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INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

REPORT OF ECONOMIC MISSION

TO

CAMBODIA - 1969

(in three volumes)

VOLUME I

THE MAIN REPORT

October 12, 1970

East Asia and Pacific Department

CURRENCY EQUIVALENTS

Before August 18, 1969

(a)	US\$ 1.00	=	Riels 35.00
	Riel 1.00	=	US\$ 0.029
	Riels 1 million	=	US\$ 28,571
(b)	F Fr. 1.00	=	Riels 10
	Riel 1.00	=	F Fr. 0.10 (= US\$ 0.020)
	Riels 1 million	=	F Fr. 100,000

After August 18, 1969

US\$ 1.00	=	Riels 55.54
Riel 1.00	=	US\$ 0.018
Riels 1 million	=	US\$ 18,004
(F Fr. 1.00	=	Riels 10 = US\$ 0.18)

Note: On August 18, 1969 the new parity for the Riel was defined as 16 milligrams of fine gold, which corresponds to the new parity of the French Franc (which was devalued on August 10, 1969) at the same rate of exchange as before. However, the exchange rate for non-Franc currencies was brought in line with the Franc rate.

Foreword

This is the report of a World Bank economic mission which visited Cambodia in October-November 1969. The report considers the Cambodian economic situation only up to that time. The writing of the report was completed in February 1970 and there have been no changes since then to take account of subsequent developments in Cambodia.

Members of the mission were:-

Rudolf Hablutzel	Chief of Mission
Miss H.J. Goris	Economist
George C. Maniatis	Economist
Yves Franchet	National Accounts
Maurice Gaide	Agriculture (Consultant)
Martin Karcher	Transport
Raymond H. Rollet	Power
Jeremy Bonnett	Tourism
Miss G. Gagnon	Secretary

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MAPS

BASIC DATA

<u>Area</u>	<u>Square miles</u> 7,000		
<u>Population</u> (mid-1969)	7.28 million		
Rate of growth	2.7%		
<u>GDP at constant 1966 prices</u> (million Riel)	<u>1952</u> 15,120	<u>1960</u> 25,482	<u>1968</u> 34,381
Rate of growth	1952-1968 5.3%	1960-1968 3.8%	1964-1968 4.7%
<u>GDP per capita</u> (in 1966 Riel)	3500	4680	4850
<u>GDP at current market prices</u> (1966, million Riel) of which, in percent	31,255		
Agriculture, fishing, livestock, forestry	41.0		
Power	1.1		
Manufacturing, energy, construction	15.9		
Commerce	22.9		
Public administration	13.7		
Others	5.4		
<u>Expenditure on GDP at market prices</u> (%)	<u>1968</u>	<u>Average</u> <u>1962-1968</u>	
Consumption	87.4	86.7	
Public	17.5	19.4	
Private	69.8	67.2	
Investment	15.1	16.5	
Net exports of goods and non-factor services	-2.5	-3.2	
<u>Percent of GDP at market prices</u>	<u>1968</u>	<u>Average</u> <u>1962-1968</u>	
National saving	12.6	13.3	
Government tax revenue	17.0	16.3	
Government total revenue	20.5	19.4	
<u>Resource gap as % of investment</u>	<u>1968</u> 16.6	<u>Average 1962-1968</u> 19.4	
<u>Consumer price index</u> (1949 = 100) (Working class in Phnom Penh)	1959	239	March 1969
			354
<u>Money and credit</u>			
Exchange rate			
Before August 1969	1 Riel = 0.0286 US \$ 1 Riel = 0.1 French Franc		
After August 1969	1 Riel = 0.0180 US \$		
Means of payment (1968, million Riel)	8,815		
<u>Consolidated government operations</u> (billion Riel)	<u>1968</u>	<u>Average</u> <u>1962-1968</u>	
Revenue	7.5	5.7	
Current expenditures	7.2	6.2	
Capital expenditures	1.4	1.3	
Deficit	1.1	1.8	

<u>Balance of payments (million Riel)</u>	<u>1968</u>	<u>1967</u>
Export of goods	3,038	3,076
Import of goods	3,415	3,225
Trade balance	-377	-149
Net services	-32	-82
Current account deficit (-)	-469	-88
Gold and foreign exchange reserves (million US \$) at October 31, 1969	65.7	

SUMMARY AND CONCLUSIONS

1. Cambodia became a modern independent nation in 1953, maintaining the form of a constitutional monarchy; King Norodom Sihanouk renounced the throne in 1955 in favor of his father, but he has continued as Chief of State to exercise the role of king.

2. Data on the economy are available since 1952; during the 17 years since then, GDP has grown on average at about 5 percent a year in real terms, but with a much faster growth in the fifties than in the sixties. A considerable amount of foreign assistance was received, particularly from the U.S., but aid from the latter source was phased out in 1963 by Cambodia's own choice in pursuance of a more pronouncedly neutral foreign policy.

3. From 1956 to 1963, the GDP growth rate was about 7 percent a year; rice production increased considerably faster than population; rice exports reached a high level of 800,000 tons compared with an average of about 500,000 tons in the mid-fifties; and industrial production increased about 7 percent a year. Government expenditures in this period increased at about 20 percent a year to reach 21 percent of GDP in 1963. Total investment in 1963 was over 17 percent of GDP, of which more than two-fifths in the public sector.

4. After this period of progress, agriculture began to stagnate. Also, the 1963 nationalization of foreign trade, banking, and insurance caused a setback to the service industries. Construction sharply declined and has since then only gradually recovered. However, value added by manufacturing industry increased faster than in the preceding period, as a number of new factories, mostly state enterprises financed with bilateral assistance, came into operation. As a result, GDP increased about 4 percent a year in real terms from 1963 to 1969.

5. Exports have temporarily increased in years of favorable rice crops, but over the period 1963-1968 they have stagnated at the level of about US\$90 million, and in percent of GDP they declined from 12 percent to 8 percent. The same observation is true for imports which remained stationary at about US\$97 million, with a temporary increase in intermediate years. The trend for rice exports has been to decline, although the 1969/1970 crop may produce a surplus as large as in earlier years due to favorable weather.

6. Since the phasing out of US assistance and a slower expansion of the tax base, the Government has faced a serious financial constraint throughout the last seven years. In spite of economies in defense outlays (which came down from 7.7 percent in 1962 to 4.7 percent of GDP by 1968) the current budget has been persistently in deficit except in 1968. Public sector capital outlays in terms of GDP declined from over 7 percent in 1963 to about 5 percent in 1968.

7. Private investment during these six years increased at the same pace as GDP of which it continued to take about 10 percent, but all of the increment over this period was for construction and stocks. Total imports of capital equipment into Cambodia showed a slight decline in absolute terms.

8. The Second Five-Year Plan (1968-1973) was adopted in 1967. It proposes a growth rate of GDP in real terms of 5 percent a year, the same as the First Five-Year Plan (1960-1964) target which was not quite achieved. The Plan gives a list of projects but no phasing of sectoral investment expenditures. Total government investments are proposed at about CR 2.5 billion a year, but only half of this level has been attained.

9. Available economic information is insufficient to permit systematic planning, although with a relatively modest effort this situation could be substantially improved. The Ministry of Planning on the other hand is at a historic low point of activity and virtually without staff. In 1960 it had been proposed to entrust it with the financial management of all public investments and foreign aid, but this idea was not carried out. All policy decisions of any consequence, economic or otherwise, are taken by the Chief of State.

10. Hitherto, social advancement has been put above economic growth as a national objective. The Second Plan, however, in establishing over-all priorities, put prime emphasis on the development of the productive sectors of the economy. The Plan's first priority is agriculture, followed by industry, tourism, transport and finally social services, in this order. Within agriculture itself, again, promotion of crops is given priority ranking in line with the relative importance of different crops for export (paddy, rubber, maize). The Government still considers these priorities as a guiding principle, but finds it difficult to pattern its expenditure policy along these priorities. One difficulty is the shortage of sufficiently prepared projects, particularly in the agricultural sector. Another is the shortage of funds. Social expenditures, as in the past, have grown faster than in any other field. In the current budget, education and health expenditures continued, up to 1968, to grow at 12 and 8 percent a year respectively, compared with 6 percent for total current expenditures.

11. Both the mobilization and the allocation of resources should be reappraised by the Government at this juncture, since it has become obvious that the Five-Year Plan is too far removed from realities to be of any further help. There can be no quarrel about the importance, in future, of promoting agriculture and industry; it would be wrong, however, to attempt to spend 50 percent of public investment funds in these two sectors (as the Plan had proposed), if adequate projects are not available. It can be hoped that a portfolio of projects in these sectors will become available within the next few years, but for the time being there is a good case for executing a number of high priority projects in infrastructure, e.g. power and transport.

12. Agriculture. Rice dominates the rural economy. Yields are very low (1 ton/hectare); cultivation techniques are traditional and only a very modest beginning has been made in promoting modern inputs for production. A large potential for irrigation and double cropping is largely untapped. The first major irrigation project at Prek Thnot has just been started with financial assistance from 12 countries under the Mekong Committee. A second project at Battambang, for which a study was prepared in 1963 by SOGREAH of France, also under the Mekong Committee, is under revision by a team of Swiss consultants.

13. The principal question mark for the economic returns on any project in agriculture (except rubber and other plantations) is the institutional framework and the ability of the government to induce the necessary change in agricultural practices, and use of inputs, and to provide adequate credit. A new Agricultural Bank is in process of being established but has not started operations. Earlier efforts by the cooperatives to provide seasonal credit are held up by a massive problem of defaulting.

14. In rubber, Cambodia has the highest average yields in the world and is highly competitive. Most plantations are French-owned, but their concession areas are almost completely planted, and new rubber plantations are through state enterprises. Smallholders are also expanding. Availability of additional suitable land for new projects in the lower Mekong basin (where almost all existing plantations are located) is uncertain, and high priority should be given to a new survey. In the province of Ratanakiri in the East, suitable virgin land is ample, but the area is relatively inaccessible. A state plantation has been installed. Further activity is hampered for the time being by military insecurity.

15. A number of possibilities exist for promotion of other crops. A study ought to be undertaken for coconut plantations on the southwest coastland where private planters have already made a successful beginning. Maize, which has been promoted in neighboring Thailand with great success for export, has been neglected in Cambodia. Sugar production on the basis of cane instead of sugar palm has been proposed in the Plan, but adequate study of suitable varieties and of water requirements has not yet been undertaken. With the recent installation of a jute mill, the cultivation of jute and kenaf has been successfully promoted.

16. Livestock and forestry have potential far beyond present production. Large numbers of beef are now smuggled to Viet Nam. Japanese private capital may enter into timber extraction. A second plywood factory is also considered in the public sector. A UN study of forestry resources in the Cardamome region is about to be completed. Technical assistance has been required from FAO to study the problem of declining fish catch in the Great Lake, and to help develop marine shrimping. Fish canning and fish-meal production has started and seems promising.

17. Industry. Cambodia has rightly not attempted to push import substitution industries as a main vehicle for economic development. Nevertheless, there is scope for further industrialization primarily in the field of processing of agricultural products both for the domestic market and for export. A difficult problem, however, is the government's policy vis-a-vis private enterprise.

18. The policy, since 1963 in particular, has been to rely almost entirely on public investments for industrialization, with the result that Cambodia now has a number of factory-size industries, many of which built under Eastern bloc grand aid, whose viability is difficult to gauge because most prices for industrial inputs as well as outputs, are so fixed by the Government as to guarantee an adequate return. Competing imports are priced into the economy at a correspondingly high level. In official circles, it is felt that the theory of market incentives and competition does not fully apply in Cambodia. In the pre-1963 period, private industry, owned by Chinese (who also controlled import trade) reportedly manipulated market prices and exploited the consumer. Reportedly, again, this has ceased with the nationalization of foreign trade and the creation of state industrial enterprises.

19. Industrial policy is thus a social, as well as an ethnic issue. Awareness of the malfunctioning of both government industries and government-operated foreign trade is however growing, and is further supported by evidence that the economy has failed to show adequate growth since the 1963 economic reforms. An attempt was made in a new law in 1968 to again "open up" certain fields of industry to private enterprise, but lack of clarity and too many provisos have prevented it from attracting private investment so far. Further clarification will be needed, and to restore a degree of business confidence in the Government, other measures will be required as well in the field of foreign trade and credit policy.

20. The two state commercial banks and the National Investment Fund have given deliberate preference to state enterprises with the effect that the private sector was virtually starved for credit. This tendency was reinforced by (a) the decline in deposit resources and the flight into currency hoards following the 1963 reforms, and (b) a credit squeeze imposed by the Central Bank. The latter policy has been somewhat misguided by excessive fears of inflation. Money supply has been kept virtually unchanged since 1967.

21. The liberalization of foreign trade has been debated ever since the December 1968 speech of the Chief of State where, in implicit recognition of the failure of the 1963 reforms, he announced a change-over from an "inward looking" policy to an "open" policy, which also led to the application for membership in the Fund and the Bank. In August 1969 a new Government was formed with "carte blanche" from the Chief of State for new measures to bring the economy back on the road to development. The only measure taken so far was the devaluation of the Riel three days after the

Government took office, but plans exist for the partial dismantling of SONEXIM, the state trading organization. All imports except government procurement would be turned over to the private sector, as well as exports with the exception of rice, rubber and maize.

22. There can be no doubt that with improved legislation on private investment opportunities, liberalization of foreign trade, a more rational credit policy, and the reintroduction of private banking and insurance, the private sector could again be led to perform a more productive role in the economy, and particularly in industry. It might even be induced to establish industries in Sihanoukville. A "free zone" with an industrial estate in Sihanoukville has been included in the Plan, but not implemented for lack of funds, as well as lack of certainty of success under the policy of state capitalism.

23. Transport. Cambodia today has a fairly adequate system of transport facilities. Major projects completed since independence are the creation of a seaport at Sihanoukville, a 4-lane highway and a railway line between Phnom Penh and Sihanoukville, two international airports (Phnom Penh and Siem Reap) and a bridge over the Tonle Sap at Phnom Penh. With these additions, the transport system will not require further major extensions in the near future; instead, priority has to be given to improvement of standards and maintenance of existing facilities, particularly of the road network. Most of the primary roads are 30-40 years old and were built to standards inadequate for modern traffic. Standards have been gradually improved in many cases but much more needs to be done.

24. The decision to build a deep-sea port at Sihanoukville proved to be a sound one, as navigation on the Mekong (previously the main traffic link to the world) was seriously hampered by the war situation in Viet Nam. With the end of this conflict, the port of Phnom Penh should be expected again to gain in importance.

25. The extension of the two existing airports and the improvement of their navigational and telecommunication equipment is planned, but the phasing as well as the relative priority as between Phnom Penh and Siem Reap has still to be worked out in conjunction with expected availability of hotel accommodation and flow of tourists.

26. Power consumption has grown 13 percent a year up to 1963 and 5 percent a year since then. Seventy-five percent of total consumption is in Phnom Penh. There is no shortage of capacity at present except in Sihanoukville, but the distribution system of Phnom Penh is highly inadequate. Owing to excessive voltage fluctuations, breakdowns, and an unfavorable rate structure, most industries in the past have installed their own generating units. A UNDP study on rates is under consideration by the government. In the medium term, it will probably be economically justified to establish a transmission link between Phnom Penh and Sihanoukville, but no conclusive study of possible alternatives is available yet.

27. Tourism. Cambodia's assets for the development of tourism are considerable: first, the unsurpassed ancient Khmer temples in Siem Reap province (Angkor) and second, the country's location in the heart of the South East Asia tourist circuit. Tourism was accorded high priority in the Second Plan but much of the development effort is expected to come from private capital, including foreign capital for hotel construction. Infra-structural and hotel development at Siem Reap so far have been uncoordinated and haphazard, and if continued in this fashion might led to less than economic use of resources and could adversely affect the attractiveness of the whole setting. The establishment of a master plan for the future development of Siem Reap is recommended by the mission.

28. Financial Constraints. Up to the early sixties, a combination of fairly rapid growth of revenues plus substantial budget support from the U.S. enabled the Government to undertake a massive expenditure program, with total outlays of the National Budget growing 20 percent each year between 1956 and 1962. The termination of U.S. assistance after 1963 left a large gap in the budget. Even though consolidated revenues increased from 21 percent of GDP in 1963 to about 23 percent of GDP in 1968, the current deficit could only be reduced by slowing down the growth of current expenditure in the budget to less than 4 percent per annum. Education and other social expenditures had acquired a momentum of their own and could not be easily slowed down. Instead, defense expenditures were prevented from expanding since 1962, and economic services and general administration were severely restrained, growing at 5 percent and 3 percent a year respectively, while education continued at over 12 percent a year. Finally, investment outlays have been kept below the 1963 level ever since that year. In spite of this, drawdown of assets and net credit from the central bank in the last 8 years have financed over two-thirds of government investments, and the balance, including the deficit in the current budget, was covered by foreign aid, largely from France in later years.

29. In future, there will be a need for a somewhat faster growth of current expenditures in economic services as well as general administration. Government salaries are far too low to attract qualified personnel and the civil service needs upgrading. On the other hand, the rate of expansion in social expenditures should be reduced.

