earnings of Household Enterprise Workers and Wage Workers



**Source:** Author’s estimates using Cambodia CSES 2014.

**Note:** The productivity of wage workers is the monthly wage earnings per the number of hours worked. The productivity of a household enterprise worker is the share of profit accruing to the worker for every hour worked in the enterprise. Only those whose main occupation is wage work or household enterprise work were used in the estimation.

**Figure 8:**   
Gender Wage Gap



**Source:** World Bank staff estimates based on the CSES 2015.

**Note:** Assumes that men and women are equal in terms of each characteristic and occupation/industry.

<sup>6</sup> This study also found that nearly 80 percent of household enterprise owners cited positive reasons for owning an unincorporated business, including earning a better income (34 percent), independence (14.6 percent), family tradition (9.9 percent), or the ability to balance personal and professional life (14.6 percent). Women were particularly likely to cite the last response.

## The current economic structure has served some populations better than others

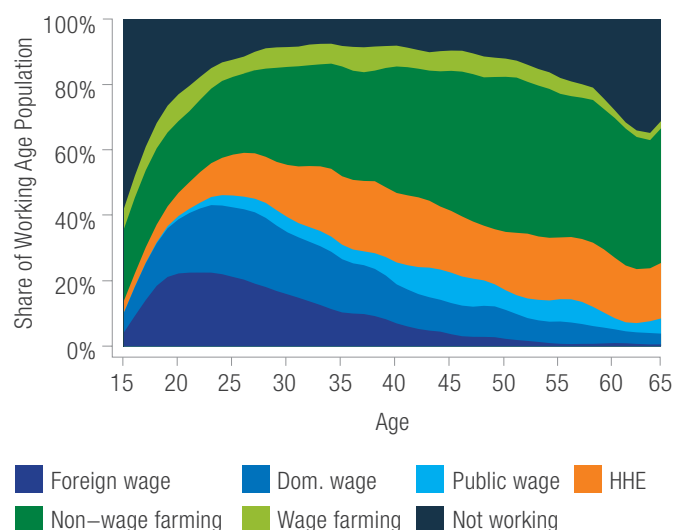
**Two in three jobs are excluded from the modern economy.** The modern and traditional sectors are weakly integrated, with the 60 percent of workers in family farming and household enterprises primarily trading among themselves. As will be discussed below, more traditional jobs grow alongside more modern jobs in Cambodia, but nevertheless very few formal links exist between them. This lack of integration limits the opportunities for improving the quality (for example, earnings and productivity levels) of jobs in the sectors with the largest employment shares.

**Modern wage-earning jobs are also concentrated in a few regions, largely due to geographic or economic factors.** Most of Cambodia's firms are located along two main corridors: Phnom Penh and its surrounding areas, which accounts for a quarter of modern jobs, and the southern part of the country, which accounts for 40 percent of these jobs. The other regions account for slightly more than a quarter, with the eastern region representing 5 percent of jobs.

**Cambodia's economy presents different opportunities and barriers to women and men.** The large garment and hospitality industries have been an ample source of jobs for women, with 17 percent of female workers being employed in the sector. The recent strong growth of the construction industry has benefitted men. Increased job opportunities for women has meant higher returns to education for women. The gender gap has shrunk from 30 percent for those with no education to 5 percent for the tertiary educated workforce. However, the average gender wage gap is similar to that in other economies. As of 2014, Cambodian women earn, on average, 85 cents for every dollar of wages earned by a male worker (Figure 8, the “actual wage gap”) compared with 88 cents in Vietnam (Cunningham and Pimhidzai 2018). The gap can be attributed to women's lower education levels, to household gender roles, and to the industry and occupation of employment; the expected earnings of women increase after controlling for these factors (Figure 8). However, even equalizing across these factors, there is still an unexplained gap with women earning an estimated 92 cents for every male dollar (Figure 8, “all factors”). This may be caused

by women taking less lucrative jobs within the same sector, women being more likely to trade off wage gains for non-wage benefits (Chowdhury et al. 2018), gender discrimination by employers, women's unequal bargaining power in wage negotiations, or a host of other factors that the data cannot capture.<sup>7</sup>

**Figure 9:** Source of Employment, by age



Source: Authors' estimates using CSES.

**While the school-to-work transition is a challenge for younger workers, older workers fare worse in the labor market.** Older workers are disproportionately employed in lower productivity family farming or in household enterprises compared to new labor force entrants (aged 15 to 24) (Figure 9). Young workers dominate private sector employment, both foreign and domestic—which often provides better wages—while the older population finds it difficult to transition into the fastest growing area of the economy.<sup>8</sup> Young people are particularly active in joining the fast-growing manufacturing and construction sectors. Only 10 percent of workers aged 45 to 59 work in these sectors as opposed to nearly one-third of workers aged 20 to 29. This disparity might exist because these jobs require skills and manual abilities that older workers have not acquired or can no longer achieve.

<sup>7</sup> Within the broad occupation categories and after accounting for education levels, women are more likely than equally educated men to be engaged in tasks that require fewer cognitive, managerial, and manual skills. Instead, women tend to work in occupations that use more interpersonal skills such as social perceptiveness.

<sup>8</sup> A similar trend was observed in Vietnam in the panel data that provide employment information for 2012 and 2014. The transition matrices show that youths (aged 16 to 24) have a higher propensity than any other age group for transitioning into formal sector wage employment, especially into jobs in the FDI sector. In contrast, older workers did not have a significant rate of transition into these sectors (Cunningham and Pimhidzai 2018).



## The Current Export Strategy May Not Deliver the Future Jobs to Which Cambodia Aspires

**Although the current export strategy has not yet reached its limits, it may not deliver the type of jobs that Cambodia wants and needs in the future.**

The returns to Stage I global integration (see Box 3) are decreasing as a result of: (i) weak employment growth partly driven by low productivity, high unit labor costs, and a low-skilled labor force; (ii) weak links between the FDI sector and the rest of the economy (where most jobs are); and (iii) the concentration of the country's exports in low sophisticated sectors. This implies that, for Cambodia to improve the quality and increase inclusiveness of its jobs, it will need to find a new engine of growth by moving up to Stage II of global integration.

## Weak employment growth in FDI and domestic firms challenges better jobs

**Given its sectoral composition and recent growth, Cambodia's apparel sector could be delivering more jobs.**

Indeed, the apparel sector is known to be labor-intensive compared to other sectors globally. Figure 10 plots the average employment elasticity (to sales) against per capita GDP for all garment firms across a range of countries. Here again, Cambodia stands at the bottom of the distribution with elasticity lower than in other countries at a similar level of economic development. This suggests that firms could be generating more jobs given the country's level of development and the sectoral composition of its growth (Figure 10).

### Box 3: The Stages of Global Integration for Development and Jobs

**Global value chains (GVCs) and the flows of foreign direct investment associated with them can provide developing countries with a short-cut to economic development and higher quality and inclusive jobs.**

However, becoming integrating into GVCs is not a one-off event but rather a cumulative, multi-stage, deliberate process.

**Stage I: Entering global production networks.** This involves leveraging the country's comparative advantage to attract foreign investors. This usually means offering: (i) abundant, low-skilled labor; (ii) a friendly business climate for tangible and intangible assets; (iii) few regulatory or restrictive measures on trade and investments; and (iv) a stable regulatory and political environment to attract multinational corporations that will provide low value-added jobs in GVCs.

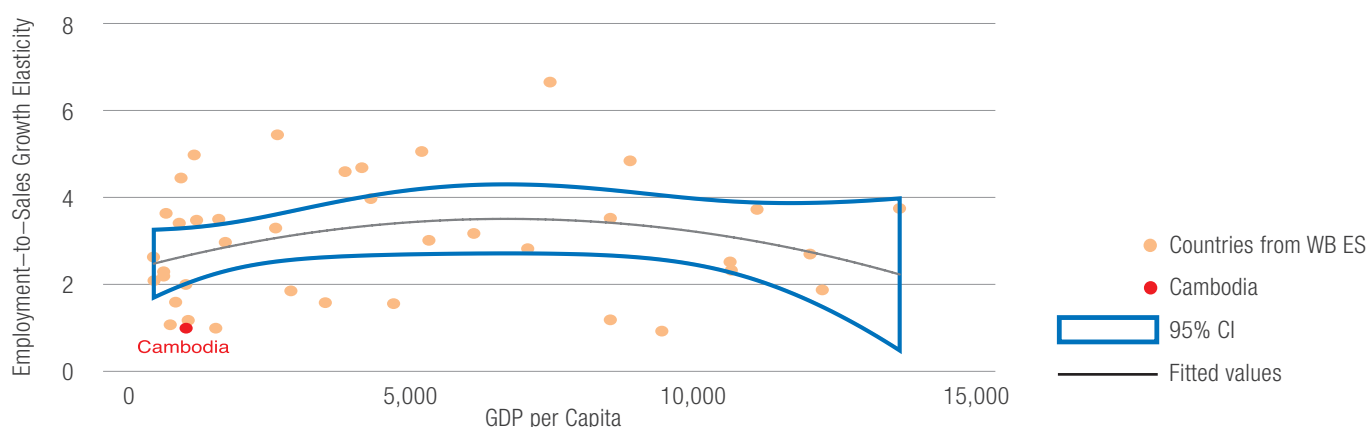
**Stage II: Attracting higher value-added FDI and increasing domestic densification.** Countries can expand and strengthen their participation in GVCs by becoming competitive in higher-value-added products, tasks, and sectors. Densification—engaging more local actors in the production network—is also desirable at this stage. Not only will domestic private firms benefit from doing business with multinational corporations, but it will also give them an opportunity to learn and to increase their productivity-led growth. In order for an economy to move into this stage, it will need a labor force with the relevant skills, absorptive capacity, and strong links between domestic firms and GVCs.

**Stage III: Sustainability.** Once an economy is at this stage, the domestic sector is sufficiently robust that it does not depend on the presence of FDI firms. In fact, as China has shown, domestic firms may have become the lead companies in GVCs. However, in order to sustain the GVC-centric approach to development, policymakers need to pay keen attention to the macroeconomic, social, and environmental sustainability of the economy's global integration.

**Source:** Taglioni and Winkler (2016)



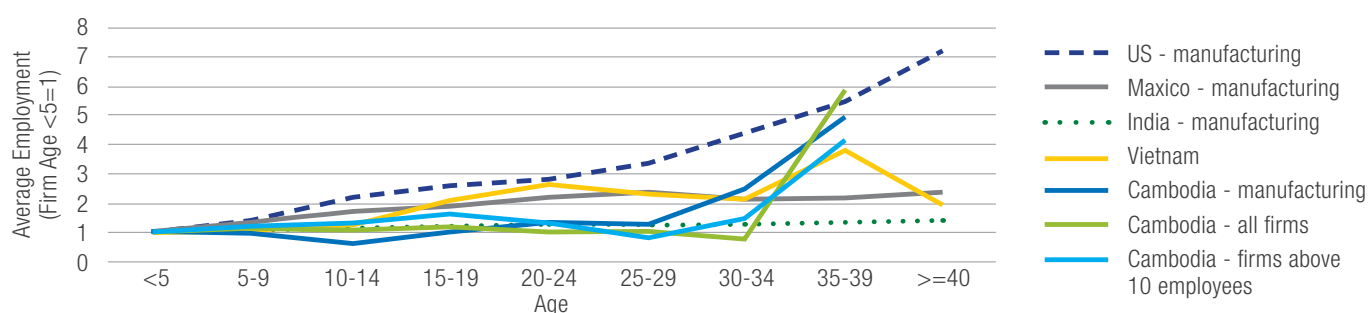
**Figure 10:**  
Employment Elasticity to Sales Growth for Apparel Firms



**Source:** World Bank Enterprise Surveys that contain a large share of garment firms.

**Note:** The “employment-to-sales growth elasticity” ( $\epsilon$ ) is the percent increase in employment for every 1 percent increase in sales. Thus,  $\epsilon = 0$  means that employment is not responsive to sales growth while  $\epsilon = 1$  means that employment growth is exactly equal to sales growth. The figure shows that employment is not very responsive to sales growth in Cambodia, even when compared to countries of similar level of development.