30. With the prospective yield of present taxes, the outlook is for a renewed expansion of the current deficit to about CR 500 million in a few years (7 percent of present revenues). Tax revenues are 19 percent of GDP and growing at the same rate as GDP. The tax and budgetary system is extraordinarily complex and in need of reform sooner or later. There would seem to be scope for action to combat tax evasion. Also, some new taxes may be devised.

31. Balance of Payments. Rice and rubber account for two-thirds of total exports. For both commodities, long-term prospects for world market prices are to go down. Rubber production for export is likely to increase but only with no further defoliation. In the case of rice, it is very uncertain whether production will grow faster than domestic consumption in the years immediately ahead. Considerable potential exists for other existing as well as new agricultural exports but this will take time, and it will also depend on the type of export regime which the Government will ultimately adopt.

32. Import requirements are certain to grow faster than GDP, and in addition there is a backlog of requirements. If an average 5 percent growth rate for GDP is to be achieved in future which is not an unreasonable target, the current account deficit might be assumed to increase from about \$14 million in 1968 to about \$32 million in 1973, even if exports are assumed to grow at a rate of 4 percent a year, which is probably optimistic.

33. Terms of Foreign Aid. Cambodia's present external debt is about \$50 million. Debt service payments due in 1970 are \$6.9 million or 8 percent of present export earnings, but payments on existing debt will gradually decline to \$1.6 million in 1980. Gold and exchange reserves declined in the last two years but in October 1969 were still equivalent to \$66 million, covering merchandise imports for about 8 months.

34. Given the level of reserves and the small amount of external debt, there is room for servicing additional loans on conventional terms. If exports were to grow at 4 percent a year, and \$10 million of conventional debt was contracted each year, the debt service ratio would not go much beyond 10 percent in 1980; however, with the uncertain export prospects, it would not be prudent to suggest conventional borrowing much above that rate.

35. Grant aid may be assumed to continue to be available up to perhaps \$10 million a year. Again, however, this is anything but assured. Of total official capital requirements of about \$30 million a year, at least \$10 million a year should therefore, if possible, be obtained in the form of loans on concessional terms.

CHAPTER I

INTRODUCTION AND BACKGROUND

A. History

1. This history of the Kingdom of Cambodia dates back to the beginning of the Christian era. The early period is not well known, but Chinese records of the 4th century A.D. indicate that Fu-Nan, as Cambodia's territory was then called, was hindu in religion, using hindu laws, and was ruled by a Brahman King. Fu-Nan was overthrown by a vassal state Chen-La, inhabited by the Khmers, in the 6th century, and a legendary King Kambu Svayambhura gave the name Kambuja to the country.

2. Between the 9th and 14th century, at the peak of the Khmer empire, it included all of present Laos and much of Viet Nam and Thailand. The now famous buildings of Angkor were erected in that period. In the 12th century, King Jayavarman VII introduced buddhism to Cambodia which still today is the state religion. He was the greatest builder, but after his death the empire began to fall apart. The Thais, under Mongol pressure from the north, invaded Cambodia and temporarily captured Angkor, the capital city, in 1353.

3. For several centuries both Thailand and Annam (North Viet Nam) invaded parts of Cambodia's territory, trying to gain control over the country. In 1846 Thailand and Annam joined together in crowning a Cambodian King, Ang Duong, founder of the present dynasty, under dual vassalage. The King however turned for protection to France, which was then fighting Annam. In 1864 the French Protectorate was proclaimed, and Norodom, the eldest son of Ang Duong, became King. He was succeeded in 1904 by his brother Sisowath.

4. Prince Norodom Sihanouk, great-grandson of Norodom, became king in 1941 at a time when Thai forces, encouraged by the Japanese, attacked the French in Indochina, and with Japanese diplomatic intervention forced them to a peace treaty stripping Cambodia of its western provinces. With the Japanese military expansion, Indochina came under their control and in 1945 the French administration was removed and the country declared independent by King Sihanouk. However, with the collapse of Japanese power, French troops reoccupied Cambodia six months later, and a "modus vivendi" was signed in 1946, giving limited sovereignty to Cambodia.

5. Both nationalist and communist movements had sprung up in the meantime and pressed the government for obtaining full independence. King Sihanouk, having left the country in early 1953 with the vow not to return before having secured full independence from the French, successfully took advantage of the weak French position in the Viet Nam war. Military command of the country was transferred to the Cambodians themselves on November 7, 1953 and independence was declared two days later. Recognition of Cambodian sovereignty was formally accorded in 1954, shortly after the conclusion at the Geneva Conference of an agreement providing for the withdrawal of all French forces.

6. In the intervening period, the internal situation had been bordering on chaos. After a new constitution had been promulgated in 1947, establishing parliamentary government, various factions had come to the fore, and personal feuds broke out in the National Assembly, leading to a quick succession of administrations, until in 1952 the King took full powers outside the Constitution, under a "Royal Mandate", dissolved the National Assembly, and appointed a new government under his direct rule.

7. Independence having been obtained, a nation-wide referendum was held in 1955 to vote whether or not the King had fulfilled his mandate. The referendum was overwhelming in his favor. Having obtained the acclaim of the nation, he resigned from the throne in favor of his father and started to build his own political party, the Sangkum Reastr Niyum (People's Socialist Party) with the aim of creating a more solid base for parliamentary government.

8. The Sangkum under the leadership of Prince Sihanouk became a most effective political instrument and over the years has been virtually in control of parliament. Prince Sihanouk as Chief of State has been energetic in promoting national unity and in defending Cambodia's interests in the international field. While remaining head of the Sangkum national movement, he has recently had occasion to express strong dissatisfaction with the parliament by referring to their corruption and narrow self-interest.

B. Political Background

9. During the 16 years since Independence, Cambodia has enjoyed peace. Earlier attempts by the Viet Minh during the mid-fifties to build up subversive elements among the Khmer population were largely unsuccessful, mainly for lack of grievances by the Khmers against the Sihanouk government. Nevertheless, in the difficult period prior to Independence a "People's Liberation Army" was formed in Cambodia, and the communists, trained and directed by Vietnamese, held some stretches of Cambodian territory. Under the Geneva Agreements, however, Vietnamese communist forces withdrew from Cambodia, and what was left of local communist supporters either withdrew with them or accepted King Sihanouk's pardon. Still there are today some leftist activists operating under Viet Cong guidance from Viet Nam. Similarly, a number of "rightist" rebels, operating partly from inside Thailand, are causing occasional insecurity in the southwestern parts of Cambodia. They are said to be inspired by Son Ngoc Thanh, former World War II leader of the Khmer Issarak (Free Cambodia) movement, Japanese appointed prime minister before the return of the French, one-time ally and later foe of Prince Sihanouk. This dissident nationalist movement (today under the name of "Khmer-Serai") as early as 1947 had set up a "Free Cambodian Government" in Bangkok, which for a time enjoyed recognition by the short-lived leftist Thai government of Pridi Phanomyong while Thailand served as a transit base for supplies to the Vietminh who were fighting the French from the other side. The movement partly surrendered to King Sihanouk, and partly disintegrated. Today, the Khmer-Serai, causing occasional incidents, occasional surrender, and ceremonial pardon, form part of the national scene, and occupy disproportionate space in speeches and national magazines.

10. What is more serious is the presence of at least 40,000 North Vietnamese and Viet Cong combat troops on Cambodia territory, mostly in uninhabited forest areas in the East, which they use for transit and retreat in the Vietnam war. The Cambodian armed forces, smaller in troop strength and less well equipped and trained, cannot seriously consider engaging them in the defense of Cambodian territorial integrity.

11. Cambodia maintains diplomatic relations with most countries except with Thailand and with the Saigon Government, neither of the latter having officially recognized Cambodia's frontiers. Relations were recently established with the provisional FLN Government of Viet Nam.

12. Cambodia as a nation today is more solidly established than it appeared ten years ago. The fact that a moderately progressist opposition group, now emerging partly within and partly without the present government, is focusing attention on relatively subtle economic policy issues, is an indication that basic facts of national existence are taken for granted. Given also the fact that the vast majority of the present population own their own land, and that in industry, commerce and banking it is the excessive degree of state capitalism that is at present giving rise to dissatisfaction, it follows that the chances for successful communist propaganda is far less than in several other countries of Southeast Asia. Short of outright military aggression a communist takeover therefore appears highly implausible.

13. A certain hostility still exists between Cambodia and Thailand. At present, it is focused on an ancient temple which is cut by the political border. A ruling by the Court of the Hague in favor of Cambodia is not accepted by Thailand, and therefore, a continuing border dispute prevents the establishment of diplomatic relations. There are some signs, however, that this issue may be resolved in the near future.

14. Prince Sihanouk has persistently followed a policy of neutrality between the Eastern and the Western bloc. Growing U.S. influence in Cambodia in connection with a substantial military aid program led to the unilateral termination of U.S. assistance by Cambodia, and initiation of a policy of self-help, in 1963, followed by severance of diplomatic relations with the U.S. two years later. Relations have been reestablished a few months ago, but no military or economic aid is sought from the U.S. Instead, more reliance is now placed on multilateral aid. Cambodia is not a member of any regional defense or other treaties, but participates, e.g. as a member of the Mekong Committee, in UN-sponsored activities.

C. Government

15. Cambodia is a constitutional monarchy. The king convokes and dissolves parliament and promulgates its laws, issues royal decrees,

appoints the members of the executive, commands the armed forces, signs and ratifies international treaties, etc. At present there is no King but Prince Sihanouk exercises these royal functions as Chief of State.

16. The National Assembly is elected by universal direct suffrage. It prepares and passes the laws of the country. In practice, although constitutionally it controls the executive, it is itself controlled by the Chief of State who is the founder and leader of the Sangkum Reastr Niyum, which is today the sole political party and holds all the seats in the National Assembly. The Chief of State is not responsible to parliament. This situation greatly reduces the role of parliament in controlling the executive, which is appointed by its own leader. What is more, all important national issues are discussed by the National Congress - instituted in 1958 as an assembly of all the people held twice each year in Phnom Penh, without any formal functions assigned to it by the constitution. The National Congress, however, by the fact that it has become a forum for the Sangkum, has acquired sufficient political weight to dominate legislative action, to be able to initiate constitutional reform, or to overthrow the government.

17. The Council of the Kingdom, theoretically an upper house, is composed of 24 members representing various socio-professional groups. In effect its role has become purely advisory, and even in this function, another consultative body placed under the King, the High Council of the Throne, seems to be of greater importance.

18. A counter-government, appointed by the Chief of State in his capacity as president of the Sangkum since 1966, was designed to fulfill the role of a political opposition but its activities today are limited to pointing up minor deficiencies in the executive and the administration.

19. The civil service of Cambodia is not a distinct and self-promoting institution with its own code of merit and selection. Rather, the appointment system originating from the top of the political organization tends to cause loyalty to be put above technical and professional merit. At the same time, it creates a certain insecurity of office and a tendency to take decisions on the basis of considerations unrelated to the national interest, or not to take them at all. A certain immobilization of the executive branch is a direct consequence of the complex interrelations within the body politic, where all the strings are held by the Chief of State. Prince Sihanouk, by the force of his personality, charisma, and by using the system within ill-defined constitutional rules, is able to monitor all activities of government of any consequence, and to thwart the decision-making process to his own will. The fact that he renounced the throne in 1955 should not be deemed to have in any way weakened his position. For the people at large, he has the potent image of being a direct descendant of an almost unbroken line of succession of god-kings, leading back over a thousand years into a past where recorded history is lost to legend, and whence the fate of the people is inextricably tied to that of the kings. While not formally head of either of the two Cambodian branches of buddhism, he is held by large segments of the population to be of a quasi-divine nature.

20. The advent of Cambodian independence, ostensibly wrought from the former colonial power personally by the Khmer King, had obviously favored the maintenance of a monarchic form of government. Furthermore, a strong-handed rule was called for in a chaotic internal situation interrelated with the military conflict in other parts of Indochina which, in different form, has continued to this day. Prince Sihanouk possessed unique prerequisites for unifying the nation during this period, laying the basis for the modernization of the country, including a massive build-up of the educational system, and steering the newly independent and exposed nation through an international situation in the surrounding region fraught with the danger of direct involvement in war.

21. It is clear that in the process of nation-building, political aims prevailed over strictly economic objectives. With the present government, the primary internal objective is political stability supported by an effort at promoting social progress. Single-minded pursuit of GDP growth, irrespective of income distribution and social relations, is an idea foreign not only to the Chief of State but to nearly all Cambodians. The emphasis on social equality is reinforced by the observation that large differences in wealth exist along ethnic differences, with the Chinese minority commanding disproportionate economic power. Another factor is that Prince Sihanouk personally seems to be influenced by the Physiocrat school of thought, where agricultural pursuits rank highest in productivity, while commercial and other service activities are looked upon as more or less parasitic.

22. It is against this general background, which in part also explains the relatively modest economic growth targets of Cambodia's five-year plans, that one has to view the limited success so far achieved in gearing the administration to the promotion of economic development. An important factor is also the level of pay scales for civil servants. Remarkably, teachers in higher education obtain the highest remunerations with a maximum of CR 11,000 per month (\$200). The average income of the upper civil servants, which are 3,200 in number, is CR 6,700 per month (\$120).

D. The People

23. The population of Cambodia at present is about 7.3 million. As to the growth rate, there is no adequate statistical base and estimates range between 2.2 and 3.6 percent a year, the former being the official figure. In all probability, it is somewhere between 2.5 and 3 percent. This would still be somewhat less than in other developing countries. The birth rate is estimated to be around 44 per thousand, which is comparatively high (only half of the girls under 25 years were married according to the 1962 census, and only 14 percent of the girls between 15 and 19 years of age), but the death rate is also still quite high at about 20 per thousand.

24. Of the total population, approximately 3 percent are recorded as Chinese and another 3 percent as Vietnamese, while 93 percent are Khmer. Demographic data are not reliable, however, particularly as regards ethnic groups. If semi-assimilated and mixed Chinese (Sino-Khmers) were included, their proportion might be closer to 7 percent. They are concentrated in urban areas - more so than the Vietnamese - and in Phnom Penh contribute roughly 20-40 percent, depending on the definition, to a total population of perhaps 550,000. Other and smaller minorities in Cambodia include Cham-Malays (today called Khmer-Islams) and Khmer-Leous. The latter are aborigines of Indonesian stock living mainly in the Eastern hills.

25. The Khmers, said to have moved into the Mekong Basin from a north-west direction 4,000 years ago, are physically and culturally distinct from the Thais as well as the Vietnamese, although there are points of resemblance with the former. The Khmer language like the Thai, particularly in script, is related to Sanskrit, while Vietnamese is not. The Khmers are generally stocky, oval-eyed, and relatively dark skinned, although the shades vary greatly. They are easy to distinguish from the Vietnamese - who are smaller in body structure and have more mongoloid facial features - and from the Chinese, but they are not so different from the Thais except for being somewhat more broad-faced. The Khmers are predominantly buddhist, belonging to the Hinayana or Theravada School which dominates also in Laos, Thailand, Burma, and Ceylon. Yellow-robed monks (bonzes) are a distinctive feature of the Cambodian scene, and they retain substantial influence in social and even economic affairs in the countryside. For one thing the pagodas are not only religious sanctuaries but an important educational institution. Also, they are often comparatively affluent and are able to help villagers in distress. This is one of the reasons why begging is not seen in Cambodia. The city of Phnom Penh is multi-religious with its large number of Chinese (some of whom maintain a form of Mahayana buddhism), of Vietnamese who are mostly Catholic, and some Khmer-Islams.

26. While in numbers the Khmers represent the vast majority of the population, the Chinese and Vietnamese play an important role in commercial, handicraft, industrial, and financial activities. Many Chinese, of whom there had been immigrants through the centuries, are assimilated through intermarriage, and there is a web of family relationships between Khmers and Chinese. Nevertheless, the latter form a closely-knit community, especially since a great number of them immigrated more recently under the French Protectorate. Their schools use the Chinese medium, but the Cambodian language is a compulsory subject.

27. While the Chinese specialized in urban pursuits and rural trade, the Vietnamese, by contrast, who mostly came during the Protectorate, either settled on the land, partly displacing Khmer farmers, or were used by the French for administrative jobs. They also later engaged in political activities. For these reasons, their presence is more widely resented by the Khmers than that of the Chinese. The Cambodian attitudes toward the latter is an ambivalent mixture of respect (Chinese men are sought after for marriage to Khmer girls) and of social resentment.

28. On the government level, there is still another point of view for judging the position of the Chinese: their difference from the Khmers in being able to migrate to Hong Kong or Singapore without loss of happiness, and their having financial and business ties with these places so that they are able to escape all manner of control by the state. What is worse, their dominance of commerce in Cambodia has enabled them, as a group, to control and manipulate prices not only of both essential and inessential urban consumer goods, but of rice to the farmer. It was in part the resulting suspicion, if not fear, of the Chinese business class that led the government in 1963 to adopt the nationalization of foreign trade, banking, and insurance.

E. Recent Developments

29. The first ten years of independence (up to 1963) were a period of political consolidation and nation-building. During that time the Sangkum party became a rallying force for the country's energies to be channelled into constructive enterprise and social advancement. A massive program for the promotion of education, health, and other facilities for the people was successfully brought under way. These efforts were facilitated by financial assistance from abroad, averaging over \$50 million a year, mostly from the U.S. which in this period provided about \$350 million, including defense support, but also from France and the Eastern Bloc. Private enterprise also played a role and savings increased. During that period, GNP grew at an average compound rate of 6.5 percent.

30. Nevertheless, the Chief of State and his government looked with growing concern on the increasing disparities of rural and urban incomes, and the conspicuous wealth of the business community, believed to originate in speculation, rigging of markets, and other unsound practices. Relations between government servants and the private sector tended to be degraded by overt corruption.

31. At the same time the U.S. aid program in Cambodia, with the increasingly conspicuous presence of an official U.S. establishment, became less and less compatible with the Chief of State's view of Cambodia's interests as a neutral state in a region torn by military conflict with direct U.S. involvement. These were the motives for Cambodia in 1963 serving notice to the U.S. for termination of aid.

32. A new era of "Self-help" was thus inaugurated. To lay a sounder base for such a national effort, the Chief of State in November 1963 announced a set of Economic Reforms, consisting of (a) the nationalization of banking and insurance, and prohibition of private firms in these fields, and (b) the nationalization of foreign trade through the creation of the

Societe Nationale d'Exportation et d'Importation (SONEXIM) with the attributes of a state monopoly. Thus a half-dozen (mainly European) trading companies and a large number of Chinese merchants and trading firms were replaced by one single organization, which was initially constituted as a mixed enterprise with a minority private participation, but three years later became totally state-owned. A number of other state enterprises was created or expanded to perform associated functions like procurement of rice for export (Office Royal de Cooperation - OROC), domestic wholesale trade (Societe Nationale des Produits d'Importation - SONAPRIM) and the state retail enterprise Magasins d'Etat (MAGETAT).

33. The new policy failed to produce the desired results if judged by economic developments since 1963. For one thing, private investment in productive enterprises stagnated and later declined, and for a time the flight of private savings into real estate caused a boom in residential construction in Phnom Penh. Official capital inflow for investment was reduced to a trickle. SONEXIM had first to be built up, and when it was functioning, part of its operations did not amount to much more than levying a fee and officially controlling what was still some kind of private trade.

34. Real GNP growth from 1963 to 1969 has been at an average of about 3.0 percent a year, barely above population growth. Government revenues failed to keep pace with expenditures, and in spite of announcements of a financial austerity program, the current deficit threatened to become a permanent feature of government finances. An economic malaise developed, in recognition of which the Chief of State in March 1968 approved a new law which drew the line between industries reserved for the public sector and those left to the private sector, in such a way as to give more opportunities for private investment. Subsequently, in December 1968 he officially announced a change from the period of self-reliance and a closed economy to an "open" policy, the creation of a Committee for Economic and Financial Recovery, and the application for membership in international financial institutions including the Bank.

35. The newly created committee was not, however, effective in proposing measures for economic recovery, and in August 1969 the government of Prime Minister Penn Nouth resigned and was replaced by a new government under Lt.-Gen. Lon Nol as prime minister, who had been an old-time associate of the Prince during the struggle for independence.

36. The new government took office with a "carte blanche" from the Chief of State to remedy the stagnating trends of the economy. As a first step, the currency was devalued on August 18 from CR35/\$ to CR55.5/\$, coming close to the black market rate of approximately CR60/\$. No other measures have been taken since then, but important "liberalization" proposals have been under preparation, including the partial dismantling of the State Monopoly in foreign trade and the re-introduction of private foreign banks.

37. In October, Prime Minister Lon Nol departed for a prolonged stay in France for health reasons, leaving the affairs of Government in the hands of Vice Premier Sirik Matak, scion of the Sisowath family preceding Norodom Sihanouk on the throne. Frictions between the government and the Chief of State apparently delayed the adoption of new economic measures by the Government, pending uncertainty regarding the prospect, not of parliament approval which was certain, but of ultimate promulgation by the Chief of State. The new measures were reportedly adopted in principle on November 15 by the Council of Ministers, but were not submitted to parliament before the mission left.

38. "Liberalization" as presently discussed in Cambodia inevitably carries with it a reappraisal of relations between different ethnic groups, mainly regarding the role of the Chinese who had been principally affected by the previous nationalization drive. Distrust of the Chinese and fear of their renewed exploitation of both farmers and consumers are important factors in delaying action towards liberalization, after a period of Khmer middle-class ascendancy through the proliferation of state enterprises.

CHAPTER II

THE ECONOMY

A. General Performance

39. For a population of about 7 million, the Cambodian economy provides for an income level, at present, of about CR 6,000 per head per annum which, at the present exchange rate is equivalent to about \$110. This is somewhat below what it is in neighboring countries, e.g. in Thailand where it is estimated at \$150. While such comparisons are not seldom misleading, particularly if internally-consumed crops are priced differently, it is true that the Cambodian economy is dominated by a relatively stagnant agriculture, with lower yields of foodcrops than in most countries in the region. With a total population of one-fifth that of Thailand, agricultural income in Cambodia is one-sixth, 1/ and the value added in Thai industry is ten times what it is in Cambodia.

40. Agriculture (including fisheries and forestry) accounts for roughly 40 percent of GDP, but the proportion of Cambodia's population living on the land is twice as high or about 80 percent. This gives a measure not only of the difference in income levels between the urban and the rural areas, but also of the importance of agricultural issues in national politics, and the emphasis placed on agricultural development by the authorities, particularly since agriculture also provides virtually all of Cambodia's exports in the form of rice, rubber and various other products.

Value added in	Share in Total GDP					Annual Compound growth rate 1952-1969
	1952	1955	1960	1965	1969	
Agriculture	56	49	45	40	38	2.7%
Manufacturing	10	9	9	11	12	6.3%
Commerce	20	22	22	24	21	5.4%
Construction	2	2	5	4	6	12.1%
Government	6	12	13	14	16	11.5%
Other	6	6	6	7	7	5.9%
Total GDP	100	100	100	100	100	5.0%

Source: Appendix Table 2.1.

1/ The difference is probably somewhat less in real terms. In the case of paddy, which is the principal crop in both countries, the domestic price used in calculating the value added, and converted at the official exchange rate, is \$50 in Thailand and about \$40 in Cambodia.

41. While population may be assumed to have been growing at about 2.5 percent a year during the whole period shown above, real GDP as a whole expanded about twice as fast, notwithstanding a substantial slowdown to an average growth of only 3 percent in the last six years.

42. In agriculture, a third of the total sector originates from rice production; the remarkable fact is that over the whole period, as seen above, the agricultural sector as a whole has grown at only about 2.7 percent a year on average, which means it has been expanding at just about the same rate as population, while the contribution of paddy increased only 2.2 percent a year. As will be noted in the next section, yields of paddy have not changed at all and the increase in production from about 1.6 million tons in 1952 to 2.5 million tons in 1969 has been the result simply of the growing population bringing additional land under cultivation. While it cannot be said that in this process the expansion has been into "marginal land", it is true that the best lands have been fully occupied long ago.

43. Manufacturing industry represented 10 percent of GDP already in 1952, but this reflects a relatively high level of handicraft activity rather than organized industry of more modern type. During the French rule, Cambodia was mainly an agricultural hinterland and industry was not encouraged or promoted, with the exception of a few branches like rubber processing for export. Since 1952, industry has grown at 6.3 percent a year and the percentage in GDP has increased to 12 percent with the installation, since independence, of a number of new factories producing textiles, glass, cement, sugar, tires, as well as cigarettes, processed foods, and beverages. However, the limitations of the domestic market have not made it possible for import-substitution industries to become an engine of growth. It appears, rather, that in the five years from 1955 to 1960 the combination of a rapid growth of expenditures by the government sector (by 25 percent a year) and of an 8 percent annual increase in agricultural production had a stimulating effect on industry which during that time advanced at the pace of over 9 percent a year. This was in a period when hardly any new factory-scale establishments had yet been completed, and must have been due largely to increased utilization of existing capacity. In subsequent years when agriculture tended to stagnate, industrial growth also slowed down (to 7.5 percent per annum from 1960 to 1965).

44. In the first five years of independence, then, the economy was moving ahead at an encouraging pace with real GDP growing at about 9.5 percent a year. This happy condition did not last into the sixties. From 1960 to 1962 rice yields were subject to climatic deterioration, production declined and exports of both rice and rubber fell to low levels. After a general but very temporary recovery in 1963 when exports reached new heights with a record rice crop, and industry and construction settled at a level more than a third higher than in 1960, the process of growth underwent a lasting setback after the nationalization of foreign trade and banking, and the phasing out of U.S. assistance. Both construction and commerce, after a period of decline, by 1969 have just barely recovered to the 1963 level, and agriculture, the largest sector, advanced at the pace of only 2.1 percent a year, which is slower than population growth. It must be noted that given its relatively small size, manufacturing industry could not have

provided a force to impart greater momentum to the economy, even if full rein had been given to private enterprise. After the 1963 reforms, as a matter of fact, industry was the only sector (other than government itself) which showed considerable strength, as a number of newly established plants came into operation in the public sector; value added in manufacturing increased, as in the second half of the fifties, by 9 percent a year from 1963 to 1969.

B. Agriculture

General

45. Nearly two-thirds of the active population of Cambodia are rice farmers, occupying 80 percent of the cultivated land and contributing about 15 percent of total GDP. The active population engaged in agriculture is estimated at just over 2 million or about 80 percent of the total, and has been growing at probably not much less than 2.5 percent a year since 1962 or somewhat below the national total. The value added by agriculture, fisheries, livestock and forestry in the last 10 years has evolved as shown below.

Primary Sector GDP, in Percent

	<u>1959</u>	<u>1969</u>	<u>Compound Change % p.a.</u>
Paddy	40	34	0.9
Fruits	13	16	4.9
Vegetables	3	6	9.7
Other crops	12	12	3.8
Rubber	5	4	negl.
Forestry	13	8	-1.5
Livestock	8	14	8.1
Fisheries	<u>6</u>	<u>6</u>	<u>1.7</u>
Total Primary Sector	100	100	2.7
Value added (CR million) ^{1/}	10.3	13.4	
Percent of total GDP	42.2	38.2	

^{1/} 1966 prices

46. About 80 percent of all farmers own their own land. The remaining 20 percent are tenants, mostly in the provinces of Battambang (35 percent of the cultivated land), Prey Veng and Suay Rieng (about 10 percent of the land). Rents vary between CR 600 and 2,000 per hectare, mostly in kind. Sharecropping also exists.

47. Ploughs are usually wooden with metal shares (cost CR 500-800). Traction animals are mostly a pair of bullocks (CR 10,000-15,000) or buffaloes (CR 8,000) Cambodia has a population of about 2.4 million cattle (mostly bullocks) and 0.9 million buffaloes. Tractors of which there are 1,500 (half of which Massey Ferguson) are used only in areas with relatively large holdings (e.g. Battambang). They are difficult to use in the lowland which is inundated or muddy when work is needed. Only 250 motor cultivators are in use, but diesel pumps are increasingly used. 1,300 pumps were counted in 1968.

48. Seed, particularly rice, is generally produced by the farmers themselves, without organization or control, except in the case of industrial crops (cotton, jute, tobacco). Chemical fertilizer is used only in limited areas; manure application is not widely practiced by farmers but has been the subject of a propaganda campaign. Plant protection materials have reportedly increased considerably in recent years but spraying is applied only on a few crops like cotton, which otherwise would be very seriously damaged.

Rice

49. While value added in crops and livestock in the last 17 years increased by 66 percent in real terms, rice has increased only 46 percent. However, rice accounts for 40 percent of the total value, and for 80 percent of the cultivated land. The area under rice has been growing along with the population except that since 1964-1965 it has stagnated at around 2.4 million hectares. ^{1/} Yields have been stationary at about 1 ton per hectare but are higher in certain regions (1.5 ton in Battambang or Kampong Cham) and lower in other (Prek Thnot). Although Battambang has fertile soils, it is exposed to hazards of climate and hydrology. For example, in 1968/1969 less than half of the paddy area actually produced rice because of drought. Most of the exported rice is grown in Battambang. Average holdings in Cambodia are not too small, around 3 hectare, but again this differs greatly between regions.

	Area (ha.)	Paddy (1000 tons)	Yield (kg./ha.)	Export (1000 tons)	
				Rice	Flour
1950	1,657	1,576	951	n.a.	n.a.
1955	1,743	1,484	851	25	75
1960	2,150	2,335	1,086	327	64
1965	2,344	2,500	1,066	473	73
1969	2,427	2,503	1,031	94	8
1972 ^{a/}		3,320	1,320		

a/ Plan target.

^{1/} An interesting phenomenon that can only partly be explained is that both rice acreage and the number of paddy farmers in the first half of the fifties increased more slowly than the population at about 4 percent in 5 years; in the second half of the fifties (following independence farmers increased 12 percent, acreage 24 percent, and production nearly 60 percent. Over the following five years, farmers increased 12 percent, acreage 9 percent, and production 7 percent.

50. No large-scale irrigation systems exist, and in general only one crop a year is possible. Slightly more than half of the paddy acreage is rainfed with paddy usually replanted with a growing season from June to December. The balance is grown in areas flooded annually by the Mekong and its tributary rivers, normally from July to February, including floating rice on about 15 percent of the total area under rice. Some dry season paddy is also grown, particularly in Prey Veng, Kandal and Takeo, accounting for about 5% of paddy acreage. When the flood waters recede, water from ponds or storage tanks is used, and lift pumps have in recent years increasingly been used. An unusually large number of rice varieties are used for seed, leading to a lowering in the quality of milled rice. New local varieties as well as IRRI have been tried but either without satisfactory results or (as with IRRI) too recently to arrive at conclusions. Local hybrids have been developed and promoted for export, but they are photosensitive and have not proven suitable in taste for local consumption.

51. Cultivation practices remain traditional, with wooden implements, bullocks, and sickle, without line sowing, and with hand-made earth mounds to retain the water. Phosphate fertilizers (natural phosphate) have been in use for some time mainly in the South to combat browning disease, caused by soil conditions. Nitrogenous fertilizers are not yet used in large quantities - a total of 5,000 tons of urea in 1969.

	<u>Fertilizer Use</u> (000 tons)				
	<u>1965</u>	<u>1966</u>	<u>1967</u>	<u>1968</u>	<u>1969</u>
Phosphate	n.a.	11.3	12.7	17.5	27.0
Urea	n.a.	1.4	3.2	4.4	5.0
Other	<u>n.a.</u>	<u>0.6</u>	<u>1.3</u>	<u>1.1</u>	<u>n.a.</u>
Total	8.4	13.3	17.2	23.y	32.0

52. Over a thousand husking shops and 650 small rice mills are reported to exist. About a third of the output is marketed, traditionally through local traders (Chinese) but more recently also through State cooperatives under OROC (Royal Office of Cooperation), as well as through SORAPA, a subsidiary of SONEXIM, for export. Procurement prices are fixed by the government.

53. It is estimated that from the present 2.5 million hectares, further expansion of paddy acreage up to 3 million hectares would be possible, but after that no suitable soils would be available. In the long run, therefore, the maintenance or expansion of Cambodia's rice exports will be conditional on more intensive cultivation and increases in yields. Technically speaking, there is large potential for increased yield by developing water control, drainage and irrigation works that would in some areas permit double cropping, and in combination with fertilizer and improved seeds could achieve a doubling or perhaps tripling of yields. However, the organizational, institutional and human obstacles to such developments are formidable, even though dams and irrigation systems can be constructed. Adequate research has not

yet been done to determine fertilizer response in the various areas with different soil conditions. Extension services are weak and need to be built up. Institutional credit is scarcely available though an Agricultural Bank is in process of being established. Cooperatives have been disappointing in their operations. Seed research is not being pursued with adequate support. Finally, farmers are resistant to change. The government's efforts have not been negligible in the past, but the groundwork laid so far needs to be strengthened much more if tangible results are expected in future.

54. A Rice Development Program was started in 1969 by OROC with assistance from the French Technical Cooperation, based essentially on fertilizer promotion. The program is for 10 years and is to cover 700,000 hectares and nearly 400,000 farmers, with a target increase of 400,000 tons in production. The approach is through a concentrated training-for-extension effort with selected farmers being trained and served by a system of agents and engineers. The supply of fertilizer is to be effected through OROC. The success will depend, among other things, on the effective strengthening of the cooperatives and the availability of credit. Furthermore, the approach ought to be expanded immediately to include the promotion of small-scale water management and development, the use of improved seeds, and above all, the introduction of better cultivation techniques.

55. Priority attention to fertilizer use appears to have been superseded recently by a more balanced approach by the responsible authorities. Indeed, in statements made during 1969 the Chief of State has been attaching first priority to water management, relegating fertilizer promotion to an issue of secondary importance. The basis for this is not self-evident, and it is clear that large-scale irrigation works like Prek Thnot, Battambang, etc. should not be considered the primary means by which to increase rice production. For such projects to be economically worthwhile, there will have to be substantial effort to improve the technical knowledge of the area, the institutional support, and the economic incentives to use the facilities. Outside of project command areas there is also scope for the development of better water management practices, and in some cases new small-scale water control structures might be found suitable.