**Figure 11:**  
The Lifecycle of a Firm



**Source:** Author's calculations for Cambodia. Hsieh and Klenow (2014) for India, Mexico, and the US.

**Note:** The base is a firm that has been operating less than five years. The graph plots the relative size of firms at different ages relative to the base firm in Cambodia, Mexico, India, the US, and Vietnam

**The possible loss of trade preferences in the near term would also hamper Cambodia's competitiveness in key export markets.** Cambodian exports currently have preferential access to the US market under the Generalized System of Preferences (GSP) and to the EU market under the Everything But Arms (EBA) scheme. This preferential access is granted based on Cambodia's level of economic development. As the country continues to climb the development ladder, this preferential access can be expected to be withdrawn. Furthermore, Cambodia's special access in the EU market may be lost much sooner as the European Commission recently informed Cambodia that it launched a procedure to temporarily withdraw tariff preferences granted under the Everything But Arms (EBA) arrangement over concerns related to serious human and labor rights violations. This will have an immediate negative impact on Cambodia's competitiveness in the EU market,

which accounts for 40 percent of the country's merchandise exports and enables it to pay zero tariffs.

**Cambodia's domestic sector is similarly stunted.** Cambodia has many young firms. Nearly 60 percent of firms have been operating only for between one and five years, which is among the largest shares in an 18-country comparison of developing economies. These firms are a significant source of job creation in Cambodia, in that they employ a higher share of the workforce than all but one other country in the sample. However, those young firms tend not to grow. The size of their labor force remains the same for up to 30 years, unlike new firms in Mexico and Vietnam, which start to grow from early on in their development (Figure 11). The stagnant growth of Cambodia's domestic firms can be attributed to the limited skills of the workforce, high production costs, the high costs of doing business, and a lack of entrepreneurial capability.

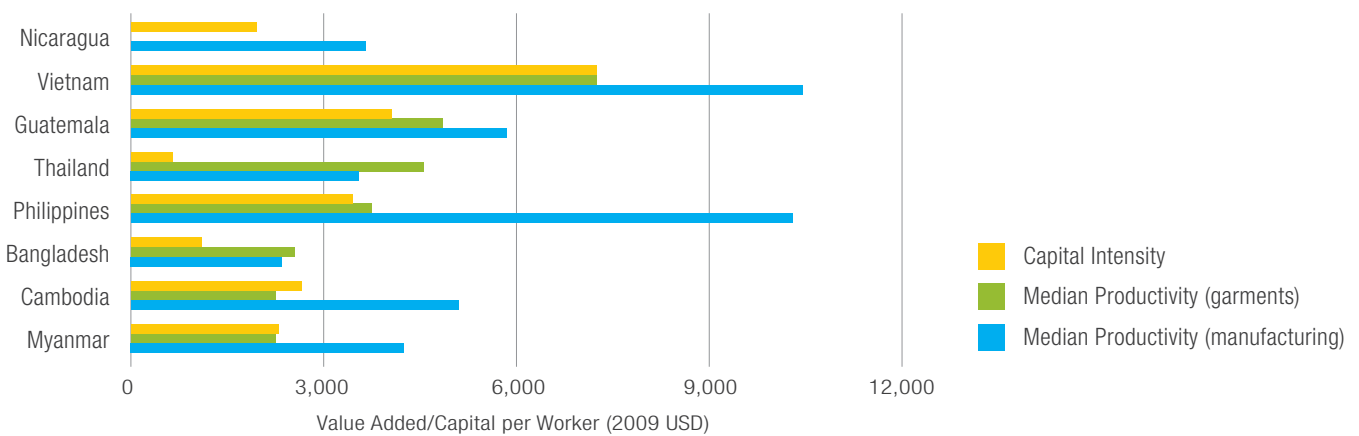
Labor productivity lags behind other countries' and unit labor costs are high

Compared to other countries, Cambodia's productivity levels and labor productivity growth are disappointing.

Firm productivity in Cambodia's manufacturing and garment sectors is on a par with that of Myanmar and Bangladesh, but lags far behind that of Vietnam and the Philippines (Figure 12). This is due to a range of factors. First, Cambodia has a history of slow labor productivity growth, which averaged only 3.6 percent in the 22 years between 1993 and 2015 compared to annual productivity gains of 5 percent in Vietnam and 7 percent in Thailand during the same period. Second, the value-added associated with Cambodia's export basket is lower than it should be given Cambodia's level of development and has been falling over time, with textiles having particularly low productivity gains. In fact, labor productivity in garments and construction—two of the

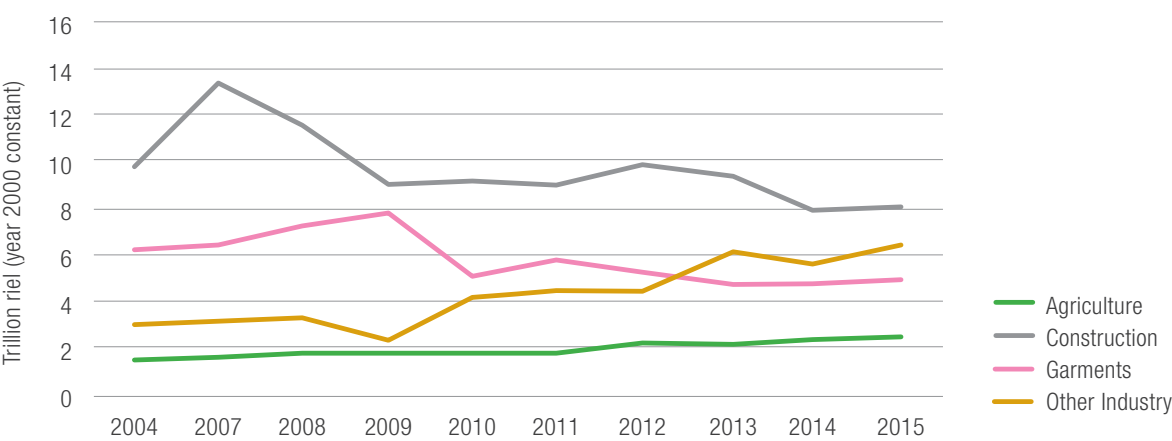
fastest growing sectors—actually declined between 2005 and 2015 (Figure 13). Third, recent productivity gains have been fueled by the real estate and the financial sectors rather than by more productive sectors. Fourth, Cambodia's business environment may be constraining investment and job creation. Sound business regulations are important for a thriving private sector and essential for the health of an economy as a whole, but Cambodia's regulatory regime is generally not conducive to the establishment and growth of businesses, especially SMEs. While the country has significantly improved its investment climate, it still lags behind many other countries, both regionally and globally, in terms of the ease of doing business. Cambodia ranked 138th out of 190 economies in terms of "ease of doing business" in the *Doing Business 2019* report (World Bank 2019). An investment climate assessment undertaken for Cambodia by the World Bank in 2018 identified a number of challenges that are discussed in Box 4.

Figure 12: Firm-level Productivity and Capital Intensity, 2016



Source: World Bank Enterprise Surveys.

Figure 13: Productivity in Agriculture and Industry



Source: Author's calculations using national accounts, CSES, and ILO data sets.

#### Box 4: Cambodia's Investment Climate Assessment

In 2018, the World Bank carried out an investment climate assessment for Cambodia that focused on regulations that affect business start-ups and operations, trade costs, and links between FDI firms and small and medium-sized enterprises.

The assessment found that the high costs involved in establishing and operating firms are the most binding constraint to private sector development and sustained growth in Cambodia. The country is one of the most difficult places in the world to register a business and receive a construction permit, ranking 185th and 179th respectively for “starting a business” and “dealing with construction permits” out of 190 countries on the World Bank’s 2019 Ease of Doing Business Index. This makes it clear that the current regulatory framework for business in Cambodia needs modernizing.

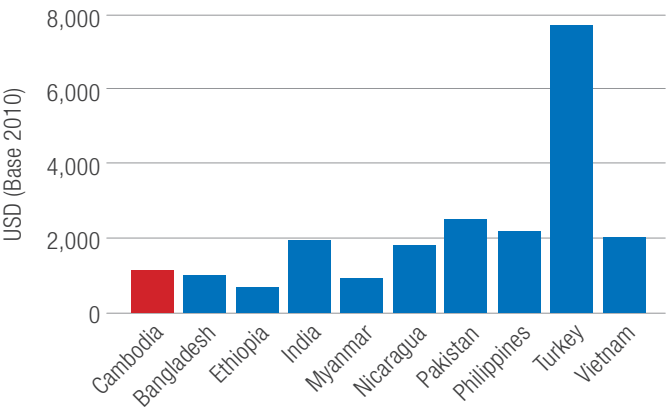
Trade costs make up a significant share of the total operating costs of Cambodia’s importers and exporters, particularly FDI firms, most of which are export-oriented. Transport and logistics contribute 14 percent of total exported value-added from Cambodia, both directly and indirectly through forward links. This is double the size of the contribution of these sectors in Thailand and three and a half times of those in Malaysia or Vietnam. Reducing trade costs will not only enhance the competitiveness of existing FDI firms but may also attract more sophisticated FDI into the country.

Cambodia has the fewest links between FDI firms and SMEs both in the region and globally. Foreign-owned manufacturing firms in Cambodia imported about 95 percent of their production inputs, by far the most among Cambodia’s peer countries. Supply chain links do not happen automatically but tend to be a function of multiple factors including the spillover potential of FDI, the absorptive capacity of domestic firms, and the host country’s investment climate and institutional environment. The assessment found that there is clearly much potential for increasing FDI spillovers into the domestic market.

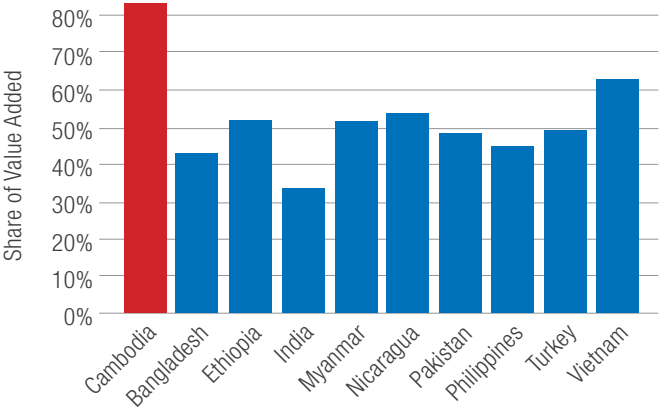
Source: World Bank (2018b)

**Figure 14:**  
Average Wages and Unit Labor Costs in Apparel Firms

(a) Average Wages



(b) Unit Labor Costs



Source: World Bank Enterprise Surveys

**Unit labor costs, rather than wages, may be constraining the further expansion of jobs in the garment and other export-oriented sectors.** The rapid increase in the minimum wage in recent years has successfully closed the wage gap between garment sector workers and those in other sectors. It has also put Cambodia’s garment sector wages on a par with the global norm for

countries at Cambodia’s level of development (Figure 14a). However, productivity in the garment sector has not increased proportionately. Instead, unit labor costs—the cost of workers per unit of production—are currently significantly higher in Cambodia than in other garment-producing countries, putting Cambodia at a competitive disadvantage (Figure 14b).

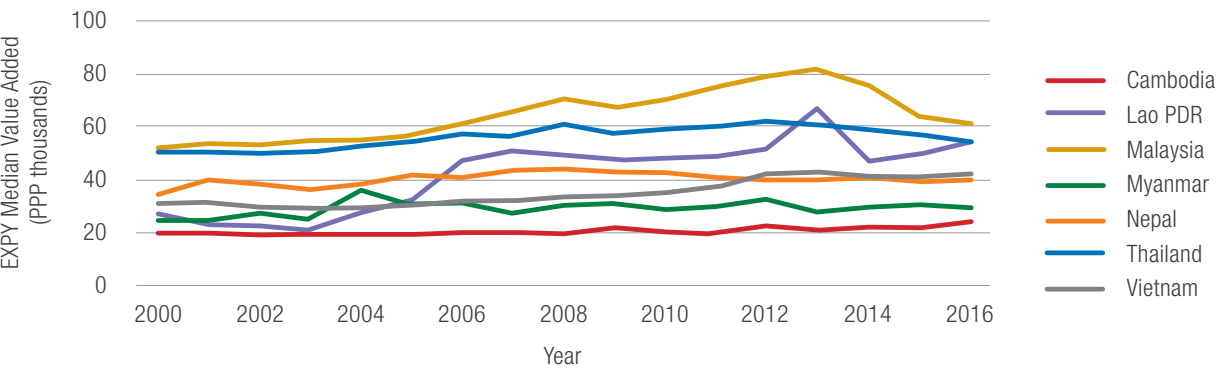
## Exports are concentrated in low-value activities

**Cambodia’s exports, and export jobs, are concentrated in low value-added segments of GVCs.<sup>9</sup>** Cambodia’s current position in the value chain may not be able to deliver the future jobs to which Cambodia aspires. The majority of FDI firms in Cambodia are export-oriented and efficiency-seeking, and they have overwhelmingly reported that low labor costs, tax incentives, and tariff preferences were their top reasons for selecting the country as an investment destination (World Bank 2018b). Many FDI firms are in the

low-quality, low sophistication, and highly substitutable garment sector.

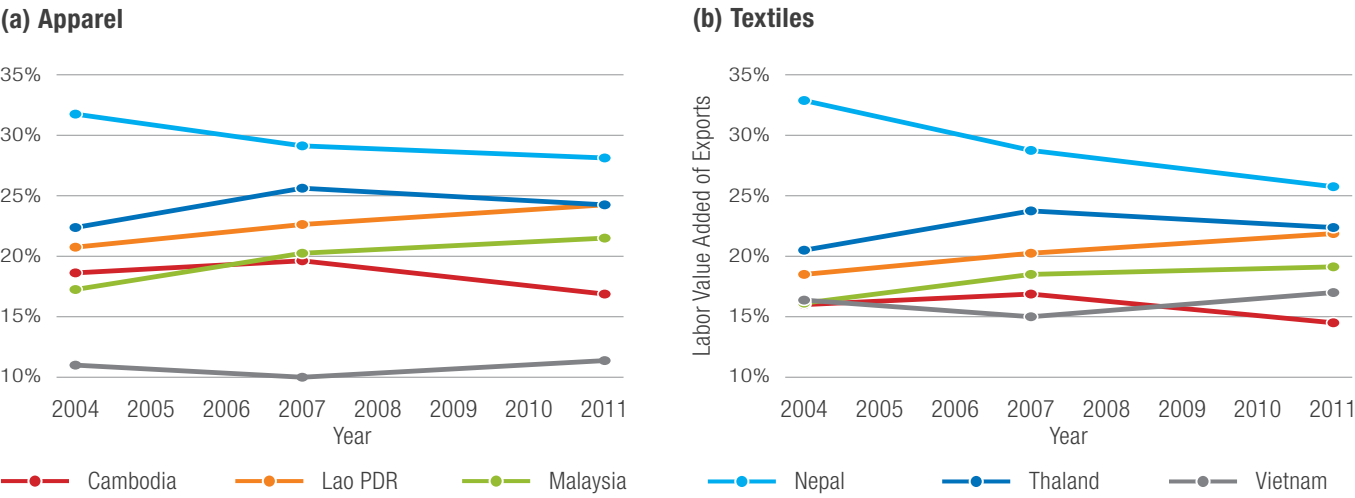
**The country’s underperformance on jobs can be attributed to the low level of sophistication of its exports compared to its regional peers.<sup>10/11</sup>** For example, Cambodia’s export basket contains more low value-added products than the export baskets of its peer countries (Figure 15). This is partly due to Cambodia’s heavy reliance on the apparel sector in its export basket. Even in textiles and apparel, Cambodia’s exports pay a lower labor remuneration rate for every unit of exports than do those of other comparator countries (Figure 16).

**Figure 15:** Median Value-Added of Exports



**Source:** World Bank staff calculations using data from UN Comtrade, the World Bank’s Business Environment and Enterprise Performance Surveys, and Shirotori et al (2010).

**Figure 16:** Total Labor Content Share of Apparel and Textiles in Gross Exports



**Source:** World Bank staff calculations using LACEX database.

<sup>9</sup> Global value chains can be defined as a production process in which the separate activities to take a product from idea generation to final purchasing may take place in several different countries.

<sup>10</sup> The labor sophistication of exports is a weighted average of export labor market outcomes such as the median wage, the median value-added per worker, the ratio of skilled to total workers, output per employee, years of schooling, and capital stock per worker.

<sup>11</sup> These regional peers are Lao PDR, Malaysia, Myanmar, Nepal, Thailand, and Vietnam.

**Although the export sector and FDI firms create more jobs per firm than non-exporters and domestic firms, experiences in other countries suggest that higher value-added jobs could be extracted from these sectors.** This would enhance the inclusiveness of Cambodia's jobs since workers in FDI firms tend to be female and young. While these firms have higher productivity and, more recently, better wages and work conditions than other businesses in Cambodia, they still lag behind those of other countries.

**Low skill levels and returns to education underpin low labor productivity**

**Cambodia's low labor productivity can partly be attributed to the particularly low skill level of its labor force.** Eighty-five percent of today's labor force has not completed secondary school, averaging only 6.3 years of education, and this education is not very good. Workers who have only one year of education and those with 11 years of education have similar levels of wages. Only those who completed secondary school receive any labor market rewards for their higher education attainment (Figure 17).

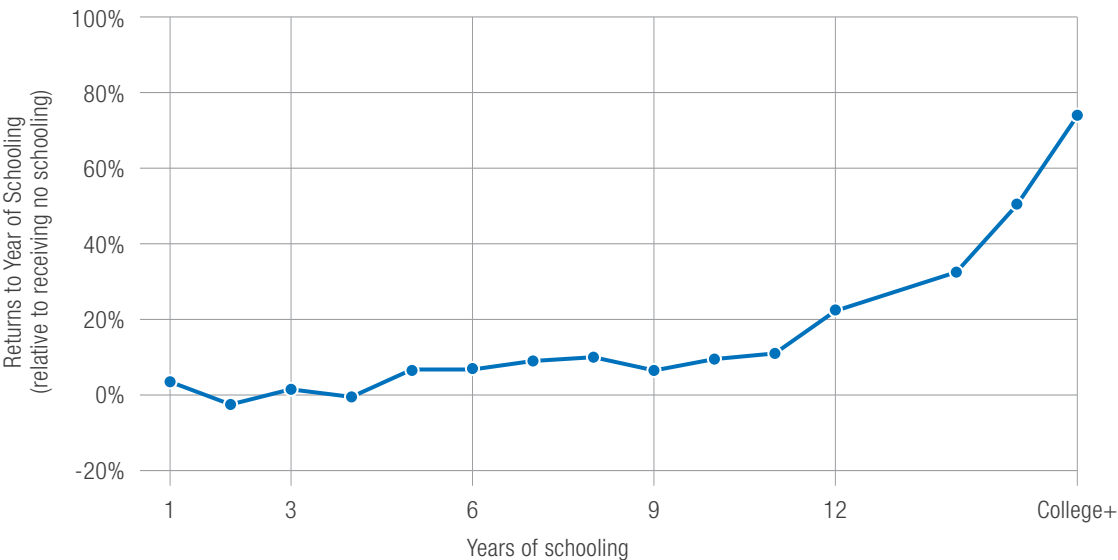
**Cambodia's firms are affected by the low skill level (and low productivity) of the current workforce.** More than 17 percent of firms surveyed by the World Bank's Enterprise Surveys identified an "inadequately skilled labor force" as a constraint to doing business, surpassed only by Lao PDR in East Asia (Figure 18). The firms require a mix of hard and soft skills and specified foreign language

skills, teamwork, problem solving, and managerial skills as especially important for jobs in large firms. Small and medium-sized enterprises, exporters, and foreign firms (in SEZs) are particularly affected by the low-skilled labor force. The lack of skilled labor not only hinders production and reduces current profits, but it also slows down business development (because of delays in R&D) and leads to bad conditions for workers who have to take on a large workload. In short, the current workforce does not have the right skills for the current jobs market.

**Low labor productivity is also exacerbated by the low level of investment.** Rather than investing in capital that complements and raises the productivity of labor, FDI firms in Cambodia mostly use labor as the main production factor.

**The skills deficit is a structural constraint to increased labor productivity owing to the lack of an effective skills development system to upgrade the skills of the *existing* labor force.** Assuming that today's educational attainment improvement rates continue into the future, only half of Cambodia's labor force will have completed secondary school by 2045. This suggests that the education system is not a solution to the current stock of workers, who will constitute the largest share of Cambodia's workforce for many generations. Instead, the skills of today's workers need to be quickly upgraded to meet labor demand. However, Cambodia's public and private skills development system is fragmented and small (Figure 19), and reform efforts so far have focused on setting standards rather than developing feedback mechanisms from the ultimate clients

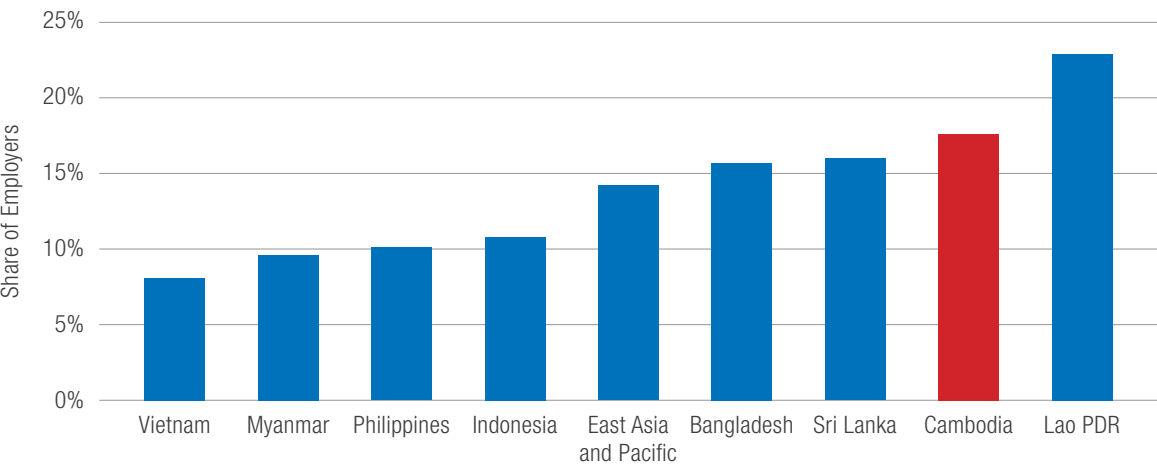
**Figure 17:**  
Rate of Return to Education



**Source:** World Bank staff calculations using CSES 2014

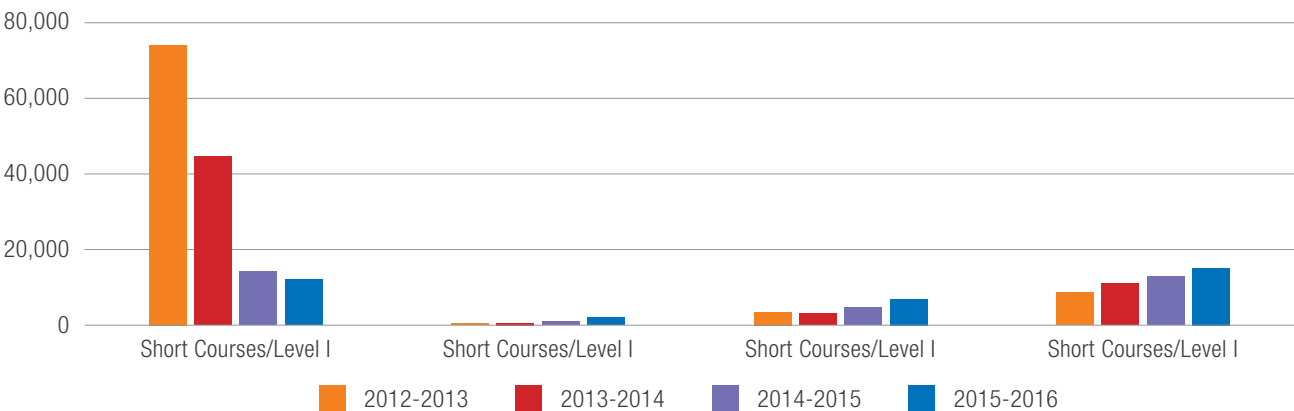
**Note:** Y-axis graphs the estimated increase in earnings of each additional year of education.