56. In addition to the points already made, the following subjects should be given special attention:

- establishment of fertilizer response on typical soils;
- research on rice varieties;
- improvement of seed multiplication and distribution facilities, including better ways of ensuring that specific varieties are used and not mixed; and
- exploration of ways to propagate the use of organic fertilizer, whose use is proven to have spectacular results.

57. The achievement of the Second Five-Year target of 3,320,000 tons of paddy produced by 1972 implies a relatively modest rate of growth, but does not appear easy to achieve. Despite a policy of price support and the initiation of official procurement activities, total output of rice

has hardly changed since 1963 except, perhaps, for the record 1969/1970 crop which seems largely a result of very favorable weather.

Rubber

58. Rubber occupies only 2.3 percent of the total cultivated area, but in terms of value added it accounts for three times as much. Most of it is exported, and rubber exports are second only to rice in earnings, and more stable than the latter in spite of changes in world prices.

59. Prior to Independence, all rubber was planted on a large scale by private French companies, but subsequently, smaller local plantations and smallholder rubber also developed up to a point. From 1956 to 1968 total area planted has doubled from about 33,000 hectares to about 67,000 hectares. With 39,150 hectares in tapping in 1967, production was 53,000 tons, giving an average yield of 1.37 tons/hectare which is considerably higher than in Malaysia. It has to be kept in mind, of course, that out of this acreage only 4 percent was smallholder rubber whereas the proportion in Malaysia is 60 percent. For 1969 a drop in production occurred owing to defoliation damage. Actual production data for the year are not yet available but damage claims for \$8 million are under negotiation with the U.S. Government.

60. Nearly all rubber plantations (92% of the area) are on the "red soils" in the provinces of Kampong Chham and Kratie, and 7 percent in Ratanakiri. Five French companies hold 70 percent of the area planted (46,000 hectares); their concessions are nearly fully planted so that in future this proportion will diminish.

61. Two large state plantations are operated by the Office de Mise en Valeur des Terres Insuffisamment Developpees (OMV), a special office in the Ministry of Agriculture; the larger one is the Preah Sihanouk plantation in Ratanakiri, set up as a pioneering unit for the opening up of that province, where an estimated 150,000 hectares of virgin "red soils" particularly suited for rubber, are available. So far 4,000 hectares have been planted on Preah Sihanouk by Compagnie du Cambodge, the largest French company, on behalf of OMV, and the latter is expected to continue new planting at a rate of 500 hectares per annum. Besides these and a few smaller state plantations, a number of private Cambodian estates have been established, many in proximity of large plantations, but their status and acreage is not known with any precision. Many of them have been successful, and they are to a large extent based on high yielding clone material^{1/} which is available in sufficient quantity from the private companies, who are approaching the point where their activities will be limited to replanting.

62. The Cambodia Rubber Research Institute (IRCC), financed by a specific tax amounting to CR 0.5 per kg of rubber produced (about 2 percent

^{1/} Reaching yields of 2 tons/hectare or more in the 12th year and up to 3 tons/hectare after the 20th year.

of the value), paid by members of the Planter's Association, is modern and efficient. Attached to the University of Kampong Cham, it also issues export certificates for specific rubber qualities.

63. Besides smoked RSS sheets, concentrated latex has accounted for one-third of exports in recent years, and new types of processing are increasingly used. ^{1/} In 1967 with the decline in world natural rubber prices, the government introduced minimum guaranteed prices for export, and export taxes above ceiling prices. The schedule at present is as follows:

FOB Contract Price (CR per Kg)	
< 20 ^{a/}	guaranteed price 20 ^{a/}
20-24	-
24-28	25% tax on increment
> 28	50% tax on increment

^{a/} CR 15 prior to the devaluation in August 1969.

The subsidy in 1967 amounted to over CR 40 million, but in 1968 taxes were collected. Prior to the devaluation the average cost of production was estimated to be somewhat below CR 15 per kg (equivalent to US¢ 12 per lb. at the new exchange rate) but it is not yet clear by how much the costs have increased with the higher price of imports and the recent wage adjustment; producers claim that the costs will go up by 25 percent (to US¢ 15/lb.) but this may be on the high side. Cambodia producers are thus very competitive at the new exchange rate.

64. The mission made attempts to verify the availability of additional land suitable for rubber in the lower Mekong basin (Kampong Cham) but it appeared that most of the estimated 190,000 hectares of red soils are either planted (61,000 hectares) or occupied by farmers growing other crops, and the remainder consists of scattered patches which, to judge from aerial inspection, in most cases are less than 2,000 hectares. No such constraints exist in Ratanakiri province, but this part of the country being virtually unpopulated (and at present militarily insecure) the problem of obtaining and settling the required labor force is considerable, aside from the area being malaria-ridden. Transport costs would also be higher, but this could be absorbed if other conditions were fulfilled including management efficiency and know-how comparable to that obtaining on the French estates. This is by no means assured if private investment cannot be attracted into the region. The OMV, created in 1964 specifically to promote rubber in Ratanakiri, operates as an administrative service of the Ministry of Agriculture, and is very inadequately staffed even to operate the existing

^{1/} Granulation of Initial Concentration Rubber (ICR), DECAN and DYNAT-GUTHRIE processes.

plantation, to say nothing of organizing smallholders settlements or undertaking a new State plantation. For such tasks, therefore, the organizational structure will need first to be put on a stronger, and preferably more autonomous basis, and for the time being the current and perhaps accelerated planting program at Preah Sihanouk will be all that can efficiently be carried out. However, preparation for longer-term planning in Ratanakiri ought to be taken in hand, and as far as the lower Mekong is concerned, a survey of available land should be given first priority, with a view either of rounding off existing concessions, or to prepare for a more organized approach to the settlement of smallholders, or both.

Coconut

65. Coconuts are generally not processed for copra. Present production is about 15 million nuts (2 per capita per year) on about 10,000 hectares, and all is domestically consumed. The price paid is up to five times the world market copra value per unit, due to strong demand.

66. Along the south-west coast below the Cardamome mountains about 110,000-115,000 hectares of mangrove-covered land is believed, with appropriate embankments and drainage, to be very suitable for coconut plantations, possibly in combination with sweet potato, rice and pineapple in the initial years. Private plantations have produced encouraging results, and a research station at Tuk Sap has been established. Large-scale plantations in blocks of 200 hectares plus smallholder plantings in the vicinity (with less problems than in the case of rubber) are suggested; a systematic study does not seem to have been made but would appear worthwhile to be undertaken immediately. The owner of a private plantation is already planning to install a small oil mill on his plantation.

Fruit

67. Fruits are an important part of Cambodia's agriculture. They include bananas, oranges, mangoes, papayas, litchees, durians and a variety of others, and total production increased from about 190,000 tons in 1955 to 240,000 tons in 1968. Considerable quantities, mainly oranges from the Battambang province, are exported to Viet Nam at present. There is little processing or juice-making.

Vegetable

68. Vegetable production according to statistics has increased more rapidly than fruit; both in terms of acreage and output, vegetables nearly tripled since 1955 to a volume of 228,000 tons in 1968. Exports to Viet Nam have also in this case grown considerably in recent years, particularly as the vegetable growing environs of Saigon became increasingly insecure after the Tet offensive. With peace in Viet Nam, however, exports should cease. Beans 1/ are not treated as vegetables in the statistics. They

1/ Principally phaseolus aureus or "green bean".

occupy 62,000 hectares, are produced for dried seeds, with yields of 400 kg./ha., and important quantities have been exported in some years.

Maize

69. Maize had been developed before World War II for export, and production at the peak was 400,000 tons in 1937. It disappeared but has been reintroduced since 1948. In 1964 production reached 204,000 tons but it has since again declined. White grain varieties are produced for the domestic market, red maize for export to Singapore, China, Japan, Hong Kong and Eastern Europe (81,000 tons in 1968). These exports have been subsidized prior to devaluation but since then the price paid to producers is about equal to world prices. Yields are relatively low at 1.5 ton/hectare but development of this crop seems possible. A mixed enterprise SOCTROPIC with Japanese participation has plans for maize growing. A starch mill for export based on maize had been proposed in the Second Plan to be built at Sihanoukville, consuming 150,000 tons per annum. However, no further studies have been made and nothing has happened for the plant.

Sugar

70. Sugar, made domestically from sugar palm juice but supplemented with raw sugar imports (amounting to a fifth of total consumption), shows a comparatively low consumption level of 7 kg/year per head, or a total of about 50,000 tons, including home-made molasse sugar.

71. Of perhaps 2 million palm trees a third is reportedly tapped, (at the trunk 50 feet above ground) each yielding some 60 kg. of molasse sugar after boiling the juice, which requires large amounts of firewood and therefore is relatively costly. A refinery was installed at Kampong Tram under a Czech loan in 1964 to use this material, but it was discovered that molasse sugar had to be turned into raw sugar before it could be refined; a sugar mill was annexed to the refinery in 1966 with local means, and the refinery is now working with half imported raw sugar and half raw palm sugar. The cost is high at CR 18 per kg.

72. About 6,000 hectares of land are under sugarcane, consumed raw, but plans are afoot to produce cane sugar on a commercial basis in Battambang province (Kampong Kol). A conclusive study has not been made on water requirements or on varieties to be used, and the large sugar mill project (10,000-15,000 tons) now envisaged ought to await the outcome of a study. More costly mistakes in the field of sugar ought to be avoided.

Cotton

73. In cotton, the volume of production over the years has been quite erratic owing to difficult problems of plant protection. Recently, production has been around 6,000 tons of seed cotton, purchased at CR 12 per kg by the two modern ginneries at Andoeuk Hap and Kampong Chham. These in turn supply two SONATEX spinning mills. Experiments have been made with medium-long staple varieties (Acala) to supplant imports for the production of fine fabrics.

Jute and Kenaf

74. Jute and particularly kenaf production was greatly expanded from 1,500 tons in 1967 to 8,000 tons in 1969 to supply the jute mill established in 1967 by SOKJUTE near Battambang. Climate and water conditions appear on the whole favorable but the existing locations are less than ideal; yields are not above 1 ton/hectare on average, but in good years reach 2-2.5 ton/hectare for kenaf and 1-1.5 ton/hectare for jute. Prices of CR 7 per kg offered by SOKJUTE are so high (and ruinous for SOKJUTE) that cultivation is expanding rapidly and supply will soon exceed mill capacity. SOKJUTE presently supplies half of the country's sacking requirements with an output of 5,500 tons and another mill is contemplated. There are reasons, however, for viewing such a project with skepticism before a study has been made on bulk handling and other factors determining future demand for sacking, as well as growing conditions and price policies.

Other Crops

75. Other crops grown in Cambodia include kapok (partly for export), groundnuts, soybeans and other oleaginous products. Only little oil is used in Cambodian cuisine but possibilities should exist for export - a vegetable oil factory has been proposed in the Plan, using groundnuts, cottonseed and maize. Climatic and soil conditions appear not favorable for oil palm, and studies have been discontinued. Tobacco is an old established crop and Cambodia is self-sufficient with cigarettes which are produced with remarkable quality and variety. Pepper is a fairly important crop, largely for export, but production techniques presently in use are high cost, making Cambodian pepper barely competitive. Alternative cultivation techniques are known and could be applied in more suitable locations, bringing down costs. In coffee, Cambodia is self-sufficient but not competitive. Some tea is grown and possibilities are under study to extend cultivation for domestic consumption.

Livestock

76. Livestock contributes as much as 5 percent to GDP. During the last 15 years, cattle and buffalo numbers have more than doubled, as a result of sanitary improvements and expansion of work animal requirements. Pork and poultry have tripled. There are a few hundred head of elephants. Cattle structure is work-oriented (mostly oxen) rather than for meat production. Cambodian cattle (of local origin, crossed with indian zebu) however, produces good quality meat, and at present large numbers are smuggled on the hoof to the Saigon area. Slaughtering is carried out only by the Muslim and the Chinese. The only modern abattoir in Phnom Penh is still on the draft board but will soon be constructed with a Danish loan signed in November 1969. Dairy farming is not known and in fact Cambodian cows are relatively unproductive of milk. Instead, concentrated milk is imported for urban consumption. Attempts to develop dairying have not so far been very successful. In the long run, Cambodia has good potential for developing meat production for export. At present various obstacles exist; e.g. low meat prices almost prohibit the setting up of cattle farms with a reasonable return; the habit of growing and providing feed for

animals is not known to farmers, and the use of land specifically for this purpose needs first to be studied, and then to be promoted. A systematic effort in this direction ought to be undertaken.

Forestry

77. Seventy-three percent of Cambodia's territory or 132,000 square kilometers is covered with forests, but only 30 percent of this is dense rain forest, concentrated in the South-West. On the whole, forests are not very productive with present techniques of timber exploitation, and the contribution of forestry to GDP has been proportionately declining. Timber is extracted by private firms (including SOKECIA with Japanese participation) and by SONEF, SONASCIE and SONACO. Private sawmills are small-scale, produce only seasonally and to order. The SONACO plywood factory produced 3,300 tons in 1968 of which 850 tons for export. A second factory is envisaged to supply the growing domestic market. Logs are exported at a rate below 100,000 cubic meters annually.

78. To develop Cambodia's forestry sector a number of steps would appear desirable, including (a) a technical study of varieties not presently exploited, (b) improvement of extraction methods, (c) a study on rejuvenation and improvement of forests, (d) standardization and (e) establishment of modern large-scale sawmills and reorganization of existing ones. A U.N. Special Fund study carried out by FAO covers the Cardamome region but it has not yet been published.

Fisheries

79. Sweet water fishing is a traditional activity and the principal source of protein in the rural diet. The Great Lake has been a miraculously rich fishing ground, but of course the Mekong river and all its tributaries are important sources. Among numerous ways of catching the fish, one particularly noteworthy, when the water recedes, is to simply pluck the fish from the inundated trees as they re-emerge. Total sweet water fish production is estimated to have varied between 105,000 and 125,000 tons, but appears to have declined in recent years. Exports, previously considerable, have almost disappeared.

80. Several causes for the decline are assumed to be operative, including (a) cutting of forests inundated during high water season, having served as breeding grounds, (b) overfishing and (c) silting up of the Great Lake, with the reduction in depth causing too high water temperatures during the dry season. Some protective measures have been initiated, and the Fisheries directorate has requested FAO assistance for a study of the problem.

81. Marine fishing is less developed and produces about 40,000 tons per annum (mackerel, tuna) with small craft without refrigeration. A fish canning factory was recently set up at Khemarek-Phouminville. A beginning has also been made in the production of fishmeal. Shrimping is still insignificant but has considerable potential. Foreign capital has shown some interest in this field, and FAO has been asked to supply an expert in trawling.

Extension

82. The existing extension service under the Ministry of Agriculture has many weaknesses, the principal one being lack of staff. At Phnom Penh it consists of 1 engineer, 4 controllers and 8 crop agents. In the provinces there is generally one agent per Srok ^{1/} who is at the same time charged with control and statistics. Essentially, extension has focussed on the propagation of manure and fertilizer use, of vegetable and fruit growing, campaigns against rats, and use of lift pumps.

83. For industrial crops, special action is taken either by the Ministry (for cotton) or by the industry concerned, but with only moderate impact. Linkage between extension and cooperatives is very inadequate. Both are supported (and thus indirectly linked) by a national organization for community development "Action Pro-Populaire" (APP), a political organization with a Central Committee and local committees structured all the way down to the village. The village committees are composed of official, private, and religious personalities including a representative of the local cooperative. The committee is in charge of supervising the cooperatives and of facilitating rice procurement, selection of model farmers, organizing meetings of farmers, etc. The APP essentially acts from above and leaves little opportunity for the lower echelon to express itself.

Cooperatives

84. The Royal Office of Cooperation (OROC) was established in 1956. Prior to the emergence of cooperatives, and to a large extent still today, the average farmer was tied in with the rest of the world almost exclusively through the local merchant who supplied him with consumer goods, inputs, and credit, and to whom he supplied the part of the crop which he did not himself consume. This system was conducive to indebtedness, the total amount of which today is unknown but estimated at perhaps CR 2 billion.

85. OROC started with setting up provincial credit cooperatives and consumer cooperatives. Both were unsuccessful and are in process of being phased out in favor of multipurpose cooperatives, of which there are about 620 functioning today. They are able to supply goods as well as credit, which they obtain from OROC. Besides these, there are also youth and production cooperatives, and the Regional Cooperative Unions (UNICOOPS), established in 1966, are in charge of paddy procurement. All are under OROC. Total membership in 1969 was 434,000 of which 264,000 are members of multipurpose units - roughly one out of four farmers. Effective action, however, is less than this would suggest; marketing of consumer goods has remained at not more than about CR 60 million per annum; whereas sales of "means of production" has increased beyond CR 100 million in 1969, this

^{1/} Subdivision of Khets (provinces); Sroks again are divided into Khums, and Khums into Phums (village level).

has to do with the fact that OROC has the legal monopoly for fertilizer and pesticides, which by itself poses a few problems since they are made available on credit only to member-farmers. Paddy procured through UNICOOPS increased by 1967 to 178,000 tons or fifth of the marketed crop, but it has since sharply declined. One of the problems has been repayment of credit by the cooperatives, who in two years defaulted to the extent of CR 70 million. Also, due to the absence of modern rice mills in the cooperative system, they are forced to depend on private milling. Farmers have reportedly turned back to private channels for the sale of rice in many cases because, it is said, they obtained better prices (not counting interest on advances).