**Figure 18:** Share of Employers Who Are Affected by An Inadequately Skilled Labor Force



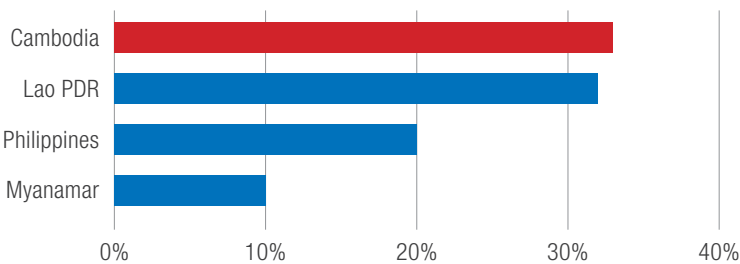
Source: World Bank’s Enterprise Survey, 2016

**Figure 19:** TVET Enrollment



Source: Ministry of Vocational Training and Labor, 2012-2016

**Figure 20:** Percentage of Second Grade Students who Perform below Proficiency on Reading Assessments (EGRA)



Source: Adapted from World Bank (2018a).

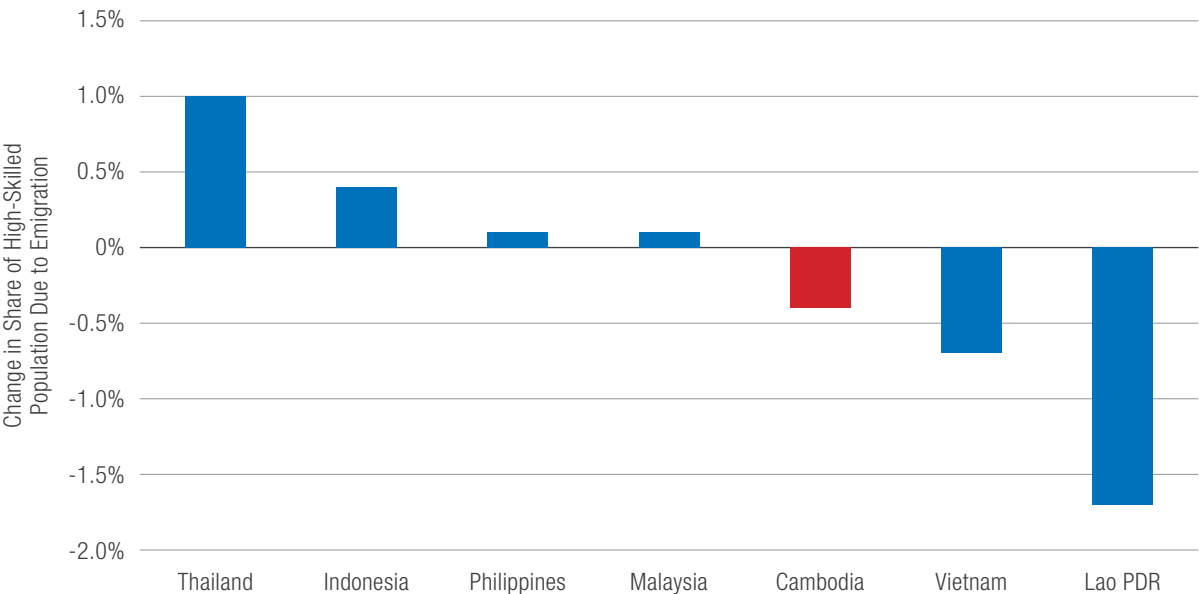
Notes: The Early Grade Reading Assessment (EGRA) measures the percentage of students in second grade who are unable to read a word. The assessments were done in Cambodia (2012), Lao PDR (2012), Myanmar (2015), and the Philippines (2014).

(the employers) or creating results-based incentives for training institutes. Only 22 percent of registered Cambodian employers offered formal training courses, compared to an average of 57 percent in the East Asia region as a whole.

**The education system is not producing a future labor force that will be able to meet Cambodia’s future jobs challenges.** While educational attainment is increasing, the quality of education is lagging far behind. All second-grade students should be able to read basic text, but one-third of Cambodia’s second graders cannot read one word—which means that they are performing even worse than students in Cambodia’s less-developed neighboring countries (Figure 20). Furthermore, over half of Cambodian sixth-graders have a “below basic” knowledge of mathematics. This poor-quality education is eroding the gains made in educational attainment. While four-year-old Cambodian children today are expected to complete 9.5 years of school, their learning will be equivalent to only 6.9 years of school in other countries as a result of poor educational quality. The quality of schooling is much worse in rural areas than in urban areas. As jobs become more knowledge-intensive (Figure 6), Cambodia’s new workers will be at a particular disadvantage by being unable to engage and thrive in these jobs.

**While internal migration may have been necessary for the rapid growth of manufacturing jobs, international emigration from Cambodia exacerbates the skills shortage.** Nearly 90 percent of internal migrants surveyed in the year 2011 had moved for jobs (MoP 2012), and both men and women found them in urban areas and in other countries. Nearly 1 million Cambodian citizens are living outside of Cambodia (Testaverde et al. 2017). Both internal and international migrants tend to have completed higher levels of education than those who do not migrate. Recent estimates suggest that 15 percent of Cambodian tertiary graduates have migrated to OECD countries. Migration has resulted in a net drain of Cambodia’s human capital (Figure 21). Most migration is through informal networks, with half of migrants following earlier migrants from their own communities. This may lead to poor job matching upon arrival, as the migrant’s job options are likely to be limited. While migrants, particularly women, send money home in an amount equal to 3 percent of GDP in the year 2015 (Roth and Tiberti 2017), it is not clear whether the recipients use these resources to invest in and enrich the local economy or whether they simply use them to fund consumption. Furthermore, the extent of return migration and their job-related activities are largely unknown.<sup>12</sup>

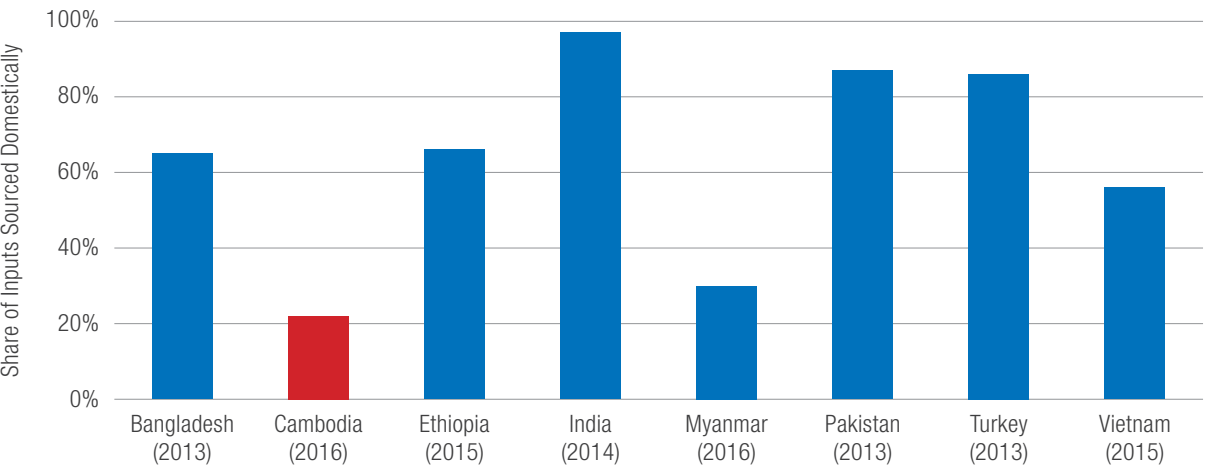
**Figure 21:** Net Effect of High-Skilled Emigration on the Share of High-skilled Workers in ASEAN Source Countries



**Source:** Beine, Docquier, and Rapoport 2008.

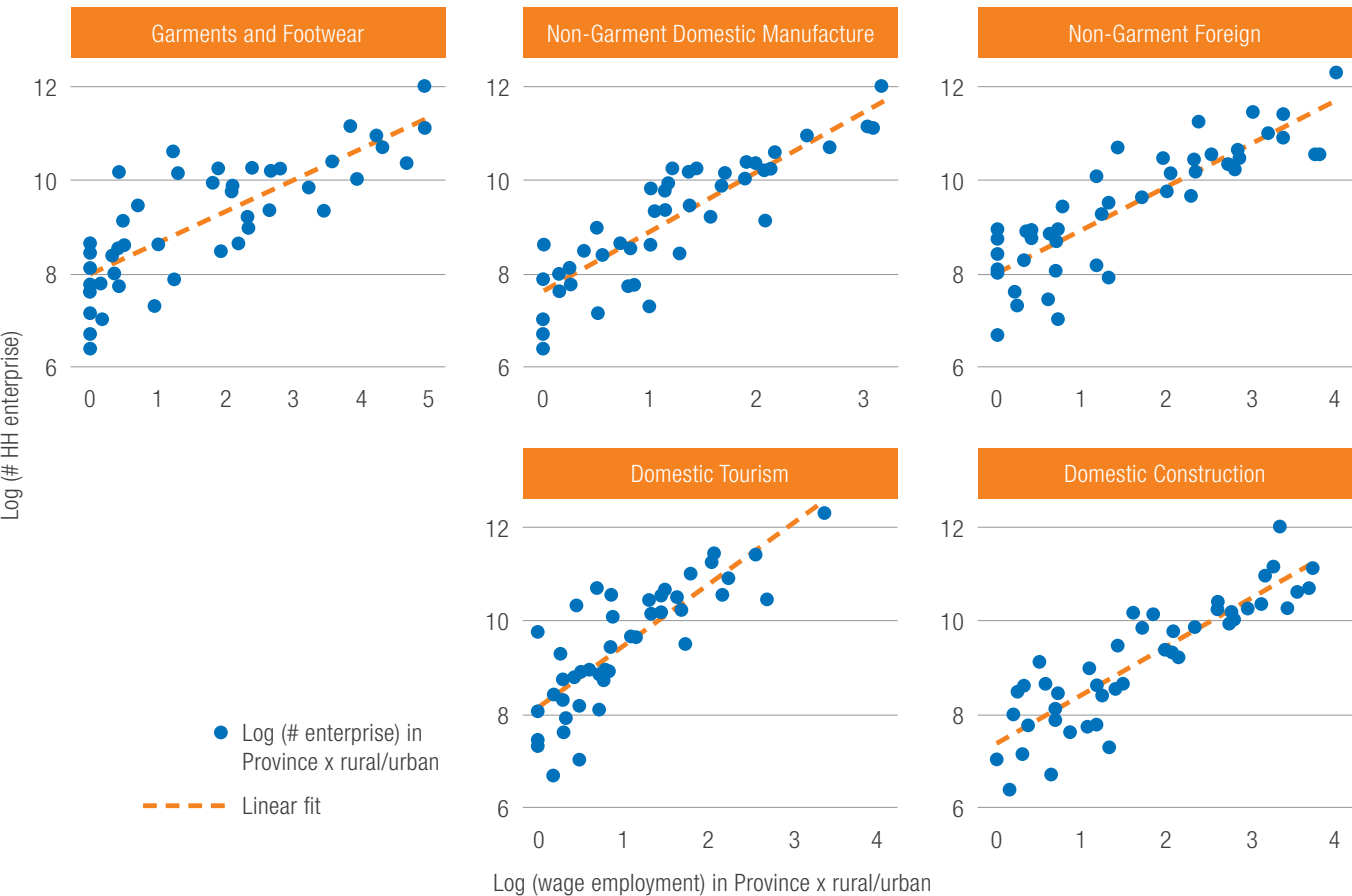
<sup>12</sup> Though migration is an important component of the Cambodia jobs story, this report does not include additional analysis on this subject due to an absence of relevant data.

**Figure 22:**   
Inputs and Supplies Locally Sourced by Garment Firms



Source: World Bank's Enterprise Surveys.

**Figure 23:**   
Correlation between Wage Employment and the Number of Non-farm Enterprises



Source: Author's estimates from Cambodia SES 2014.

Note: The regression line is weighted by the population of the rural/urban cells of each province. The title of the subplot represents the change in a particular wage employment type.



Links with the domestic sector are weak

**Cambodian foreign-owned firms have comparatively low spillovers to domestic firms.** Two-thirds of the value (and related wages) created through exports is derived from jobs that produce goods (or services) for direct export. The other one-third of value is created in domestic firms that provide inputs to exporting firms (local sourcing). In Vietnam, the shares are half and half, suggesting that Cambodia’s exporters are creating fewer job opportunities among local producers than they could.

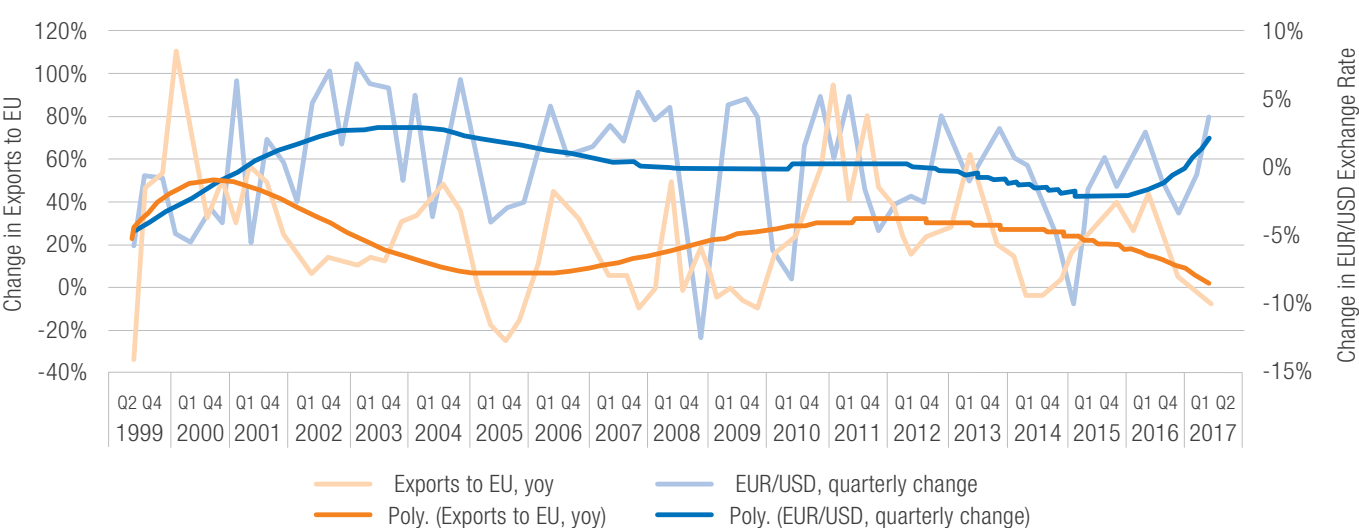
**The weak links between FDI firms and local suppliers are partly driven by the dominance of the garment industry in FDI.** It is common for FDI firms in the garment sector to source from their global suppliers rather than domestic firms. However, even within the garment industry, they have weak links with the local economy. Only 25 percent of Cambodia’s garment firms buy inputs and supplies from local providers—which themselves may or may not be Cambodian—compared with 60 percent in Vietnam, 62 in Bangladesh, and almost 100 percent in India (Figure 22). Instead, Cambodians FDI garment firms import nearly all of their inputs from neighboring countries, which are then assembled in Cambodia and exported to the US and European markets as final products. Thus, there is little value addition taking place, undermining the support that exports give to workers in Cambodia.

**Cambodia is in a position to support more jobs through domestic links with exporting firms than it currently does.** Cambodia has greater indirect export

activity than other exporters in the region. In 2016, 4.4 percent of firms in Cambodia supplied inputs for export production compared with an EAP average of 3.7 percent. However, the percentage of total inputs and supplies sourced domestically is low in Cambodia compared to the region, both in textiles (as noted above) and overall. For example, only 20 percent of inputs are locally sourced in Cambodia compared to closer to 60 percent in Vietnam and 40 percent in Myanmar. Increasing these links with domestic suppliers will not only create more jobs, but may also help retain FDI firms in Cambodia.

**Private sector employment, including in foreign-owned firms, can also promote household enterprises.** Those provinces in Cambodia with the most garment factories also have more household enterprises, as it has been found that provinces with 10 percent more garment workers have 1 percent more household enterprises. These household enterprises may cater indirectly to the industry by providing goods and services to the workers in the firms, or they may benefit generally through greater economic activity in these provinces that have plentiful wage work. For example, areas with many garment factories also have a higher incidence of household enterprises engaged in retail and transportation. Also, areas with many domestic-owned manufacturing firms have a higher incidence of household enterprises in retail and manufacturing. Similarly, tourism promotes retail shops and enterprises in the hospitality sector (Figure 23). Private enterprises generate indirect links as well by providing goods and services for consumption by workers in these factories. The growth of the private sector is also associated with growth in household enterprises.

Figure 24: Export Growth to the EU and EUR/USD Exchange Rate



Source: European Central Bank, IMF Directions of Trade Database.

## Macroeconomic risks also create jobs risks

**Cambodia has been able to maintain strong growth and macroeconomic stability under dollarization, but this may hinder the jobs strategy going forwards.**

The limitations of dollarization for Cambodia have become apparent as the European Union has become the country's main trading partner. US dollar fluctuations significantly impact the external sector, which employs around 16 percent of all Cambodian workers. The US dollar's recent appreciation vis-à-vis the euro and other currencies resulted in a decline in Cambodian garment exports to the EU (Figure 24). It has also reduced the tourist trade because it has made trips to Cambodia more expensive for non-American tourists. This has negatively affected the pace of job creation in these sectors, as well as the prospects of creating jobs in Cambodia's emerging manufacturing clusters. Dollarization has also been fueling flows of capital and credit into the non-tradable sector, with the recent increase in capital formation being driven by investments in construction rather than machinery and equipment. This puts Cambodia's macroeconomic stability (and jobs) at risk, especially in the absence of an independent monetary policy.

## Mega-trends may catalyze the economy's move to Stage II and better jobs

**Emerging external forces can alter Cambodia's jobs picture in the future.** These mega-trends can erode Cambodia's investment position and threaten FDI-related and domestic jobs, but they could also provide an opportunity for Cambodia to move into Stage II of global integration characterized by higher value-added investment and jobs. Four mega-trends are particularly relevant in the Cambodia context.

**First, changing consumption patterns resulting from higher urbanization and a growing consumer class within Cambodia and Asia will shift the composition of domestic demand and export demand.** By 2030, more than 90 percent of developing Asian households are expected to have enough income to allow for discretionary consumption, meaning that they can cover their basic needs and still have some money left over. Urbanization means that households will buy food and services that in the past they may have produced themselves. They will also spend a higher share of their income on services rather than on food or other basic necessities. This has two implications for Cambodian jobs. First, domestic demand will shift toward more, different, and higher-value goods and services than in the past. Second, regional trade patterns will shift to accommodate wealthier and more urban East Asian

populations, which means potentially more and higher value jobs for Cambodia.

**Second, several new countries entering GVCs, along with emerging technologies and shifting trade agreements will affect global trade patterns.**

Labor-intensive manufacturing is moving out of China, which will open up opportunities for other developing countries, including Cambodia. However, the new countries participating in GVCs have vast and rapidly growing labor forces in industries where Cambodia currently holds a comparative advantage, thus challenging Cambodia's position.<sup>13</sup> Also, digitalization may reduce the advantages of producing GVC goods in economies with low labor costs and may reorient global production and trade back towards sources of demand. At the same time, production may become increasingly concentrated in regional or local hubs closer to end markets, thereby strengthening regional rather than global value chains. Outward FDI from Asian investors (particularly from China) into other developing countries has become a much more significant share of global FDI, suggesting that this could be a source of new FDI to diversify Cambodia's exports. The emergence of these new Asian investors is happening at the same time as Cambodia faces the threat of the loss of the tariff preferences that it currently enjoys from the EU in the short term and the US in the medium term. These trends will shape Cambodia's future participation in GVCs, which is a core feature of its export-oriented growth strategy.

**Third, automation has the potential to create more, better, and more inclusive jobs—but also to make others disappear.** Production processes in industries that have been a standard phase of the global integration process—such as automobile production—have become heavily automated, thereby displacing labor. However, technology is creating better jobs in other industries. Machines are improving production processes, such as the pattern cutting technology in the apparel sector or improved food processing facilities that better meet international food safety norms. The creation of machines in the rapidly growing electronics industry is a new source of better jobs as well. Mobile phone technology and the internet are unlocking new markets and efficiency-saving tools for small producers, even among household enterprises and family farmers. While technology will replace low-skilled, routine jobs in the future, this is still a long way off in the industries that the government hopes to nurture, since these machines do not yet exist, are not cost-effective, or are not sufficiently flexible (Box 5). Machines will eliminate some jobs, but the greater change will likely be that the tasks carried out within jobs will become more sophisticated, thus requiring workers to have higher-level skills and a broader range of skills.

<sup>13</sup> For example, Myanmar in East Asia Pacific is attracting new FDI in the garment sector, and Ethiopia is also starting to expand its manufacturing assembly activities.

### Box 5: The Rise of the Sewbots? Maybe Not Quite Yet...

Recent publications have estimated that East Asia's garment jobs will be wiped out by machines in the next 15 years. This is certainly a frightening prospect, given that this USD 5 billion industry is the source of 80 percent of Myanmar's exports (2015) and of more than 850,000 jobs. However, a closer look at the apparel industry suggests that these predictions of job losses may be excessive, especially in the short run. The jobs that cannot be automated—the production of specialized apparel and knowledge tasks that are higher up the value chain—will still exist. Also, a host of new jobs will be created, for example, in running and repairing the machines, programming machines to accommodate new styles, and designing shop floors to be machine-friendly.

Several factors need to come together for machines to begin replacing humans, none of which are yet occurring in the apparel industry:

1. **The existence of machines to replace labor.** While technology is being employed in some parts of the apparel GVC, there is still no machine that can replace the cut-make-trim (CMT) process that employs 70 percent of garment workers as sewing machine operators. While the first CMT machine is expected on the market in 2019, it can only produce the most basic garment, an 8-step tee-shirt quite distant from the 78-step dress.
2. **Repetitive tasks with few changes.** Fashion changes quickly. While people can easily learn to stitch a new angle, stretch a new fabric, or add a new adornment, machines will not have that flexibility for many years.
3. **High labor costs relative to the cost of machinery.** Although labor costs are increasing in Vietnamese garment factories, they are still low compared to the cost of machines. While the CMT machine for tee-shirts is estimated to be able to pay for itself within two years (of displaced worker wages), the machine itself will need to be replaced frequently as fashion changes.

Sources: ILO (2016), Frederick (2017), <http://softwearautomation.com/>

### Fourth, Cambodia is a young country in an aging region, which means that new and better job opportunities are likely to be increasingly available in neighboring countries with shrinking labor forces.

The size of the labor force has peaked in most of Cambodia's neighbors such as Thailand, Vietnam, and China. Wealthier countries, such as Singapore and Japan, have already moved beyond their peak and are now suffering from labor shortages. This is an opportunity for Cambodian workers to find jobs in countries that pay higher wages and may require higher skills. This could be beneficial to Cambodia if it puts in place mechanisms to attract these workers back to Cambodia after they have increased their skills.

### Policy for a Jobs Future Consistent with Cambodia's Vision 2050

**While current trends predict a somewhat sluggish jobs picture, emerging mega-trends present Cambodia with new and better job opportunities provided that policies are put in place to take advantage of those trends.** This report proposes a two-pronged strategy for creating better jobs in Cambodia: (i) getting more out of FDI and (ii) aligning the domestic agenda with jobs goals. These are inter-related. The key to upgrading Cambodia's

jobs is to move to Stage II of global integration, which will involve attracting higher-value FDI, supporting links between exporting firms and input-supplying firms, and upgrading worker skills. Doing so will require policymakers to adopt policies designed to attract higher-quality foreign investment and to prepare Cambodia's workers and domestically-owned businesses to leverage better jobs from this investment. This will only be effective if Cambodia focuses on building competitiveness at home by instituting policy reforms in the short and medium term aimed at creating more, better, and more inclusive jobs.

### Seven sets of policies can help firms, workers, and foreign investors to overcome the constraints that are preventing the creation of higher-value FDI jobs and of FDI spillovers into jobs in the domestic economy.

The analytical analysis underpinning this report identified the key challenges to upgrading Cambodia's jobs and also areas where policy intervention is needed. We selected policies to overcome these challenges based on existing analytical work within Cambodia as well as other countries' experiences in overcoming similar challenges. These policies are designed to complement sectoral policies and were chosen because each meet the criteria of being impactful, feasible, sustainable, and measurable. Moreover, these policies overlap with all four rectangles in Phase IV of the Rectangular Strategy as well as with the "environment" and "core" policies. The

**Figure 25:**   
Seven Policies for More, Better, and More Inclusive Jobs in Cambodia



matrix in Annex I maps the policy options in this document to those in Phase IV of the Rectangular Strategy and also identifies the government agencies that could take the lead in each policy area. The successful implementation of these proposed policies will also require strong coordination across government.