Credit

86. Seasonal credit (7% interest to coops, 12% to farmers) through OROC in 1967/1968 reached a high of CR 107 million, of which CR 90 million of new credit for paddy - which, CR 500/hectare, would cover requirements for 7.5 percent of the total paddy acreage. It dropped the following year as OROC was left with inadequate resources considering the volume of non-repayments. Repayments were 33 percent of amounts due in 1967/1968 and 24 percent in 1968/1969, resulting in a growing liability.

87. Medium-term credit through cooperative is virtually non-existing, and long-term (7 years) credit has only recently been introduced to rubber smallholders, who pay 7% interest.

88. Cooperative credit appears to have reached a point where, after a swift expansion, the emergence of institutional problems puts a brake on further development, and the difficulty with getting the money back paralyzes the system. Underlying this problem is (a) a lack of sufficient experience on the part of those in charge at all levels, and (b) the inherent tendency of the farmers to look upon cooperatives as an instrument of the paternal State, designed for the liberal distribution benefits. Thus, credit is repaid in priority to the moneylenders because of much higher interest rate.

89. A new Agricultural Bank (BAPAY) ^{1/} was formally established in September 1969. BAPAY will extend short, medium and long-term credit to cooperatives, agricultural associations and individual or familial agricultural undertakings. It may also participate in state and cooperative enterprises, or enterprises of an agricultural, industrial or commercial or financial character. Credits will in principle be combined with technical assistance, while priority will be given to those areas which dispose of adequate technical staff.

^{1/} Banque Agricole Paysanne, placed under the control of the Ministries of Finance and Agriculture and the Central Bank.

90. BAPAY is to start with an initial capital of CR 100 million. Its resources can be further increased through government endowments, loans from the state or other financial institutions and from foreign sources. It will also accept deposits. The mobilization of savings in the rural areas will be facilitated with the establishment of branches in the provinces and the promotion of Agricultural Funds (Caisses Rural de Credit) down to the villages.

C. Irrigation and Water Management

91. Given the irregularities of rainfall in the (South-West) monsoon period on the one hand, coupled with uncontrolled inundation, and the length of the dry season on the other, the future development of agriculture will be intimately tied in with progress in water control, drainage, and dry season irrigation.

92. So far only about 74,000 hectares are irrigated, of which nearly two-thirds are through historic irrigation works. One for 13,000 hectares is near Siem Reap with the artificial lake Baray Occidental, being part of the Angkor monuments, and the other at Bovel (Battambang), with a command area of 30,000 hectares. Existing works (small-scale reservoirs and deviation dams) generally permit only supplemental irrigation during the rainy season, and drainage is highly inadequate.

93. The Rural Works Division (Ministry of Agriculture) gives priority to improving existing systems and to create additional small-scale water control facilities for which 25,000 hectares were inscribed in the Second Plan. In addition, the farmers themselves are encouraged to build their own irrigation tanks and to use lift pumps. Small-scale water control and irrigation offer possibilities which, although technically limited by natural water availabilities, have the advantage of being cheap, particularly if carried out with voluntary labor. Much more needs to be done to explore underground water reserves which are very little known.

94. Large-scale water projects are the responsibility of the Societe Nationale des Grands Barrages (SNGB), a semi-autonomous public body created in 1968 in connection with the first hydroelectric scheme at Kirirom. The SNGB is responsible for all activities in Cambodia falling, on the international level, within the terms of reference of the Mekong Committee.

95. Numerous possibilities exist for medium- and large-scale water projects, either on the Mekong itself or its tributaries, polders around the Great Lake, and in the delta. The largest project is Stung Treng on the upper reaches of the Mekong, with possibilities of irrigating up to 2 million hectares. A preliminary study by a Japanese Reconnaissance team in 1960 suggested a dam 61 meter high and a power capacity of 2.2 million KW (more recent estimates up to 5 million KW). The reservoirs would submerge the major part of Stung Treng province as well as part of Lao territory. A systematic survey has not yet been undertaken to permit the initiation of a feasibility study. Some seismic studies have been conducted

by Geofizica (Yugoslavia) and geological borings started by a French firm since 1967. At present, the area is militarily insecure. Not quite as gigantic but still very large would be a project proposed at Sambor, conceived mainly as a run-of-river power project (about 0.6 million KW) with possible irrigation of up to 100,000 hectares. Recent studies by a Japanese group concluded unfavorably on the possibility of using power on this scale in Cambodia.

96. Apart from these mainstream projects which are to be considered only in the very long-term context, several tributary projects have been pursued more actively.

97. The Prek Thnot project, in the vicinity to the west of Phnom Penh, is designed for all-year irrigation of an area ultimately to cover 70,000 hectares, with a dam on the Thnot River and a reservoir capacity of about 1 billion cubic meters. Two generating units of 9,000 KW each are expected to provide power to the extent of 50 million KWH in a normally wet year. The project was prepared within the framework of the Mekong Committee; Japanese and Israeli experts completed studies on the power and irrigation aspects, and detailed engineering was carried out by the Snowy Mountains Hydroelectric Authority of Australia. The project area is one of the most highly populated regions of Cambodia with comparatively unfavorable soil conditions and fragmented holdings averaging less than 2 hectares. Rice is virtually the sole crop with a very low yield of 0.75 tons per hectare on average. It is hoped that a combination of water, improved inputs and better cultivation would bring this yield to beyond 2 tons per hectare, and it is planned to introduce other crops in rotation with rice. An experimental farm with Israeli technical assistance has made farm trials as well as some agricultural extension to neighboring villages, but the location of the farm and its soil conditions are not considered representative of the project area.

98. The first phase of the project including the dam, the power facilities and a pilot irrigation zone of 5,000 hectares, has been taken in hand for execution in 1969. Of the total cost of \$28 million, the foreign exchange cost of \$19.3 million is financed by grant assistance and credits from a group of 12 countries. The UN Special Fund undertakes the study of the second phase for 35,000 hectares. The first phase is expected to be completed within four years, and after 1973 the SNCB expects to be able to extend the irrigation network at a rate of 5,000 hectares per annum. The financing of the second phase is not yet in sight.

99. The Battambang project is for irrigation of 68,000 hectares immediately west and south of the city of Battambang, in an area which has traditionally supplied Cambodia's rice export surplus. Soil conditions are generally satisfactory and average holdings larger than elsewhere. Ninety percent of the project area is under rice with present yields of about 1.5 tons per hectare. A study of the project prepared, also under the Mekong Committee, in 1963 by SOGREA, concluded that the irrigation facilities would by themselves permit increases in yields to over 2 tons per hectare, and with intensified techniques they could go up to 4 tons

per hectare. An experimental farm under a special fund project at Banan was started in 1966 but its work has been delayed and so far only wet season rice experiments have been carried out.

100. The Battambang project, according to the original plan, is to be executed in four phases, starting with 23,000 hectares for irrigation over a 5-year period, on the basis of a deviation dam, followed by a storage dam and power generation facilities in a second phase. In the third phase the remaining irrigation works would be undertaken, and in the fourth phase the height of the dam would be increased and more power installed. A Swiss team is at present in process of completing a new survey of power markets (report expected March 1970) and is carrying out the detailed studies for the first phase (report expected March 1971). Tentatively it is now expected that the first phase, costing about \$10 million in foreign exchange plus about \$7 million in local currency, would be executed between 1971 and 1977. A second phase which would include the main dam and the power facilities would be started in 1972, to be completed also 1977. The Asian Development Bank is considering the possibility of financing the first phase.

101. The feasibility study for the Stung Chinit project has been completed by a Japanese team but the report is not yet available. The project is for the irrigation of 25,000 hectares, about 50 km. southeast of Kampong Thom, covering an area which also is almost entirely under rice. A 5,000 KW power unit is also proposed which would, among other things, supply power for pumping. Three pilot zones are to be established in 1970 with Japanese aid, and detailed engineering studies are expected to be completed by 1972.

102. In connection with these projects, the major and very difficult task of the government will be to create the conditions necessary for achieving the agricultural benefits expected from the new irrigation facilities. Given their long gestation period, some of these projects have been made multi-purpose projects by adding power generation in order to ensure an acceptable rate of return.

103. In existing irrigation areas water has so far been supplied free of charge. With the new projects this will have to be changed, but present proposals to solve the problem by reassessing the land values for land tax purposes do not seem to be a satisfactory answer.

104. The Rural Works Division who will take over the facilities from SNGB for operation, will have to be newly equipped to perform this function in cooperation with the water users. The erection of terminal irrigation structures is so far proposed to be left to the farmers, but the organizational aspects of this activity are still unresolved, and the difficulty in some areas like Prek Thnot are compounded by the need to consolidate and enlarge fragmented holdings.

105. New cropping patterns are to be evolved unless simply double cropping of paddy is possible, which is not certain for many areas. Marketing studies for new crops will have to be carried out in detail. But these are relatively easy tasks compared with the selection, provision

and actual use by the farmers, of a package of inputs with the help of extension services, cooperatives, and credit. In this general field, much will have to be initiated if not from scratch, at least with an entirely new approach.

D. Industry

106. At the time of independence, Cambodia had very little organized industry, but small-scale cottage and artisan-type industry, producing bricks, pottery, metalware, basketware, and wood products. These, together with traditional rice milling, other food processing industries and cigarette factories, accounted for 9 percent of GDP in 1955.

107. Prior to 1958, total investment in manufacturing may have been in the order of CR 50 million a year or less than 5 percent of industrial GDP, but in the following five years, with industrial state enterprises being started, it was about six times as much. Throughout the period since then, private and public investments have been about equal in importance, 1/ but whereas private enterprise largely concentrated in the Phnom Penh area and in fairly small-scale undertakings, the public sector took the lead, with the help of foreign bilateral assistance, to set up new large-scale industrial enterprises in various parts of the country. Since the 1963 reform public and mixed enterprises in industry have gone further ahead, while private investments started to dry up. The largest single investment in the public sector 2/ in recent years has been the Sikanoukville refinery, financed with the help of a French credit, but important public enterprises had been financed earlier by People's China (two textile mills, a hardboard and newsprint factory, cement plant and glass factory) and Czechoslovakia (tire factory, sugar refinery and tractor assembly).

Value Added in Manufacturing Industry
(Cr million, 1966 prices)

	<u>1953</u>	<u>Increase</u>		<u>Increase</u>		<u>Increase</u>	
			<u>per annum</u>	<u>per annum</u>	<u>per annum</u>	<u>per annum</u>	
		<u>%</u>	<u>1958</u>	<u>%</u>	<u>1963</u>	<u>%</u>	<u>1968</u>
Food processing	693	3.3	815	1.8	893	11.8	1,562
Other	713	12.0	1,260	6.7	1,737	7.3	2,473
Total	<u>1,406</u>	<u>8.1</u>	<u>2,075</u>	<u>4.9</u>	<u>2,630</u>	<u>8.9</u>	<u>4,035</u>
% of GDP	9.2		9.8		9.0		11.7

1/ Data for private investment, however, indicate only investment proposals, not actual outlays. More detail is given in Part II of this report.

2/ In the statistical tables, the refinery is treated as a "mixed enterprise"

108. In the ten-year period 1953-63 manufacturing industry just kept pace with the economy as a whole; in the latter part some of the new industry plants started operating, but only since 1963 did previous investments produce results in terms of output. Production data are available for 1962-66 and they show an average annual increase of 9 percent, the same rate as shown for value added in the above table for the last five years and about twice the rate of total GDP growth. This acceleration coincided with a slowdown in agriculture, construction, and services.

109. If food and raw material producing industries are taken together, they account today for about 70 percent of industrial production, but a notable development has taken place in the textile industry, where between 1963 and 1965 output was doubled and has continued to rise ever since. In the following paragraphs a summary is given of presently existing and proposed manufacturing industries.

110. Known mineral resources in Cambodia are very limited and not of great economic value. Limestone is mined for the local cement plant near Kampot. Phosphate rock is extracted in the same region and has for a considerable time been used together with imported phosphates as a fertilizer on acid soils for rice. Precious stones (e.g. sapphire, ruby) are extracted but much of this goes illegally to Thailand for cutting. With the creation of a state trading company SONEXPIEROR, it is hoped to promote local cutting, jewelry production, and export.

111. Cement is produced in a Chinese-financed plant at the present rate of about 60,000 tons/year or one-third of total domestic demand. The plant is to be expanded to 150,000 tons by 1970. A second cement factory has been proposed in the Second Plan for which adequate clay and limestone deposits appear to be available, but in the absence of a demand survey and feasibility study it is not yet clear what size this plant should have.

112. In the fertilizer field, domestically crushed phosphate rock with 12,000 tons (only 15-16% phosphate content) covers only half of present requirements and the deposits are limited, so that to avoid closing down the existing mill in the foreseeable future, the government is planning to search for new deposits. Another alternative would be to plan for processing, at Sihanoukville, of important phosphorite. A urea factory producing 35,000 tons per annum was proposed in the Plan, and French assistance is being sought for its construction at Sihanoukville, using distillation products of the existing oil refinery. Present consumption of urea is only about 5,000 tons per annum but more extensive use of nitrogenous fertilizer, partly in conjunction with phosphate, is part of the present drive to increase rice production. While a urea plant of the size proposed is prima facie uneconomic, a feasibility study has not yet been prepared.

113. The oil refinery at Sihanoukville, financed with French assistance in 1967, went on stream early in 1969 with an annual processing capacity for 600,000 tons of crude oil. Petroleum products are still distributed by Shell, Esso and Caltex but their operations will be phased out, in stages, in favor of TELAKHMER, a two-thirds State-owned distribution company created

in 1969, presently supplying 28 percent of the market. Some products like fuel oil and naphtha for which the domestic market is inadequate, will be exported. The refinery is saving foreign exchange at the rate of \$2 million per annum and ensures domestic supplies which previously had to come, uncertainly, through Viet Nam.

114. There are some other chemical industries producing oxygen, acetylene, paints, varnishes, glues, and soaps. A match factory supplies all domestic requirements. Three fairly large cigarette factories produce good quality cigarettes sufficient for the domestic market plus some illegal exports to Viet Nam, virtually 100 percent from domestically grown and cured tobacco. Cigarette imports are prohibited.

115. Cambodia has a large number of small but no large modern rice mills. This unfavorably affects the quality of rice for export and proposals exist for a modern mill to be set up at Sihanoukville. Brown palm sugar is produced by 35 small units; a sugar refinery was built with Czech assistance but it was not suited to processing the available brown sugar, so that additional facilities had to be set up for prior processing, and in addition, raw sugar had to be imported. A new sugar mill to be based on cane was included in the Plan, and a study has been prepared, but the area for sugar cane planting has not been secured and other questions remain to be resolved. A new milk reconstituting plant is just being completed in the private sector with foreign participation to substitute for imports of concentrated milk which have been at about \$2 million a year. Other food processing industries include vegetable oil, confectionery, rice noodles, preserves, condiments, etc.

116. Several projects for food processing were included in the Plan but have made no headway, e.g. a vegetable oil plant and a starch factory at Sihanoukville for export, feedmills, and a shrimp freezing plant. A relatively small canned fish and fishmeal plant was recently set up by the government and is operated by SONACOP.

117. Various liquors and spirits are produced in remarkably good quality by SKD, a state monopoly, and in 1968 it started producing beer at Sihanoukville.

118. SONATEX operates two cotton textile mills in Kompong Chham and Battambang, with a total output of 3,000 tons based on domestic cotton and some imported synthetic fibers. Two weaving mills by SONATEX now produce 8-9 million square meters of cotton fabrics a year, and smaller private weaving mills also produce fabrics for the domestic market. Imports of both cotton yarn and cloth have come down substantially in recent years, from about \$9 million in 1965 to \$2 million in 1968. A new spinning mill for long staple cotton and synthetic fibers is proposed as a mixed enterprise, but it has not been forthcoming yet.

119. A public jute mill (SOKJUTE) started operating in 1967 and was very successful in stimulating jute cultivation, but the high price paid to growers makes the firm non-competitive. Another jute mill is proposed.

120. Bamboo and rice straw plus imported pulp are used to produce about 4,000 tons per annum of hardboard and newsprint at the SONAPAP paper mill at Chhlong (Kratie), and a second plant, to be established in phases to a 20,000 ton capacity, has been studied by French experts who, however, presently suggest a much larger mill to be located at Sihanoukville, based on a combination of russian pulp and pulp to be produced domestically from rubber wood, at the rate of 100,000 tons per annum.

121. Cambodia is fairly well endowed with timber resources, and about 500 sawmills exist in the country. A plywood factory is producing 4,000 cubic meters a year of which 1,000 cubic meters are exported. A second plant, entirely for export, is under study. As already noted, timber extraction is not an efficient industry.

122. Besides rubber processing plants owned by the private estates in Kampong Chham, other industries are producing rubber products, including bicycle and automobile tires and retreads; bricks, roof and floor tiles, pottery, earthenware and glassware. The state-owned glass factory supplies bottles and sheet glass, and three small private factories produce various types of glassware. Private plants also assemble transistor radios and bicycles, and produce small quantities of water pumps and agricultural implements. SONATRAC has recently installed an assembly line for 1,000 tractors and 800 trucks a year, and plans exist to manufacture motorcycles which are now imported at the rate of 5,000 a year.

123. Industrial activity is heavily concentrated in Phnom Penh. To avoid further concentration of industry in the capital, the government proposes to develop Sihanoukville into a second pole of industrial growth. This is expected to be helped by the establishment of a free zone. A site for an industrial estate has also been located but no significant work has yet been done for its development, partly for lack of funds but also because of hesitancy in assessing potential response by the private sector. So far, only public industries have come up in Sihanoukville, and some difficulties have been encountered in labor supply. In the longer run, the success of the free zone scheme is conditioned on the existence of noticeable advantages over Hong Kong and Singapore, of which there is no striking evidence.

Industrial Policies

124. Agriculture has always taken precedence over industry in the economic and political thinking of the Cambodian authorities. Over-ambitious plans for import substituting industries have rightly not been drawn up. The absence of pressing unemployment problems, as well as the ample availability of uncultivated land may have something to do with this attitude. Realizing the domestic market constraints and the remoteness of prospects for an independent, modern, and competitive export industry in the light of basic manpower constraints and the lack of know-how, industry is realistically viewed as an instrument to achieve a more balance growth, rather than a self-powered engine for development. In line with this thinking, the Second Five-Year Plan (1968-1972) aims at the promotion of industries facilitating the growth of agricultural production, making possible the trans-

formation of raw materials into finished and semi-finished products, and of selected industries catering to final consumption. Export-oriented industries relying on certain industrial crops to be developed in the agricultural sector are also given precedence. On the whole this seems to be a sound approach, and there are no economic reasons to discount hopes for fairly rapid development of such industries. Considerable progress has been made in establishing factory-scale establishments over the last 15 years, starting virtually from scratch, and some of these industries produce consumer goods for the domestic market in lieu of imports at acceptable quality. Based on this experience a range of new industries can be visualized, some of which have already been mentioned, both for further import substitution and in certain cases for export, drawing mainly on Cambodia's present and future agricultural production. In addition, new medium-sized engineering industries could also be developed that would produce supplies for the agricultural sector such as implements, pumps, and the like.

125. The Five-Year Plan does not go much beyond the enumeration of industrial projects which prima facie are deemed desirable. Although the Plan is now in its third year, feasibility studies have not been produced yet for any of these projects. Also, the Plan did not give any indications as to the manner in which these projects would be financed, and this is part of a more serious problem regarding the role of private enterprise which is further discussed below.

126. Local industry is protected to a varying degree through tariffs. However, tariffs are not an instrument of a conscious policy of industrial protection, and up to the recent devaluation they barely compensated for the overvaluation of the currency. Thus, up to now real protection was available only in the form of ad hoc prohibition of imports, or through quotas, or by the government fixing the price at which SONEXIM could sell imported goods, as in the case of cement, jute bags, etc. New investors can apply for the granting of specific protective measures.

127. Various tax advantages are available to new industries under a law of 1965, which provides for exemption from import duties for machinery and raw materials, as well as from income tax, and for accelerated depreciation allowances. Eligible industries are listed in a decree of 1967 but the specific advantages are decided by additional decrees for each case. A guarantee against nationalization of foreign capital up to a period of 10-30 years is contained in a law of 1957 which also specifies that a minimum local equity participation and Cambodian personnel will be necessary (to be decided in each case by the Ministry of Finance). In case of nationalization "on grounds of public interest" a fair compensation is foreseen. Repatriation of capital, as well as transfer of profits, may both be allowed for up to 20 percent of the investment each year. Despite these provisions, foreign private investment to speak of has not been attracted so far.

128. To establish some greater clarity on what the government considers the function of private enterprise, a new "law on the Apportionment

of Economic Activities between the Public and Private Sectors" was issued in 1968. It specifies the activities reserved to the public sector (e.g. banking, insurance as before since 1963, also power, alcoholic beverages, pharmaceuticals, petroleum products, chemical fertilizer) and leaves all other activities open to the private sector, with the proviso, however, that the public sector may step into any activity otherwise opened up to the private sector, if the general interest so requires (inadequacy of private performance, high prices, etc.), but would be operating "on equal terms" with private enterprises. The response to this law by the private sector has been to look at the "stepping-in" rather than the "opening-up" clause, and with some justification regarded the "equal terms" provision for public enterprises as of doubtful value.

Problems

129. The limited size of the domestic market and the absence of a mineral resource basis do place important limitations on industrialization. A similar constraint is the lack of technical and managerial skills. Industrial operations at present are furthermore generally hampered by the restrictions on the importation of vital industrial inputs, the cumbersome licensing procedures, the imposition of state intermediation in foreign trade transactions, the state price-fixing system of raw materials and industrial products, and the inflexible bank credit policy. More imponderable, but of even more serious consequence is the continued ambivalence of the government towards private enterprise, and the proliferation of state enterprises.

130. The technical and financial assistance of the People's Republic of China and of Czechoslovakia have indeed made possible the establishment of a nucleus of state industries which in all likelihood would not have come into existence had the government relied on private capital. A few more have been created with the government's own resources. The establishment of these state enterprises has not, however, been based on sound technical and economic feasibility studies. Rather, turnkey plants were received from the donors as gifts without much scrutiny into the type of equipment installed, prospective costs of production, sources of raw materials, etc. As a result, some plants of less than economic size were set up and with technically outdated equipment, and production methods were not always adapted to local conditions. Numerous difficulties have arisen which are far from being resolved, including long delays or inability to get spare parts for machinery where the models installed had been discontinued in the country of supply.

131. It is difficult to judge the operating efficiency of state enterprises, since they have been made to operate in an environment of fixed prices for inputs and outputs. Some of them have been put up in pursuance of social goals rather than profitability. Though the majority of them show some profit, this does not necessarily imply efficient management, if profits are the result of a fixed mark-up, or of a fiscal monopoly. Of course, the opposite is also true if deliberate losses are incurred.

132. There is a general shortage of cadres in key technical, administrative and financial positions, and managers were seldom selected for their qualifications. Not perhaps unconnected with this fact, managerial autonomy is virtually non-existent, prices of final products may be set for social reasons below actual costs, and almost all state undertakings are forced to maintain excess staff and provide various social benefits to employees.

133. Despite the dominant role of the state in several sectors of industry, private entrepreneurs have nevertheless been a vital element in the industrial progress so far achieved. Private industrial investment, not including mixed enterprises, has represented about 40 percent of total investment in industry during the period 1957-1968. However, it has shown a definite decline in recent years.

134. The conviction prevailing in Cambodia, at least until very recently, has been that the road to industrialization goes through the establishment of state enterprises. This is partly because, in effect, large-scale investments do not often have a prospect of being financed from private capital. Moreover, however, there is an attitude, strengthened by ethnic differences, on the part of government to look with distrust on private ventures, to consider private profits, if large, as unjustified, and to assume further that any industry will lead to monopoly power inimical to the public welfare unless it is in the public sector. At the same time, it is recognized that private enterprises often are operated far more efficiently than factories run by public officials. These conflicting insights are reflected in the law of 1968 on the apportionment of economic activities, where a line is drawn between industries reserved to the public sector and others that are open to private enterprise - but with the proviso, as noted, that the state may step in and "compete" with the private sector if the latter misbehaves.

135. In summary, the economic climate and the policy framework, particularly since 1963, have not been favorable to attract private capital, either domestic and foreign, into industry, and as a consequence industrial progress has been less than what it could have been. Again, the above law of 1968, as well as some other recent measures and proposals for liberalization, have been in recognition of this fact, but without so far changing the basic situation.

E. Transport

General

136. Cambodia's population, economic activities and transport requirements are concentrated in the Central Plain, which extends clear across from the Thai border in the northwest to the Vietnamese border in the southeast, along the Tonle-Sap, the lower Mekong and the Bassac. The plateau and mountainous regions in the north, northeast and southwest are

sparsely populated, with densities as low as 5 inhabitants per square-kilometer, and generate little demand for transport, except along the borders for strategic regions.

137. Cambodia is favored with an extensive network of navigable rivers and, up to the opening of Sihanoukville Port in 1960, relied exclusively on river transport on the the Mekong for its overseas trade. In addition, Cambodia's Central Plain is served by a fairly well developed system of primary roads and by a railway, which links the rice producing Province of Battambang with Phnom Penh and, since the end of 1969, with Sihanoukville Port. The small size of the country has so far militated against the development of domestic civil air transport which, aside from mainly international tourist traffic between Phnom Penh and Siem Reap, remains virtually non-existent.

138. Since independence, investments in the transport sector, which have been absorbing a sizeable proportion of Cambodia's domestic and external resources, have led to the following major developments:

- (i) the creation and subsequent extension of a seaport at Sihanoukville;
- (ii) the construction of a 4-lane highway (224 km) and a railway line (262 km) from Phnom Penh to Sihanoukville;
- (iii) the construction of two international airports at Phnom Penh and Siem Reap; and
- (iv) the construction of a bridge over the Tonle Sap in Phnom Penh and of a road (not yet completed) joining with the northern and northeastern road network and avoiding a ferry crossing on the Tonle Sap.

139. Following these additions, the transport system will not require further major extensions in the near future, but instead it will need improvements in the standards and in the maintenance of the existing infrastructure. While less glamorous than the construction of new facilities, the task of upgrading and maintaining the system is at least as rewarding economically, and the flow of investment funds (and recurrent expenditures) to the transport sector should not be allowed to drop drastically from its estimated level of CR 500-700 million in the past four years.

Roads

140. Cambodia's primary road network consists of some 4,200 kilometers of national highways and 1,700 km of provincial highways. The major road arteries radiate from Phnom Penh and connect all the important centers of economic activity. The density of the road network is highest around the capital. About 60 percent of the national highways and less than 10 percent of the provincial highways are paved with a bituminous surface. The remainder is about equally divided into gravel and earth roads. In addition, there are

some 13,000 kilometers of earth tracks, which have been built by local authorities and by the Cambodian armed forces to serve rural or military traffic. They are usually poorly maintained and impassable for motorized traffic, especially during the rainy season.

141. Most of the primary network dates back 30 to 40 years and was built to standards which today are inadequate for modern traffic. While standards have been progressively improved, pavements and shoulders remain narrow, embankments insufficiently compacted, alignments sharply winding in places, and bridges generally single-lane and weak.

142. Manual traffic counts taken on major national highways in recent years show relatively high traffic volumes typically ranging from 500 to 2,500 vehicles per day, with a roughly even distribution in the number of motorcycles, light and heavy vehicles. The highest recorded traffic volumes were on the Phnom Penh-Sihanoukville highway. On provincial highways, traffic rarely exceeds 100 vehicles a day, partly because of the low standards of these roads.

143. Since the completion of the Phnom Penh-Sihanoukville highway, which was built with United States financial and technical assistance, programs of road construction and improvement have been on a very limited scale: over the past three years, for instance, budget allocations for major repairs, resurfacing and new road constructions were less than 100 million riels annually. These funds barely cover urgently needed repairs to keep the road system open, especially after the flood damages following the monsoon, and the construction each year of some 30 km of new roads scattered over the country.

144. As long as financial stringency precludes larger investment for road development, essential stopgap measures should aim at preserving the existing road plant by increasing maintenance efforts, in order to reduce road transport costs generally on the system. To achieve even this limited objective will require new maintenance equipment and spares since most of the present stock is in a state of disrepair or immobilized for lack of spare parts. Out of 186 trucks, less than 25 percent were listed in good condition in 1967; all of the heavy equipment (rollers, tractors, graders, etc.) is now between 9 and 15 years old, and has reached the limits of its economic life. The foreign exchange required to replace and supplement the existing equipment could amount to about US\$2.5-3.0 million equivalent.

Road Transport

145. Within the past decade, Cambodia's motor vehicle fleet increased from about 15,300 to about 36,400 vehicles at the end of 1969, at an average annual rate of over 9 percent. Motorcycles and scooters are not included in these figures. The fleet consists of some 9,700 trucks and vans, 1,360 buses and 25,600 private cars and taxis. In relation to the size of the population, the vehicle fleet is relatively small: one four wheel vehicle for every 200 people.

146. Government controls over the road passenger transport industry consist in technical inspections of vehicles, setting of maximum fares and route licensing of bus and taxi-bus operations. In fact, actual fares have generally been well below the maximum authorized tariffs because of competition; the route licensing system is also fairly flexible to take into account traffic demand. In addition to buses, there are over 2,000 taxi-buses which either ply on regular routes within urban areas or are licensed within a given district (srok) and over 1,000 cars for hire which may ply anywhere in the country. The competition from these vehicles may explain the slow rate of growth of buses of about 2.8% per year in the 1960's.

147. For road transport of freight, similar controls exist, except that there is no route licensing. However, on the most important route between Phnom Penh and Sihanoukville, two companies regrouping former customs agents share the monopoly of import-export traffic on account of SONEXIM. The direction in which the situation will evolve with the opening of the new railway line and the possible dismantlement of SONEXIM remains unclear.

The Railways

148. A state-owned autonomous public enterprise, the Royal Cambodian Railways operate two lines of meter-gauge single track: (i) the old line from Phnom Penh to Battambang and the Thai border (385 km) built before 1940; and (ii) the new line from Phnom Penh to Sihanoukville (262 km) which has been under construction since 1960 and was opened to traffic over its entire length at the end of 1969. The old line links up with the Thai Railways; it was part of the former Indochina network and was to be extended up to Saigon to serve international traffic. Its main function, however, was - and remains - the linking of Phnom Penh with the Province of Battambang. By connecting Phnom Penh with Sihanoukville Port and with the Oil refinery near the port, the new line provides an alternative to road transport for import-export and oil traffic. It also serves the two provincial capitals of Takeo and Kampot.

149. Over the 1951-1968 period, freight traffic fluctuated extraordinarily widely, without any apparent growth trend, between 135,000 tons and a maximum of 388,000 tons. These fluctuations resulted from the Railways' overwhelming dependence on agricultural products, which represented over two thirds of total freight traffic. Other freight traffic has been on the decline. A direct consequence has been the lopsided directional traffic distribution: between 1960 and 1967, traffic moving in the Battambang-Phnom Penh direction accounted for almost 90% on average of total freight traffic. Moreover, the demand for transport of agricultural products is seasonal and concentrated in the months of March through June, which also adversely affects the Railways' operations and finance.

150. Contrary to freight, passenger traffic exhibited a sustained growth during the 1951-1968 period. From 675,000 passenger journeys in 1951, traffic rose to 2.4 million passenger journeys in 1968 at an annual growth rate of 7.8 percent. Passengers kilometers rose slightly faster, indicating an increase in average lead from 67 km to 72 km.

151. As freight traffic has traditionally been the main source of revenue for the Railways, the financial results could not but reflect the vagaries of agricultural output. While in the record crop year of 1965, gross receipts from freight (CR 70.6 million) were nearly double those from passengers, freight receipts in the following year actually fell almost 20 percent below passenger receipts.

152. In contrast with fluctuations of up to 35 percent from one year to the next in gross operating revenues, operating expenses have shown a much more stable and predictable pattern of growth. Over the 1953-1968 periods, gross operating revenues exceeded working expenses in all but three (poor harvest) years, and in all but five years did the Railways earn a positive net operating income after meeting depreciation charges. However, in retrospect, annual depreciation charges were set at such unrealistically low levels as to invalidate accounting results and to deprive the Railways of the capacity to replace worn-out assets out of their own reserve funds. A revaluation of the Railways assets appears indispensable to arrive at realistic depreciation charges; however, the time lost for building up an adequate depreciation reserve will not easily be made up, as road competition would prevent the Railways from raising their tariffs and income substantially.

153. The Railways are in an uncomfortable financial position, with long-term debts of CR 1.6 billion at the end of 1968, amounting to over 4-1/2 times their equity funds. This situation developed because the funds for the construction of the new line (totaling about CR 1.9 billion) which were obviously beyond the Railways' internal financing capabilities, were being lent to the Railways, rather than put up as equity capital by the Government. The Railways have drawn the Government's attention to their inability to meet interest payments during construction and full principal and interest payments later on; they rightly urged the loans be converted into a Government contribution to their capital, leaving the Government to assume the financial obligations under the loans. While final settlement is pending, the Government has granted the Railways a de facto moratorium on the loans.

154. As the chances for mitigating traffic characteristics and operations on the old line are slim, any material improvement in the Railways' earning position must come from the new line. On the new line, the Railways expect a more balanced directional distribution of traffic, less seasonal variations and empty hauling, heavier trains and cheaper tractive power. Whether in the end, the new line will pay for itself in financial terms remains doubtful and that will depend on the Railways' ability to compete effectively with road transport and to raise some of its tariffs. Whether it will pay for itself in economic terms is even more open to question, should the Railways be required to earn a return on the invested capital above the financial interest charge of 3 percent per annum.

155. On completion of the new line, the Railways are turning their attention to investment requirements on the old line. In particular, the task of reinforcing structures and bridges on the old line is becoming more urgent in order to permit through traffic of new rolling stock over

both lines. Subsequently, the Railways will face problems of track and rolling stock renewals on the old line. However, no investment plan or cost estimates are yet available and the lack of renewal reserve funds will prove a major obstacle. In the meantime, the Railways have been seeking technical assistance from the UN and the French Government for improving their operational efficiency.