### 1. Diversify Exports and FDI into Higher Value-added Value Chains (or Segments of Value Chains)

**Diversifying Cambodia’s export basket to include more higher-value activities could attract more productive jobs that pay higher wages.** In order to encourage the creation of better jobs, policymakers will need to focus on policies to attract jobs-friendly FDI (from global or emerging regional markets) and to move the economy into higher value-added value chains (or segments of value chains), including services for export. Specifically, they will need to reduce the costs of imports and exports, which can be done in several ways, including: (i) modernizing procedures in trade facilitation; (ii) developing logistics infrastructure; (iii) simplifying border processes; (iv) providing new types of incentives that target specific investments; and (v) creating quality assurance facilities. Policymakers also need to explore ways to maintain Cambodia’s preferential access to key markets for its new labor-intensive exports as the end-dates of the US and European preferential access treaties draw nearer.

**In the short run, the following policy directions should be prioritized:**

- Shifting away from tax holidays towards streamlined incentives aimed at attracting private investment in machinery, such as tax credits on capital investment and

technological transfers. These incentives will help firms upgrade their production processes, thereby increasing investment in the domestic economy and increasing labor productivity.

- Reviewing and streamlining customs requirements and the clearance process for export and import licenses. This will help to save time and reduce costs for traders, thus making Cambodia’s exports more competitive in global markets.
- Signing, finalizing, and enforcing international trade and investment agreements with Cambodia’s key trade partners to diversify across destinations as well as products. Securing preferential market access will help this.

**In the medium term:**

- Introducing super tax deductions for R&D and staff training to incentivize firms to undertake these activities. These investments will not only yield returns for investors, but they are also expected to generate spillovers to the domestic economy through knowledge and technological transfers.
- Automating the process of sanitary and phytosanitary certification while fostering more use of IT. By meeting global certification standards, Cambodia will not only ensure the high quality of agricultural goods but will also support agricultural exports to feed expanding regional and urban populations.

**New analytical work is needed to identify the bottlenecks to expanding Cambodia’s export and FDI base.** This could include exploring models for economic diversification from the point of view of trade diversification and GVC participation, including in the garments and tourism sectors (Box 6). It will be particularly important to identify the current workforce constraints and skills needed

## Box 6: Policies to Move Up the Value Chain in Cambodia's Tourism Sector

Although the tourism sector in Cambodia generates good jobs and has significant spillover effects on and links to the domestic economy, its jobs potential is not being fully realized. The sector generates jobs and opportunities along its value chain, including in the primary sector, where most of the Cambodia's poor are engaged (World Bank 2017a). Tourism can be a way to develop jobs in regions where opportunities for industrial development are often limited. However, in spite of Cambodia being home to some of the more archeologically valuable sites in the world, its tourism sector is generally low-value and with weak or only informal links to the domestic economy. While it creates many jobs, they are of a lower quality and are less inclusive than the tourist sector has the potential to create.

The World Bank has identified the following recommendations for supporting the continued development of Cambodia's tourism sector (see World Bank 2017a):

- **Improve the infrastructure and connectivity within Cambodia.** Growing urbanization and tourism mean that the country needs to have better infrastructure and transportation in place to accommodate the needs of locals and tourists, curb potential traffic issues, and build resilience of the sector.
- **Develop new tourism markets, products, and services.** For example, policymakers could look into encouraging the development of specific segments of the tourism value chains, including protected area tourism, domestic tourism, and business and events tourism. It will also be important to improve management of these tourism destinations if these markets are to be tapped.
- **Help producers and providers of food, crafts, and other local goods and services to access tourism value chains.** This might include supporting enterprises to make Cambodian-made products that meet market demand or establishing associations among farmers and food processors to supply domestically produced foods to hotels. This would help to increase the overall benefit of tourism to featured destinations.
- **Expand and upgrade the skills of local workers, while strengthening public-private partnerships to provide tourism-related training.** This might include fostering public-private partnerships between Government and training providers to provide and increase access to quality training for youth and women from poor communities to acquire the relevant skills and knowledge for the tourism industry, thus maximizing their potential employability. Greater collaboration among local workers, farmers, small and medium-sized enterprises, and tourism-related associations will also help expand and upgrade skills.

in the future since these investments take time to mature. Any policies aimed at fostering Cambodia's transition into GVCs such as garments and hospitality, which tend to be important for female employment, should also support inclusive jobs.

**The policies that we identified for diversifying exports and FDI into higher value-added value chains correspond to the Overarching Environment within Phase IV of the Rectangular Strategy.** The main implementing agencies would be the Ministry of Economy and Finance, the Council for the Development of Cambodia, the Ministry of Commerce, the Ministry of Agriculture, Forestry and Fisheries, and the General Department of Agriculture.

## 2. Streamline Procedures and Reduce the Costs of Establishing and Expanding SMEs

**Firm sales are generally required to grow for firms to hire new workers.** This points to a set of policies that are directed toward enhancing firm profitability, which is then expected to have spillovers on job creation. A range of policies can support the creation of new firms and their expansion. Four sets of policies that are particularly important for creating more jobs and better jobs, in terms of reduced labor turnover, are identified.

**First, reduce the cost of doing business for domestic firms.** The policies from the Cambodia Investment Climate Assessment Report that are particularly important for job growth include:



- Reducing business registration costs and simplify procedures by: (i) reviewing and reducing the fees for starting a business and consider implementing a flat fee that reflects the cost of service and (ii) introducing a single platform for business registration by integrating the incorporation process with registration at the MoC, General Department of Taxation (GDT) and Ministry of Labor (MoL);
- Enhancing the quality of land administration by finalizing the issuing of land titles in the country and developing an integrated online registry system for land, including ownership and cadaster information;
- Improving commercial dispute resolution by reviewing the existing case management system at the courts and considering the development of an electronic case management system for judges and lawyers; and
- Facilitating the implementation of the insolvency legal framework by establishing the insolvency administration profession and improving the capacity of the public and private sector related to insolvency matters.

**Second, develop an ecosystem for domestic firms to increase business skills and knowledge.** To deepen Phnom Penh's nascent ecosystem and broaden it to the rest of the country, the government should prioritize:

- Instituting formal processes to encourage public and private dialogue (PPD) for the private sector to raise their concerns and discuss possible solutions; and
- Providing more public support to entrepreneurship and innovation structures by supporting structures including incubators and research institutes. Funding to these structures could be made conditional upon results.

**Third, increase access to finance through a grant program and fiscal incentives.** This includes:

- Financing a Jobs Fund to support different segments of firms with high job potential through technical assistance and matching grants for three windows: (a) the consolidation of fragmented activities/small-sized firms so that they can compete in national (and possibly international) markets (such as agro-processing firms); (b) increased support to potential domestic suppliers of existing and nascent FDI-dominated value chains, such as apparel and electronics; and (c) domestic investment projects with a high potential for job creation; and
- In a more long-term approach, considering lowering the size of the investment determining the eligibility of domestic firms for fiscal incentives, as these requirements are a potential barrier to entry for SMEs.

**Fourth, increase the ability of domestic firms to hire and retain workers by:**

- Developing and strengthening intermediation mechanisms (job matching platforms and the National Employment Agency, see below); and
- Subsidizing some of the basic benefits (such as health care coverage and a retirement pension) that are usually provided to workers by their employers. This could be accompanied by an information campaign educating domestic firms about the importance of providing these benefits to workers and increasing worker awareness of their legal rights.

**The policies that we identified to streamline business procedures and reduce the costs of establishing and expanding SMEs correspond Rectangle III (Private Sector and Job Development) Side 2 (Promoting SMEs and Entrepreneurship) within Phase IV of the Rectangular Strategy.** The main implementing agencies would be the Ministry of Economy and Finance, the Ministry of Industry and Handicrafts, the Ministry of Commerce, and the Ministry of Labor and Vocational Training.

### 3. Support Household Enterprises to Enhance Their Productivity

**Not only are household enterprises a significant source of job creation—a phenomenon that is likely to increase with urbanization—they also employ many vulnerable workers.** Since only 6 percent of household enterprises hire workers from outside the household, policies aimed at fostering the growth of household enterprises should focus on upgrading job quality (productivity or incomes) rather than expanding the number of jobs that they provide. As older workers are more likely than younger workers to be employed in household enterprises, improving job quality would increase the inclusivity of Cambodia's jobs, since older workers tend to have lower participation in good jobs than young workers. While little is known about the nature of these jobs—which indicates an urgent need for more research—we have developed some policy recommendations based on the analysis in this report, recent data analysis of household enterprises in Vietnam (Pasquier-Doumer et al. 2017), and lessons from policy interventions in other countries designed to support household enterprises.

**First, more research must be completed to understand the nature of household enterprises in Cambodia and how to best support them.** Only a few countries have collected data on household enterprises, and these data

have revealed that these enterprises have very different motivations, aspirations, and challenges than do those of firms that are driven by a profit motive and that are not an extension of the household. Since the number of household enterprises is likely to grow as Cambodia urbanizes and becomes wealthier, it is crucial to understand this sector better,

**Second, it will be important to “professionalize” household enterprise owners so that they have the tools to run their enterprises as a business rather than as an offshoot of their households.**

**In the short run, policymakers can:**

- Provide training in basic accounting and marketing practices to household enterprises to help them make sound financial decisions and expand their production. While experience in other countries has shown that such training programs improve business practices, the evidence is weaker about their effect on profitability, probably because of the short duration of such programs in other countries.
- Match younger firms with more established firms that can mentor them and help them to upgrade their skills. A study of how mentoring affected Kenyan microenterprises showed that participating enterprises saw their profits increase (Brooks et al. 2016). Other mentoring programs have successfully been implemented in the United States and India.

**In the medium term, the government might consider:**

- Creating a one-stop online shop to provide household enterprises with information and technical assistance, including basic training programs. This would reduce the transaction costs involved business upgrading and create a virtual community of household enterprises.

**Third, policymakers should foster the use of IT solutions to expand household enterprises’ access to markets.** Many household enterprises rely on their personal network to supply inputs. Data from Vietnam showed that more than 80 percent of household enterprise inputs were purchased from other household enterprises (Pasquier-Doumer et al. 2017). This can be a significant barrier to efficient operations, particularly in rural and remote areas where there are fewer and more limited informal networks available. To use the hypothetical example of a retail shop, large wholesalers in cities find it very costly to collect information about demand from retail shops in rural villages and similarly the owners of these village shops find it costly to travel to the cities to purchase limited amount of goods that they need for their small shops. So, they each buy from and sell to those closest to them, usually at higher prices and for goods of lower quality than if they

had full information across all locations. IT can overcome this problem by aggregating demand from rural and remote areas and make it worthwhile for large suppliers, or other intermediaries, to engage productively with small-scale household enterprises.

To assist household enterprises in accessing markets, policymakers can:

- Support the development and use of IT solutions to improve the business and management practices of low-skilled, small-scale producers. Some household enterprises in Cambodia are already using technology, such as PassApp or Facebook, to reach new customers. Targeted apps to reach customers and new apps for business management are already being used in other countries. However, the evidence of their impact on business and management practices is still weak.
- Expand ICT infrastructure to ensure nationwide access.

**The policies that we identified to help household enterprises to enhance their productivity correspond to Sides 1 and 3 of Rectangle II (Economic Diversification) within Phase IV of the Rectangular Strategy.** The main implementing agencies would be the Ministry of Posts and Telecommunications and the Ministry of Commerce.

#### **4. Support the Development of Links between FDI Firms and Domestic Input-supplying Firms**

**Strengthening links between exporting FDI firms and domestic SMEs can be a new way to foster SME expansion, technology transfer, and the creation of indirect export jobs.** Cambodian exporters source very few of their inputs locally. Experience in other countries, such as Thailand, Malaysia, and China, has shown that these backward links can be a rich source of new good jobs.

**However, these connections often do not emerge naturally.** Most of Cambodia’s domestic producers do not meet the quality standards and/or productivity levels to qualify to supply FDI exporters. In surveys, FDI firms have cited a lack of industry-ready suppliers and of both technical and soft skills as the main barriers to buying from domestic input producers in Cambodia (World Bank 2018). Therefore, foreign investors do not actively seek out domestic suppliers. Also, the absorptive capacity of these local suppliers is weak, so they do not benefit from GVC spillovers in knowledge and technology.