The Ports

156. Not until 1960 did Cambodia have a seaport for its international trade, which previously was handled exclusively at the river port of Phnom Penh. The decision to build a deep-sea port proved sound, as navigation on the Mekong was seriously hampered by the war situation in Vietnam. Since November 1966, ships transiting through Vietnam are required to wait for weekly convoys, and are thus liable to substantial delays.

157. Since 1960, traffic at Phnom Penh and Sihanoukville Ports was as follows (in tons):

	<u>Phnom Penh</u>	<u>Sihanoukville</u>	<u>Total</u>
1960	842,000	34,700	876,700
1961	741,000	95,500	836,500
1962	898,000	166,300	1,064,300
1963	962,500	369,600	1,331,600
1964	707,800	714,800	1,422,600
1965	595,400	754,600	1,350,000
1966	517,100	548,500	1,065,600
1967	535,200	545,200	1,080,400
1968	453,100	747,800	1,200,900
1969 (9 months)	227,700	358,300	586,000

Phnom Penh's share of traffic has declined drastically in favor of Sihanoukville; nevertheless, Phnom Penh's importance should not be underrated, as its closeness to Cambodia's main production and consumption centers gives it a decisive advantage over Sihanoukville for shipments to and from ports in the Far East. While Phnom Penh has definitively lost the oil traffic now going to the new refinery at Sihanoukville since 1969, shipments with origins or destinations in North Vietnam and Mainland China should again transit through Phnom Penh at the end of the hostilities in Vietnam, and possibly Phnom Penh may recoup a considerably slice of Sihanoukville traffic when navigational conditions on the Mekong are relaxed.

158. The Japanese have shown interest in the development and transfer of Phnom Penh Port from its present location on the Tonle Sap to a new location on the Mekong (a short distance away) by participating in a preliminary techno-economic study. The implementation of the project, which was also part of an urbanization plan and would have permitted deeper draft ships to call on Phnom Penh, has been indefinitely postponed for financial and political reasons. Its estimated cost is about CR 240 million at the post devaluation rate. With the large decline in traffic in the 1960's, there is no immediate problem of congestion; in the future, the development of Phnom Penh and Sihanoukville Ports should be studied jointly.

159. Sihanoukville Port was first equipped with a 285 meter long pier providing for two berthing places on each side. As traffic soon exceeded initial projections, two new berths totalling 350 meters were built, along with a turning basin of 500 meters in diameter, and two warehouses. For lack of a final settlement between the Port and a French supplier on the performance of a dredger delivered in 1967, siltation has reduced the available draft in the turning basin from -10 meters to -6.5 meters, so that the new berths have not been utilized fully. With the dredging of the basin and the surfacing of the access roads, the Port should have sufficient capacity to handle annual traffic volumes of the order of a million tons, assuming reasonable operating efficiency. It follows that further major extensions of the port should be preceded by a thorough study of traffic, and linked to concrete indications that the planned industrial zone will materialize.

Inland Water Transport

160. Historically, inland water transport played the dominant role in Cambodia's communication systems. While road and rail may by now have supplanted it, its function still remains far from negligible. In some areas, particularly on the left banks of the Mekong and the Tonle Sap, water transport remains the only means of communication with the rest of the country. As in many countries, however, reliable statistics on inland water traffic are hard to come by, thus preventing meaningful intermodal comparisons; nevertheless, the length and depth of navigable waterways and the size of the registered fleet attest to the continued importance of inland water transport in Cambodia.

161. Some 660 km of waterways (equivalent to the length of the rail network) are navigable all year round, whereas an additional 930 km are accessible to motor-launches during the high water season. The main waterways are the Mekong River (up to Kratie), the Tonle Sap and the Bassac. Ocean-going vessels can travel on the Mekong River some 200 km from the Vietnamese border as far as Kompon Cham, with maximum draft restrictions of 4 to 5 meters in the dry season. Further upstream to Kratie, draft restrictions of up to 1.5 meters limit navigation to smaller crafts. Between Phnom Penh and Kompong Chhnang the Tonle Sap River (90 km) is accessible to 50-ton motor-launches, whereas the Great Lake takes mainly smaller launches (5-25 tons) and fishing boats. Because of the irregular river-bed and channels and of road competition, the Bassac (90 km) has lost its former importance and is now used mainly by junks and barges in the transport of

building materials and wood. Other year-round navigable rivers are found mostly in the coastal Provinces.

162. The registered fleet comprises 824 motor-launches, of which three-quarters carry freight traffic exclusively. The average capacity (68 passengers and 8.6 tons) is relatively small. Actually, a good proportion of the cargo-launches are used as tug-boats for the junks and barges, of which 2,400 are registered with loading capacities over 16 tons. The size of the fleet has remained stable for a number of years, but the proportion of small boats has been increasing; nevertheless, there has been an important switch-over from steam or petrol engines to diesel engines over the past ten years.

163. For passenger boats, a route licensing system similar to that for buses exists. Some 60 scheduled services call daily at Phnom Penh Port, where about 700,000 passenger journeys originated or terminated in 1968. Regular services reach as far as Kompong Chhnang (100 km in about 8 hours) and Kratie (212 km in about 15 hours). On the basis of the registered capacity of 15,000 passengers and of an estimated average daily run of 15-25 km at full load, annual passenger traffic could amount to some 80-140 million passenger-km and compared with 173 million passenger-im on the Railways in 1968. Similarly, judging by the registered capacity of cargo-launches, junks and barges (about 120,000 tons), freight traffic moving on inland waterways may be substantial, although difficult to estimate in the absence of utilization indicators. However, as mooring facilities at river ports are generally rudimentary and inefficient, it is unlikely that the fleet's utilization could be high. Commodities shipped by water include rice and other agricultural products, building materials, wood, charcoal, potteries, fish and cattle. The rates charges are usually below the maximum authorized of CR 1.04 per ton-km.

164. Except for some 4 million Riels of maintenance expenditures annually on the lower Mekong, no public funds have been allocated in recent years for the maintenance or development of waterways. Mooring facilities usually are in private hands. Given the importance of inland water transport, it seems likely that greater efforts on the Government's part in improving the waterways navigability would prove highly justified, and a study on river transport should be undertaken as a first step.

Civil Aviation

165. While Cambodia may boast of having as many as 26 airfields, civil air transport is almost exclusively concentrated at the two major airports of Phnom Penh (Pochentong) and Siem Reap. At present, there are no scheduled services to any of the other airfields, which serve administrative, military and some private traffic. Distances between the main cities are too short and potential markets for air services too small to make domestic air transport an economic alternative to rail and road transport. In fact, most of the present traffic consists of international traffic, and foreign tourists account for a major share of traffic on the only scheduled domestic air-route between Phnom Penh and Siem Reap.

166. Passenger traffic at Phnom Penh and Siem Reap airports has been increasing rapidly. Over the 1958-1968 period, the number of plane movements at Pochentong grew at the annual rate of 6 percent, while passengers increased by 15.5 percent yearly, from 30,000 to 127,000. At Siem Reap passengers increased from 28,200 in 1966 to 47,700 in 1968, a 70 percent rise in two years. Up to the opening of Siem Reap to Boeing 707-type planes in November 1969, Pochentong was the sole port of entry for international traffic. Since about 50 percent of this traffic continued by plane to Siem Reap, it is likely that from now on the importance of Siem Reap airport will increase in relation to Pochentong, as part of the tourist traffic will call directly at Siem Reap - Angkor, where Cambodia's unsurpassed tourist attractions are located. Freight traffic remains negligible at less than 1,000 tons in 1968.

167. In addition to the already large sums which, over the past five years, were mainly directed to the development of Siem Reap airport (CR 256 million) further important investments are required in order to accommodate the rapidly growing passenger traffic. New investments (about CR 300 million) are needed at both airports to improve the presently low safety standards (navigation control, telecommunication and firefighting equipment) and to increase the limited capacity of the air terminal buildings. Moreover, it is planned to complete the parking area at Pochentong and to widen the Pochentong runway. At the time of the mission, a Government commission was studying the needs and priorities for the extension of the two airports, in connection also with the eventuality of "Jumbo" jet traffic by 1972/1973. It seems that any such extension must be linked to prospects for increasing hotel accommodations, so that airport and hotel developments do not lag behind one another. Further, it should be established whether and when the provision of "Jumbo" jet facilities would be economically justified - and for which of the two airports, - by estimating the losses to Cambodia from tourist traffic foregone in the event such facilities were not provided.

168. Cambodia's national airline, Royal Air Cambodge (RAC), was founded in 1956 with 60 percent Cambodian and 40 percent French participation, and started operations by chartering aircrafts. At present, RAC owns and operates three aircrafts (1 Caravelle, 1 DC-6 and 1 DC-4) on the Phnom Penh - Siem Reap route and on a number of international routes, including Hong Kong, Singapore, Bali and Canton. Traffic has been increasing rapidly from 27,300 passengers in 1964 to 70,600 in 1968, at an average rate of 27 percent annually. Except for 1966, RAC has been operating at a loss in the 1965-1968 period, which has caused a heavy drain on RAC's liquidities. With the disappearance of the exchange rate disparities, the situation is expected to improve and RAC is planning to acquire a second Caravelle in 1970 or 1971. (Up to the devaluation of 1969, exchange receipts had to be converted at CR 35/\$ while aircraft, bought in France, had to be amortized at the French Franc rate of CR 10/FR.)

F. Power

169. Power is generated and distributed to most areas by Electricité du Cambodge (EDC), a mixed enterprise with 85 percent government participation, which is under the supervision of the Ministry of Public Works. A small private company 1/ supplies power to Battambang. Power from these two companies were consumed at the rate of about 83 million kwh in 1969, which is a low level for a country the size of Cambodia. Twenty percent of the total is consumed for light and home uses and only 18 percent by industry. However, many industries use their own generating units, both in Phnom Penh (which accounts for 75 percent of Cambodia's electricity consumption) and elsewhere, because of voltage fluctuations, breakdowns and high rates. Reportedly it is a third cheaper, at present EDC rates, to use private diesel units.

170. Power consumption has grown 13 percent a year from 1958 to 1963 but not more than 5 percent a year since then. There is at present no shortage of power capacity except that Sihanoukville will shortly need an expansion. The Kirirrom power dam, built with Yugoslav assistance, was the first hydro-electric project; it went on stream in 1968 with a capacity of 10 MW and is connected with a 110 KV line to Phnom Penh, which has two distribution grids each with different type (and phase) thermal stations. The available capacity in Phnom Penh is 50.5 MW but the peak load in 1968 was not more than 20 MW.

171. Siem Reap now has diesel plants with a capacity of 2.5 MW which is adequate to meet hotel expansion through the next several years. Battambang's capacity of 1.8 MW is also not yet fully utilized but the existing 1 MW plant in Sihanoukville is not adequate. Total private generating capacity, scattered in numerous units, is about 20 MW, of which 12 MW in Phnom Penh.

172. The main present shortcomings in power are (a) an inadequate rate structure and (b) highly outdated and ineffective distribution in Phnom Penh, inhibiting full use of existing generating capacity. A rate study has been completed by UNDP with recommendations presently under consideration by the government. Projects have been prepared for both a high voltage grid and a new distribution system for Phnom Penh, which appear feasible and should be pursued actively.

173. Future developments for Sihanoukville, as well as longer-term overall requirements and projects, are discussed in Volume II of this report.

1/ Société Franco-Khmère d'Electricité

G. Telecommunications

174. Internal and international public services are under the Direction of the Posts and Telecommunications branch of the Public Works Department. There are local automatic telephone exchanges at Phnom Penh (4,000 lines) and several smaller centers. Interurban connections are by carrier working on open wire lines. International connections are by H.F. radio and include 6 voice channels and a few teleprinter connections to the neighboring countries.

175. Radio Broadcasting and Television are under the direction of the Ministry of Information. Transmitters are located in the capital only at present.

176. Expansion plans include a microwave system to link the capital with principal towns. This will be principally for public telecommunications services but the opportunity will be used to include channels for radio and television relay. The cost will be US\$8.5 million, \$5 million attributable to public services. Increased international circuits and a telex exchange for Phnom Penh are planned at a cost of \$2.5 million. Several new post offices are also planned for Phnom Penh at a total cost of US\$1 million.

H. Tourism

177. Two factors combine to provide Cambodia's tourism sector with very good prospects for the future; they are the presence of the ancient Khmer temples in the province of Siem Reap (Angkor) and the country's location in the heart of the South-East Asia tourist circuit. Until recently the exploitation of this potential was hindered, partly by a restrictive attitude towards foreign tourism on the part of the Government, but mainly, by the relatively poor access to the main tourist attraction - Angkor. These two constraints have now been removed; the Government is actively promoting foreign investments in hotels, having recognized the foreign exchange earning potential of tourism, and the airport at Siem Reap, close to the temples, opened in late 1969 to international jet aircraft flights. The growth of the tourism sector in Siem Reap would now seem assured, although, to what extent Phnom Penh and other parts of the country will share in this growth, is at present difficult to predict.

178. Until the mid 1960s Cambodia did not share in the growth of visitor traffic to South East Asia and between 1965 and 1969 visitor arrivals grew at less than the growth experienced by neighboring countries. Nevertheless, visitor arrivals did increase from 23,000 in 1964 to an estimated 45,000 in 1969 representing an annual average growth of 19 percent. This was achieved during the height of the Vietnamese War at a time when access to the temple attractions was difficult; thus indicating Cambodia's basic tourism potential. Of the visitors arriving in recent years some 70-80 percent are estimated to have been on pleasure trips and

over half of these were in some sort of an organized group. The average length of stay of all visitors to Cambodia has been around 3-3.5 nights but pleasure visitors at Siem Reap had lower average stay of between 2-2.5 days. The total of foreign visitor bednights recorded in 1968 was between 110,000-124,000 and, as in previous years, they were spread fairly evenly through the year.

179. The main growth of foreign visitor bednights is expected to be in Siem Reap during the period up to 1975 and, given the mission's evaluation of the demand potential, the growth of bednights is projected to total in the range of 300,000-320,000 in 1972 and 490,000-660,000 in 1975 (including also an estimation of the growth of bednights in Phnom Penh).

180. Whereas, in Siem Reap the supply of hotel rooms appear to have more or less kept pace with demand in the past and in the immediate future is likely to be the factor conditioning the possible growth of benights, in Phnom Penh, a surplus of medium class and a shortage of first class accommodation exists. The surplus of medium class rooms is likely to be aggravated when the first class hotel, now under construction, opens and absorbs some of the traffic presently in medium class rooms. In this situation the mission recommends that hotel projects for Phnom Penh should be carefully reviewed with regard to future demand. The future hotel capacity in Siem Reap is difficult to project, but the mission believes that, by 1975, some of the past impediments to hotel investments will have been removed and that the supply of hotel rooms will not be a factor limiting traffic growth.

181. A major problem seen to be facing the tourism sector is one of protecting and preserving the major attractions at Siem Reap, i.e. the temples. It is feared that uncontrolled hotels and related developments will destroy their forest settings and that other dangers, perhaps jet aircraft noise, could serve to damage the structures themselves. The need for the allocation of development zones, and protected areas and the setting of building standards, etc. is urgent and related to this need is the requirement for infrastructure developments to be placed on a planned and coordinated basis (presently hotels are making provision for their own electricity and water without regard to the public plans for these utilities). In view of this, the mission recommends that a study should be carried out to establish a tourism master plan for the development of Siem Reap. A draft application from the Government for UNDP assistance for such a study has been prepared.

182. With respect to the economic implications of future tourism development, the main effect calculable at the present time is the effect, on the gross and net earnings of foreign exchange likely to result from the development of the tourism sector. In 1969 it is estimated that gross foreign exchange earnings from foreign tourism totalled around US\$3 million which, allowing for capital and current costs in foreign exchange, probably resulted in net foreign exchange earnings of some US\$2.3 million. On the basis of the projected foreign visitor bednights in 1975 it is calculated that gross earnings could rise to between US\$12-16 million, representing

a likely net increase of foreign exchange earnings of about US\$9-12 million. In employment terms, those directly employed in hotels and travel agencies etc., could more than double in numbers from 1,500 to over 3,000, between 1969 and 1975. In addition the numbers of those employed indirectly by tourism in agriculture, handicrafts and construction etc. would also be expected to rise considerably.

183. The State's involvement in the tourism sector is considerable due to its ownership of several hotels and majority holding in the largest travel agency (apart from its interest in Royal Air Cambodge). However the current Five Year Plan, which accords the priority to the tourism sector while allocating relatively little from the budget, demonstrates that the Government expects private enterprise to take a considerably greater share of the new investment in the sector. In line with this policy, private hotel investments are now accorded tax holidays and the importation of duty-free construction materials. The State still requires a central planning and coordinating agency and, in theory, the Department of Tourism should fill this role. However, it tends to lack dynamism and apart from its vital need for a better statistical and research service, seems ignorant of the dangers which exist in the development taking place at Siem Reap. If tourism is to expand rapidly in Cambodia in a way which does not fundamentally damage the basic attractions, the Department of Tourism must, through studies of the type suggested for Siem Reap above, appreciate the problems and move to develop the industry on a planned and coordinated basis rather than in the haphazard way which presently appears likely.