**The right policies can help to build links between exporting firms and domestic input-supplying firms.** These policies include:

- Developing a database or directory of potential suppliers that have adequate technology and capacity to partner with multinational FDI firms to overcome information failures;
- Establishing local supplier development programs to help domestic enterprises become qualified suppliers or subcontractors for FDI firms;
- Simplifying and improving the administration of VAT reimbursement to ensure that exporting firms can receive refunds in a timely manner;
- Requiring the Cambodia Investment Board to find out from existing investors: (i) what constraints and challenges they face in sourcing their inputs locally; (ii) what their future investment and expansion plans are; and (iii) whether and how they would benefit from the relocation of international suppliers to Cambodia (World Bank 2018); and
- Strengthening the domestic absorptive capacity of the local private sector and workforce while supporting and promoting entrepreneurship and SMEs as well as workforce development (these policies are discussed elsewhere but are relevant here).

**The policies that we identified for strengthening links between FDI firms and domestic input-supplying firms correspond to Sides 2 and 4 of Rectangle III (the Promotion of Private Sector Development and Employment) as well as the Overarching Environment of Phase IV of the Rectangular Strategy.** The main implementing agencies would be the Ministry of Economy and Finance, the Council for the Development of Cambodia, the Ministry of Commerce, and the Ministry of Industry and Handicrafts.

## 5. Build a Skills Development System that will Attract Higher-value FDI and Increase Productivity across the Economy

**Cambodia's lack of a strong skills development system presents policymakers with a chance to build a system geared towards 21st century jobs that will increase the skills level of the workforce, the returns to education, and productivity levels throughout the economy.** There are two elements to building such a system. First, the education system needs to provide students with a strong foundation in a range of knowledge, behavioral, and digital literacy skills. Second, the technical and vocational training (TVET) system should be agile, flexible, and market-responsive so that workers can regularly upgrade their skills

throughout their working lives to keep pace with evolving technology and the knowledge economy. Building this skills development system is such a massive undertaking—as highlighted in the government's Education Strategic Plan 2014-2018 and the TVET Strategy: 2016-2021—that in this report we only discuss the policies for making the education and training system more responsive to the labor market.

### We have identified seven priority policy priorities:

- Incorporate digital literacy, socio-behavioral skills (creativity, innovation, interpersonal, teamwork, and leadership), and higher-order cognitive skills (mathematics, logic, critical thinking, complex problem solving, reasoning) into the school curriculum with cumulative learning throughout a student's primary and secondary school career. Experiences in a range of countries have shown the viability of teaching these additional skills in the classroom without imposing undue burdens on instructors.<sup>14</sup>
- Expand innovative models for increasing secondary school completion rates, such as the bridge program, access to computer-aided learning, and incentives to encourage households to invest in schooling.
- Provide incentives for women to continue in secondary and post-secondary education, particularly in the STEM fields. Data show that women attaining higher levels of education and employed in specific sectors and occupations are key to reducing the gender wage gap and expanding employment options for women.
- Introduce results-based financing (RBF) for TVET institutions with good results being defined as the successful integration of students in the job market, as well as expanding the provision of short courses (those that are short and flexible and that teach practical skills in high demand) to serve the working adult population.
- Incentivize the enterprise sector to play a larger and more structured role in providing, guiding, and advocating for a demand-driven skills development system. This would involve: (i) co-funding skills development programs in partnership with the enterprise sector with the financing being contingent on graduation, job placement, or job promotion rates; (ii) subsidizing infrastructure and technology for training centers within special economic zones (SEZs) to take advantage of economies of scale (similar to the Penang Institute in Malaysia); and (iii) developing incentive mechanisms to systematize the dialogue and cooperation between employers and skills program providers. Additionally, creating a standardized

<sup>14</sup> See Cunningham et al. (2016) and Guerra et al. (2014) for a review of methods for teaching socio-behavioral skills in pre-school, primary, secondary, and post-secondary schools.



testing and certification framework for skills, combined with incentives based on results, can encourage private providers of skills training to play an active role.

- Collect and disseminate user-friendly information to students, jobseekers, education and training institutes, and employers to enable them to make skills development choices that are aligned with market demand; this will require collecting, analyzing, and disseminating information on emerging jobs and associated wages, the skills that are in greatest demand, and the quality of skills development programs as measured by job placement rates.

**Additional analytical work is urgently needed, as well.** First, carrying out a systems assessment will give the Ministry of Labor and Vocational Training the tools to prioritize the long list of policy reforms, identify international best practices that could be considered in the design of the proposed skills development system, and set a baseline and an M&E system to monitor the effectiveness of reforms. In addition, future analytical work will need to be done to assess employer-driven training programs in Cambodia and elsewhere in the world.

**The policies that we identified for implementing a skills development system that will attract higher-value FDI and increase productivity across the economy correspond to Sides 1 and 2 of Rectangle I (Human Development) as well as Side 1 of Rectangle III (the Promotion of Private Sector Development and Employment) within Phase IV of the Rectangular Strategy.** The main implementing agencies would be the Ministry of Labor and Vocational Training and the Ministry of Education, Youth, and Sports.

## 6. Promote Efficient Labor Mobility and Job Matching

**To enhance the allocative efficiency of labor, workers need information and support to find and access the best possible jobs for their skill sets.** In Cambodia, workers usually find jobs through personal contacts, whether the job is in their locality or in another country. While this is a common practice, if workers have access to information about job vacancies, occupations, and skill needs, they can then find more appropriate jobs, especially if they are also provided with support in applying for those jobs.

**Policymakers can enhance job matching in Cambodia by:**

- Expanding and deepening the operations of the National Employment Agency (NEA) to collect more and more timely data on job vacancies, developing outreach

programs to populations that tend to use informal job search mechanisms, and expanding the information used by and the role of job counselors to guide jobseekers in the job search process; and

- Investing in hardware and software for the labor market information system managed by the NEA.

**A more detailed analysis on the scope and impact of labor migration requires data that Cambodia does not currently possess.** This is especially the case since most of Cambodia's migration is informal and thus not systematically recorded and compiled. Migration is an important component of Cambodia's jobs picture, as migration is common within Cambodia just as Cambodia is the source of 12 percent of all intra-ASEAN migration (Testaverde et al. 2017). Better data about migration trends can be collected in two ways:

- Revise the census and existing household surveys (CSIS, Labor Force Survey) to include questions about migrant household members, who typically are absent from the household roster. Special questions can be added on how these members interact with the current household in ways beyond remittances. This information can be used to create an absentee/migrant roster that aggregates information on the reasons for migration, their current location, demographics, labor supply, and remittances. This in turn would be extremely valuable for analyzing the scale and patterns of domestic and international migration.
- Use specially dedicated migration surveys (or modules in general-purpose surveys) to gather more detailed information about the dynamics of different forms of migration. Beyond the information on the broader migration trends that can be captured through a census, it is important to collect information about migrants who move temporarily, seasonally, change destinations, engage in repeat migration to the same or different destinations, or who change the purpose of migration. These dynamics can be captured using survey instruments that require their own methodology. This is valuable for helping policymakers form policies that maximize the gains from all forms of migration.

**To support more meaningful job searches and safer international migration and to safeguard the human rights of migrants, the Cambodian government should continue its negotiation of bilateral migration agreements.** However, given that most migrants do not use these formal channels, the government could also:

- Link Cambodia's labor market information system to the labor market information systems in countries offering better jobs; and

- Support pre-departure training services for workers searching for work abroad, online resources for potential or actual migrants, and incentives and processes to facilitate the repatriation and re-integration of these workers into Cambodia's labor market.

**The proposed policies are aligned with side 1 of Rectangle III (Private Sector and Job Development).**

The key actions focus on “providing work orientation training and expanding job recruitment and advertising services; as well as streamlining labor market information both inside and outside the country in order to increase employment opportunity in an equitable manner and reduce risky work migration.” It also aims to strengthen the governance of migrants' work, with the aim of improving the quality jobs and migration experiences, as well as to support returning migrant workers to invest in their home communities.

## 7. Regain Macroeconomic Independence and Exchange Rate Flexibility

**Cambodia should take steps to regain exchange rate flexibility and monetary policy independence to shield jobs from fluctuations in the US dollar and other macroeconomic risks.** Cambodian policymakers could consider developing a market-based de-dollarization strategy to progressively regain policy autonomy. The development of a domestic bond market would also help to both foster domestic savings and progressively increase exchange rate flexibility to support job creation going forward. Policymakers also need to encourage private investment and credits to invest in the tradable sector instead of construction and real estate, sectors that are prone to instability and have fewer good job opportunities than the exporting sector does.

**This points to a range of macroeconomic and fiscal policies to support job-creating industries.** Policymakers can:

- Institute a campaign to publicly recognize private sector institutions that pay salaries in Khmer riel— a short-term action that would support the use of local currency.
- Adopt and gradually implement a larger market-based de-dollarization strategy by: (i) gradually increasing reserve requirements for deposits in dollars and (ii) bringing down the riel benchmark interest rates to promote borrowing in the national currency.
- Develop a domestic debt market (both public and private) and starting to issue sovereign debt to mobilize domestic and foreign savings. This will help increase investment

and capital stock accumulation to sustain high economic growth. It will also help the corporate sector to access sources of long-term funding and establish alternatives to investing in construction and real estate to mitigate some of the current macro-financial risks.

- Strengthen the public Investment management framework to foster capital formation and introduce investment tax credits for the acquisition of machinery and equipment.

**The policies that we identified for macroeconomic and exchange rate management correspond to the Overarching Environment of Phase IV of the Rectangular Strategy.** The main implementing agencies would be the National Bank of Cambodia and the Ministry of Economy and Finance.

**Perhaps the biggest challenge for the implementation of these policy areas is in coordinating the reforms across the government, yet these proposed policies must be coordinated to ensure that they collectively result in the creation of more, better, and more inclusive jobs.** The fact that the policies presented in this report cut across all aspects of Phase IV of the Rectangular Strategy demonstrates the complexity of the jobs agenda while highlighting the risk that some crucial jobs policies might not be implemented or be implemented in a coordinated manner.

**To ensure that these agency-specific actions are sufficiently coordinated, the government can undertake two processes.** First, policymakers could mobilize stakeholder support for a Jobs Strategy. This Strategy would: (i) identify the strategic jobs goals that are yet not defined in Phase IV of the “Rectangular Strategy; (ii) specify those sectoral policies from the Rectangular Strategy that are also crucial for creating more, better, and more inclusive jobs; and (iii) set up a system for monitoring jobs-specific policy actions across the many different ministries, agencies, and other stakeholders involved in implementing the strategy. Second, they could appoint a Jobs Champion with the leadership skills to oversee the reform across the entire government. As noted in Phase IV of the Rectangular Strategy, inter-institutional or ministerial coordination is an important key to the successful implementation of the Rectangular Strategy and will be similarly crucial to the successful implementation of the Jobs Strategy. This can be achieved by creating a coordinating body that will both guide and hold accountable all government and private sector actors involved in the drive to create more, better, and more inclusive jobs for Cambodia's future growth and prosperity.

### Box 7: Policy Implications for Inclusive Jobs

**The report proposes analysis and policy recommendations for better and inclusive jobs. Indeed, “inclusiveness” is streamlined through the policy recommendations.** However, it is useful to explicitly identify how these jobs may improve the inclusiveness of future jobs.

**First, diversifying the export and FDI sector will benefit women and young workers. Women are the employee of choice in FDI and exporting firms today (Policy Area #1).** Countries with more diversified exports and FDI-sectors also see a high share of women working in industries related to electronics, food processing, and service exports. However, for Policy Area #1 to truly work for women, the government can make particular efforts to attract the kinds of exporting industries that tend to employ women. Further, these workers tend to be young, so this policy will provide new jobs for young workers.

**Support to improving the productivity of household enterprises (Policy Area #3) will disproportionately benefit the poor, women, and older workers.** Productivity enhancing mechanisms that can be easily accessed from home, such through technology, will be particularly beneficial to women, who tend to need to combine home and work duties, and to people with disabilities that are mobility constrained. Further, efforts to link domestic (including household) enterprises with FDI (Policy Area #4) can benefit these small producers.

**While a skills development system will benefit everyone (Policy Area #5), women, older workers, and the poor will particularly gain.** Women still have lower levels of education than their male counterparts, so there is a basic need to level the playing field across genders. The expansion and enhanced quality (measured as relevance) of TVET services will be crucial since the majority of today’s workforce does not have the skills needed today, let alone in the future. At the same time, younger workers will need to develop a broad set of skills to lead Cambodia into Industrial Revolution 4.0.

**Young people, the unemployed, and those trying to climb the career ladder will benefit from an expanded labor market information system and an even stronger National Employment Service (Policy Area #6).** These services will permit them to better prepare for and find the best jobs for their skills and interests. On a related note, improved information and processes for migration may provide better work experiences for young men and women (who tend to migrate) and may draw them home again.

**Finally, Policy Area #7 on macroeconomic independence and exchange rate flexibility will be particularly beneficial to young women, who are over-represented in export-oriented jobs.**

**Additional actions can be undertaken to support women, youth, older, low-skilled, and rural workers.** These additional policies should co-exist with the seven policy areas defined in this report to meet the goal of more inclusive jobs.

## A Vision of Cambodia's Future Jobs

Based on current trends in Cambodia's economy, the emerging mega-trends, and the successful implementation of the proposed policies, we can predict the sources and nature of Cambodia's future jobs that will provide firms and workers with even greater benefits than those enjoyed today.

**The export sector will generate more higher-value jobs both in its own factories and in new domestic SMEs that will supply those FDI firms.** Garment manufacturing is likely to decline over the next decade as a result of mega-trends, the potential loss of the tariff preferences currently offered by the EU and the US, and Cambodia's aspirations to move into Stage II of global integration. If Cambodia is successful in diversifying and expanding into higher value FDI and in creating links with domestic producers, more good jobs will emerge that will particularly benefit women (working in FDI firms and in tourism) and younger workers.

**Household enterprises and SMEs will grow, be more profitable, and be more integrated into the economy as a whole.** These are already the source of most good jobs in the Cambodian economy. If the rising consumer class materializes as expected and if links can be developed between SMEs and the FDI firms, the number, size, productivity, and wages of SMEs are likely to increase as well. This is likely to mostly benefit young workers as they have a higher propensity than other age groups to work in these kinds of jobs.

**Labor productivity and wages will increase.** If Cambodia can successfully upgrade the skills of its existing labor force through intensive, short-term, and market-oriented skills development, while simultaneously strengthening the education system to shape the workers of the future, then labor productivity, innovation, and wages will increase. When Cambodia's workforce has more skills, this will attract FDI in higher value-added segments of existing GVCs and in new value chains. Productivity in the traditional sectors will also increase and will raise the earnings of those in subsistence household enterprises.

**The number of knowledge-intensive jobs will continue to grow, while the number of subsistence jobs will gradually decrease.** Cambodia is already moving in this direction. However, these policy reforms will speed up the transformation. Cambodian policymakers need to increase better jobs either by attracting higher value-added FDI or by encouraging the creation of firms that are knowledgeable and skillful enough to recognize new competitive opportunities.

**There will be more jobs that require the use of ICT.** Technology will continue to be a source of entrepreneurship and of better jobs. The automation of tasks will also mean greater use of ICT in production. For example, entrepreneurs who create technology will be the generators of knowledge-intensive jobs. Household enterprise owners who use ICT in their business and management practices will increase their productivity. Technology can also be used to advertise current and future available jobs, to open access to markets, and to learn new skills. For example, one-stop virtual shops can be used to enable workers to receive training to prepare them for the jobs of the future. IT solutions that aggregate products and/or suppliers, facilitate e-commerce, and reach new customers can widen market access, especially for rural firms seeking to reach urban markets, and create jobs in the process. Nonetheless, some jobs may also be lost due to automation. Therefore, it will be important for policymaker to understand which types of technology will complement labor-intensive, high value-added tasks and which will replace labor in certain occupations.

**In closing, Cambodia is at a turning point.** It can continue its current development and jobs strategy, making policy changes at the margin and continuing a slow upward movement in jobs quality. Alternatively, it can take on bold, more aggressive policy reforms and move to a higher equilibrium of good jobs that are particularly inclusive of women and those working in the traditional sectors. This report argues that greater gains are possible through a deliberate Jobs Strategy that focuses on our six policy reform areas, together with leadership by a strong coordinating body and commitment across government to create the jobs that will lead Cambodia toward its upper-middle income Vision for 2050.

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## ANNEX1: Summary of Policy Recommendations

Policy Areas	Selected Policy Actions		Long-term Goals	Corresponding Parts of Rectangular Strategy-Phase IV	Main Implementing Agencies
	Short term (within the new five-year plan)	Medium term (by 2030)			
<b>Diversify exports and FDI into higher value-added value chains (or segments of value chains)</b>  <i>Because most of Cambodia's current jobs are in low-value segments of GVCs.</i>	1. Shift from tax holidays to streamlined incentives that foster private investment in machinery, such as a tax credit on capital investment and technological transfers.  2. Review and streamline customs requirements and clearances for export and import licenses to reduce the time and costs of trading across borders.	1. Introduce super tax deductions for R&D and staff training  2. Automate the process of sanitary and phytosanitary certification and foster the adoption of more IT  3. Pursue trade agreements with new international partners	Attract higher value-added investment to create better jobs in new GVC sectors  Reduce the transaction costs of importing and exporting while ensuring the high quality of exports to integrate into regional and GVCs	Overarching Environment	Ministry of Economy and Finance, Council for the Development of Cambodia, Ministry of Commerce, and Ministry of Agriculture, Forestry and Fisheries (General Department of Agriculture)
<b>Streamline procedures and reduce costs of establishing and expanding SMEs</b>  <i>Because firm start-ups are a significant source of jobs and could generate even more in the future, but firm growth (in terms of adding workers) is seriously constrained.</i>	1. Reduce the cost of doing business for domestic firms and support the development of an ecosystem for firms by: (i) reducing business registration costs and simplifying procedures, (ii) improving dispute resolution processes and insolvency administration, (iii) providing more public support to entrepreneurship and innovation structures, including incubators, tech hubs, and research institutes; and (iv) starting a Jobs Fund to provide firms with technical assistance and matching grants;  2. Increase the ability of domestic firms to hire and retain workers by: (i) developing and strengthening intermediation mechanisms, and (ii) subsidizing some basic worker benefits.	Complete and approve the Law on Electronic Commerce	Create a range of institutions that can assist entrepreneurs at the various stages of the development of an enterprise, including ideation, incubation, acceleration, and development.	Rectangle II (Economic Diversification) Side 1, Side 3	Ministry of Economy and Finance, Ministry of Industry and Handicraft, Ministry of Commerce, Ministry of Labor and Vocational Training

Policy Areas	Selected Policy Actions		Long-term Goals	Corresponding Parts of Rectangular Strategy-Phase IV	Main Implementing Agencies
	Short term (within the new five-year plan)	Medium term (by 2030)			
<b>Help household enterprises to enhance their productivity</b>  <i>Because nearly one-fifth of jobs are in this sector, which is likely to expand with growing urbanization.</i>	1. Enhance access to markets by encouraging the development of sustainable IT solutions that can aggregate products and/or suppliers, facilitate e-commerce, and help firms to reach new customers.  2. Professionalize household enterprises by: (i) matching younger firms with more established firms through mentoring and (ii) improving the business and management practices of low-skilled small-scale producers by providing them with IT solutions.	1. Open one-stop (virtual) shops where household enterprises can go for registration, information, and technical assistance including basic training programs.  2. Expand ICT infrastructure nationwide.	Increase the productivity and incomes and improve the welfare of household enterprises.	Rectangle II – Economic Diversification Side 1, Side 3	Ministry of Posts and Telecommunications, Ministry of Commerce
<b>Support the development of links between FDI firms and domestic input-supplying firms</b>  <i>Because working with FDI firms can help SMEs to expand their jobs and profits, but these links need to be fostered.</i>	1. Simplify and improve the administration of the VAT reimbursement system so that importing firms can get refunds in a timely manner.  2. Ask existing investors: (i) what their constraints and challenges are in local sourcing; (ii) what their future investment and expansion plans are; and (iii) how they might benefit from the relocation of international suppliers to Cambodia.	1. Develop a database of SMEs and suppliers to enable FDI firms to identify the right suppliers with adequate technology and capacity.  2. Increase the productivity of indirect exporters, in particular SMEs, by introducing behavioral incentives to encourage FDI firms to invest in local workforce development, R&D, local sourcing, and supplier upgrading activities.	Foster the integration of SMEs into jobs-friendly GVCs by becoming indirect exporters	Overarching Environment Rectangle III - Promotion of Private Sector Development and Employment Side 2, Side 4	Ministry of Economy and Finance, Council for the Development of Cambodia, Ministry of Commerce, and Ministry of Industry and Handicrafts



Policy Areas	Selected Policy Actions		Long-term Goals	Corresponding Parts of Rectangular Strategy-Phase IV	Main Implementing Agencies
	Short term (within the new five-year plan)	Medium term (by 2030)			
<b>Build a skills development system that will attract higher-value FDI and increase productivity across the economy</b> <i>Because a knowledge-based economy requires an employer-driven, results-oriented, and flexible skills development system.</i>	<p>1. Expand innovative models for enabling students to finish secondary school, such as the bridge program and access to computer-aided learning, and give incentives to households to invest in schooling.</p> <p>2. Develop a plan for engaging the enterprise sector in providing, guiding, and advocating for a demand-driven skills development system.</p> <p>3. Provide incentives to encourage women to pursue secondary and post-secondary education, especially in the STEM fields.</p> <p>4. Collect and disseminate user-friendly information for students, jobseekers, education and training institutes, and employers to help them to make skills development choices that are aligned with market demand.</p>	<p>1. Incorporate digital literacy, socio-behavioral skills (creativity, innovation, interpersonal skills, teamwork, and leadership) and higher-order cognitive skills (mathematics, logic, critical thinking, complex problem solving, and reasoning) into the curriculum.</p> <p>2. Allocate public resources to results-based skills development programs.</p>	<p>Develop a collaborative (public-private) skills development system that prepares and equips workers for a competitive and constantly changing jobs market.</p> <p>Provide information to students, jobseekers, education and training institutes, and employers to enable them to make skills development choices that are aligned with market demand.</p>	<p>Core (Governance)</p> <p>Rectangle I - Human Development</p> <p>Side 1, Side 2</p> <p>Rectangle III - Promotion of Private Sector Development and Employment</p> <p>Side 1</p>	<p>Ministry of Labor and Vocational Training and Ministry of Education, Youth, and Sports</p>

Policy Areas	Selected Policy Actions		Long-term Goals	Corresponding Parts of Rectangular Strategy-Phase IV	Main Implementing Agencies
	Short term (within the new five-year plan)	Medium term (by 2030)			
<b>Promote efficient labor mobility</b> <i>Because Cambodia has a highly mobile labor force that is not finding the best jobs to fit their skills</i>	1. Expand and deepen the NEA's operations. 2. Revise the census and other relevant surveys to better collect data about migration trends. 3. Support pre-departure services for migrants going overseas to look for work and sponsor a website covering migration practices, rights, and resources. 4. Strengthen incentives and initiatives to repatriate skilled Cambodian migrants who are working abroad.	1. Invest in hardware and software to expand the NEA's job vacancy database. 2. Link Cambodia's labor market information system with those in countries offering good job opportunities.	Increase allocative efficiency by ensuring that workers are well-matched to their jobs and can acquire skills.	Rectangle III - Private Sector Development and Job Employment Side 1	Ministry of Labor and Vocational Training
<b>Regain macroeconomic independence and exchange rate flexibility</b> <i>Because US dollar fluctuations impact Cambodia's export sectors, which employ a large share of workers.</i>	1. Promote the use of the local currency through a campaign to publicly recognize private sector institutions that pay salaries in Khmer riel. 2. Strengthen the public investment management framework.	1. Develop, adopt, and gradually implement a market-based de-dollarization strategy by: (i) gradually increasing reserve requirements for deposits in dollars and (ii) bringing down the riel benchmark interest rates to promote borrowing in the national currency. 2. Consider developing a domestic debt market and start to issue sovereign debt.	Regain exchange rate flexibility and monetary policy independence to shield jobs from factors affected by US dollar fluctuations.	Overarching Environment	National Bank of Cambodia and Ministry of Economy and Finance





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