I. Education

184. The provision of general education has been a task of high priority since the country became independent, as little had been done under the Protectorate in this field. In 1955 only about 230,000 boys and 58,000 girls attended public primary schools, and another 25,000 attended private schools. This represents an enrollment rate of about 37 percent for the total. Furthermore, the pagoda schools were the only educational facilities in many rural areas. Much of their teaching was religious and not oriented to the provision of practical knowledge.

185. Achievements in the following 15 years have been quite impressive. A total of 920,000 children attended primary school in 1968, bringing the enrollment rate up to 76 percent. Of these, 382,000 were girls. This rapid expansion, much of which had to take place in rural areas, required a substantial effort in teacher training so that the number of primary school teachers could reach the present figure of about 23,000 compared with 6,900 in 1954. Over 2,000 new schools were built, partly with voluntary contributions from the local people.

186. Progress in secondary education appears even more remarkable; from about 5,300 in 1954, the number of pupils increased to 118,000 in 1968, and the number of teachers from 150 to 5,000.

187. It is difficult to comment on the quality of primary and secondary education, but informed observers note a certain deterioration which seems almost inevitable considering the rapid numerical expansion. It appears difficult to meet teacher requirements at present; for example, against a total requirement of 3,500 additional teachers in 1969 only 700 were produced; this however in part seems to be a consequence of budgetary constraints.

188. Higher education has also undergone a period of rapid expansion. The number of university students went up from about 1,700 in 1960 to about 7,000 in 1968, of which 1,460 were studying at the Technical University, created in 1964 and supported by technical and financial assistance from the USSR. At present there are 9 universities and 34 faculties, including the Agricultural University. For a country with the economic structure of Cambodia, it is disappointing to see only 130 students in agriculture in 1968.

189. In a general way, the educational system has been built up with relatively little consideration of the requirements of the economy. Man-power planning in Cambodia has not yet started. There is nothing to be said against continued rapid expansion of primary and secondary education, except that the point has been reached where more benefit could be achieved by consolidation and quality improvement. School equipment is badly lacking. The curriculum in rural primary schools is too much patterned after French education and is of little practical use to the future Cambodian farmer. Also there is the question of cost. About 12 percent of the national budget was spent on education in 1954. This ratio has today reached 24 percent. Education expenditures have grown so rapidly that general administration and economic services had to be cut back. As noted further below, this is not a policy that can be continued for much longer.

190. A general reappraisal of achievement should include a review of primary and secondary school curricula, and of ways and means of promoting vocational education, both in vocational schools and to some extent as part of general education, particularly in the rural part of Cambodia. The tendency at present is for the system to produce far too many candidates for white collar jobs, and the prejudice is still widespread that the purpose of education is to guarantee social advancement to the school leavers, with the orientation generally being towards government service.

J. Banking and Credit

Financial Institutions

191. The banking sector comprises the Central Bank (Banque Nationale du Cambodge), two state commercial banks (Banque Khmère du Commerce, and

Inadana Jati) which extend mainly short-term credit, and the National Investment Fund (Caisse Nationale d'Equipelement) which is to be transformed into a Development Bank, and so far has been granting medium- and long-term loans to industry and agriculture. An Agricultural Bank was established in 1969, but it is still in the process of organizing its operations. Outside the banking sector, the most important financial institutions are the Royal Office of Cooperation (OROC), which advances credits mainly to agricultural cooperatives, the National Insurance Company (S.N.A.), which has the insurance monopoly since the nationalization in 1963, and the Government Pension Fund (C.P.C.K.).

192. The Central Bank (B.N.C.) was established in December 1954 as a mixed enterprise, although there have been no private shareholders. After the nationalization of the banking sector in 1963, it became a state enterprise (for its assets and capital structure see Table 6.4). B.N.C. is, in the first place, a bank of issue. According to its statute, bank notes are backed by gold and foreign exchange to an extent not less than 33 percent. The B.N.C. makes advances to the Treasury the extent of which, according to its statutes, cannot exceed 25 percent of the fiscal receipts of the preceding year. The amount of such advances now stands at CR 1.5 billion. The 25 percent limitation is not too meaningful, however, since B.N.C. is also enabled to extend credit e.g. to the Caisse Nationale d'Equipelement for the financing of government investments. Such credit has been obtained e.g. for financing local currency costs of the railway project, the petroleum refinery, etc. B.N.C. may make commercial advances up to 90 days on collateral, rediscount commercial paper of less than 180 days and grant production loans to the primary and secondary sectors for a period not exceeding 300 days on the basis of eligible paper. Through its Foreign Exchange Office, B.N.C. controls all foreign exchange transactions. The B.N.C. is to ensure monetary stability. To control money supply, it may buy and sell government securities and private credit instruments of high quality. Finally, B.N.C. is the consultative organ to the government on monetary and other economic matters.

193. Before the 1963 economic reform, four Cambodian banks (Banque Khmère, Banque Commerciale Cambodgienne, Banque Souvannaphum, Banque de Phnom Penh) and five foreign banks (Banque Nationale pour le Commerce et l'Industrie, Banque d'Indochine, Banque Franco-Chinoise, Chartered Bank Ltd., Hong Kong and Shanghai Bank) were in operation. With the nationalization of banking, the foreign banks were made to withdraw, private banks were liquidated, and two new banks were established in their place whose share capital is held by the B.N.C. The Banque Khmère pour le Commerce absorbed the Banque Khmère and its share capital was further increased by a CR 100 million participation of the Central Bank. In 1968, capital and reserves amounted to CR 267 million. Inadana Jati was established in 1964 with a paid-up capital of CR 100 million. They both have branch offices in the major provincial towns.

194. The government seems determined to maintain the two state banks in their present form, as it is felt that they have been relatively more successful than any other institution created as a result of the 1963 reform, by adequately serving the needs of trade and fulfilling broad

national objectives such as increasing bank branches in the provinces, accommodating credit needs of the government sector, etc. Nevertheless, the opinion has recently gained ground that in conjunction with the proposed liberalization of foreign trade, it would be beneficial for the economy to permit newcomers into the banking sector. The idea is that in permitting entry to foreign banks, they should be obliged to bring in new resources in the form of foreign medium- and long-term deposits. They would carry out specialized activities, such as credit to agriculture and industry, hotels, real estate, but would not be allowed to accept sight deposits and be involved in foreign trade. Private banks would however be allowed to operate in the free zone of Sihanoukville. Such an approach is not likely to meet with immediate response by foreign banks.

195. The National Insurance Company emerged in 1964, following nationalization, as a successor to the mixed enterprise Société Khmère d'Assurances. Its paid-in capital is CR 31.6 million and the assets amount to CR 200 million. S.N.A. insures against all risks except life. The profits are turned over to the Treasury. The Government Pension Fund derives its resources from the 6 percent deduction from the salaries of civil servants and the 6 percent contribution of the government (originally 14 percent). The total accumulated funds amount to about CR 1.4 billion and are deposited with the Treasury.

196. Cooperative credit through OROC, as noted in paragraph 86 has expanded considerably for a few years, with a high in 1968, but since then the cooperatives have been plagued, if not paralyzed by the problem of repayment; the solution appeared to be the creation of a new Agricultural Bank, but it is not yet operative. Industrial credit, through the National Investment Fund, has been available only on a relatively modest scale since the Fund's resources have been limited, besides an equity capital of CR 170 million, to advances from the Treasury and - for government projects - from the central bank. Under the circumstances, the Fund's credit to private industry altogether has not exceeded CR 200 million in the last ten years. This being highly inadequate, and there being no other industrial finance institution, private enterprises would normally turn to commercial banks and obtain substantial and regularly extended overdraft facilities, as is done in other countries even where an industrial bank exists, e.g. in Singapore. But the two commercial banks in Cambodia have also been extremely hesitant in offering such facilities, mainly because of the tightly restricted re-discount policy of the central bank.

Credit Policy

197. As shown in appendix table 6.1, credit to the economy has been rather erratic over the years, with a high in 1963 of CR 2.6 billion, dropping to one-third of this amount in the following year and only gradually increasing again to a level of CR 2.8 billion by the end of 1968. Figures for the middle of 1969 suggest that there was a considerable credit expansion in the first six months, but general information obtained from private borrowers suggest that there has been no noticeable relief from the tight credit policy of recent years.

198. There is little doubt that the nationalization of banking in 1963 is the principal cause for the inadequacy of credit. The statutory restrictions on the central bank's credit to the government has caused an unduly large proportion of commercial and specialized bank credit to be pulled into the public sector, where the growing number of state enterprises, some of which almost permanently in deficit, created growing needs for bank accommodation. At the same time, the financial resources of the banks, already limited before the nationalization, contracted sharply. Time deposits which represented only a fifth of total deposit resources, did not decline much, but demand deposits contracted from CR 1.9 billion in 1962 to CR 0.7 billion in 1964, as shown below. One of the results of nationalization was the flight into currency; the ratio of currency to the total stock of money has gone up from 48 percent in 1962 to 75 percent in 1969.

Deposits With Commercial Banks
(CR million)

<u>End of Year</u>	<u>Demand Deposits 1/</u>	<u>Time Deposits</u>	<u>Savings Accounts 2/</u>
1960	1,432	380	-
1961	1,473	320	-
1962	1,923	394	-
1963	1,165	281	-
1964	712	334	-
1965	1,133	515	22
1966	1,400	597	34
1967	1,775	613	54
1968	1,765	536	64
1969 <u>3/</u>	1,468	484	71

1/ Sight deposits and current accounts.

2/ Only for Inadana Jati.

3/ September.

199. Total bank deposits today are no larger than what they were seven years ago. This has not only to do with the lack of effort on the part of the banks to revive and promote the banking habit (e.g. by an appropriate interest rate policy for deposits), but also with the general slowdown of the economy which, in turn, is partly related to monetary and credit policy. The government itself has succeeded in restraining the budget deficit and limiting its recourse to the central bank, but the latter continued strict control over the commercial banks' lending operations. The overriding consideration of the central bank has been to avoid inflation, but in imposing a credit squeeze on private borrowers, other motivations have been operative, including the belief that leverage could be used to force private cash assets held abroad back into the country.

Money and Prices

200. Inflation has successfully been avoided in Cambodia. From 1960 to 1968, middle class consumer prices increased by about 3.7 percent a year, and the average GDP deflator averages 3.9 percent a year for this period. It would be less if it had not been for the establishment of relatively high government fixed prices for major agricultural crops in the intervening period, and for other non-monetary factors in connection with the import policy. The cost of living index for the working class increased only 2.5 percent a year.

Growth Of Money Supply and GDP
(Percent)

	1960	1961	1962	1963	1964	1965	1966	1967	1968	1960- 1968 Average
GDP (current prices)		7.6	9.0	10.0	2.0	10.1	7.9	5.1	10.7	7.8
GDP (constant prices)		-3.7	8.2	7.3	-2.7	4.6	7.9	5.1	4.6	3.9
Money supply		10.5	0.6	-	1.7	6.0	12.0	11.0	1.7	4.2
Consumer price index		7.8	3.6	6.3	4.3	3.1	-1.2	0.9	4.9	3.7
Money supply as % of GDP in current prices	26.2	27.9	25.2	22.9	22.8	22.0	22.7	22.8	24.1	
Money supply as % of GDP in constant prices	20.0	23.3	21.6	20.1	21.0	21.3	22.8	22.8	22.8	

201. The above figures show that money supply has increased at a pace only marginally faster than real GDP, allowing virtually for no monetization of the economy. In fact, money supply decline in proportion to GDP at current prices. Adequate information is not available to obtain GDP deflators for the different sectors of the economy during this period, but it must be assumed that most of the price increases occurred in agriculture, which in real terms grew only 1.8 percent a year which means more slowly than population, while the secondary and tertiary sectors expanded, again in real terms, at 6.2 percent a year.

202. In 1969 the central bank continued its orthodox credit policy in the face of a significant upward pressure on the price of rice, following the drought affecting the 1968/1969 crop. There were reports in late 1969 of Cambodia actually importing rice, although on a small scale, from China.

The 1969/1970 crop, however, is expected to be very good, and prices should come down. There were also expectations for a significant push on domestic prices following the August 1969 devaluation, but it was realized by November that no such effect had taken place. Central bank officials attributed this fact to a general shortage of money.

203. Nevertheless, there are no indications for a change in credit policy. One hurdle for the adoption of a more liberal approach by the BNC is the belief that large quantities of bank notes are (a) hoarded because of lack of confidence in the government's management of the economy, and (b) in circulation outside Cambodia in connection with illegal trade transactions with Viet Nam (see paragraph 319 below). Thus fears are entertained that (a) revived confidence in the economy, if the proposed liberalization of foreign trade is carried out, would induce dishoarding and obviate the need for more liberal credit, and/or (b) peace in Viet Nam might cause a massive return flow of currency.

204. It would seem that monetary changes of this kind are not sufficiently imminent to justify a deflationary policy. Nor is it desirable, by denying credit to the private sector, to further postpone the day of a resurgence of general confidence in the interest of monetary stability. There are other means to cope with the eventuality of dishoarding or with the threat of currency influx. Even if some inflationary pressures were eventually to materialize, this would seem to be a lesser evil than continued economic stagnation.

CHAPTER III

APPROACH TO DEVELOPMENT

A. Savings and Investment

205. The slowdown of the economy in the last five or so years probably bears little relation to the level of investment, at least as far back as pertinent data are available. Total investment as a proportion of GDP has been fairly stable at an average of 17 percent between 1962 and 1966 and has only recently shown a tendency to decline to about 15-16 percent. Except for this decline, the level of total investment as such is not to be regarded as unsatisfactory; it is its limited effectiveness that is left to be explained.

206. Public investment has been running at close to 7 percent of GDP up to 1966. About 10 percent of this was in industrial state enterprise, and the other 90 percent went largely into infrastructure, e.g. transport, power, and administration. It has already been noted that considerable excess capacity has been installed in power; in the case of transport, the immediate effect of new investments on the productive sectors is very small in any case, and administrative buildings mainly contribute to GDP growth while being constructed. It may also be said that a considerable amount of construction was devoted to nation-building. For example, Cambodia today has a fine sports stadium, a modern sports and youth complex, a new National Theater, a National Film Theater and several other facilities of national pride, besides large new hospitals, schools and universities including the Soviet-Khmer Technological Institute.

207. About 77 percent of public investment in the last seven years was in construction; this proportion has been fairly constant over the years. Although a certain amount of this has been for rural infrastructure, very little of public (as well as private) investment has benefited the agricultural sector.

208. Private investment, including mixed enterprises, has increased over the years but in proportion to GDP remained about constant at around 10-11 percent. However, if the Petroleum Refinery and other government majority controlled enterprises are excluded, private investment has declined appreciably in relation to GDP.

	<u>Investment and Savings</u>						
	<u>(% of GDP)</u>						
	<u>1962</u>	<u>1963</u>	<u>1964</u>	<u>1965</u>	<u>1966</u>	<u>1967</u>	<u>1968</u>
Private investment	10.2	10.1	9.5	9.6	11.8	11.5	9.9
Public investment	<u>7.7</u>	<u>7.4</u>	<u>6.8</u>	<u>5.2</u>	<u>7.0</u>	<u>4.0</u>	<u>5.2</u>
Total investment	17.9	17.5	16.3	14.8	18.8	15.5	15.1
National savings	<u>8.5</u>	<u>13.9</u>	<u>15.6</u>	<u>13.8</u>	<u>13.8</u>	<u>14.0</u>	<u>12.6</u>
Resource Gap	-9.4	-3.6	-0.7	-1.0	-5.1	-1.5	-2.5

209. As a proportion of total investment, imported transport equipment and machinery went down from 25 percent in 1962 to 18 percent in 1968, with an absolute decline in real terms. All of the increment in investment over this period was for construction and stocks. Residential construction has been an important outlet for private savings since the 1963 reforms.

210. The savings rate shown above is subject to significant changes from year to year, which is difficult to explain; national accounts data from which they are derived are not reconciled with the balance of payments, and a satisfactory breakdown between public and private savings is not available. In particular, the financial sources of state enterprises and public corporations (railways, ports, etc.) and the amounts of their deficits is not well known. The government itself has persistently had negative savings in the order of 2 to 4 percent of GDP. It appears that private savings over the years have varied between 14 and 20 percent of GDP, which is substantially more than was invested by the private sector. Inversely, foreign financing in the public sector fall substantially short of covering the public savings gap. In addition to deficit financing, some other means may have been used to effect a resource transfer to the public sector, but as already noted, this is one of the fields where much more research is needed to throw more light on the basic facts.

211. For a country in the situation of Cambodia, it is natural to expect a high incremental capital-output ratio, particularly in a period where there was a substantial need to build up infrastructure. While this need today is still far from being met, it is fair to say that in many respects the existing infrastructural facilities are quite satisfactory and that within that framework the optimum pattern of investment will shift towards the productive sectors. Some pronouncements to this effect have occasionally been made in the past, but it proves to be a difficult task, particularly as regards agriculture.

B. Objectives and Issues

212. Official objectives and target for economic development in Cambodia have generally been modest. The projections of GDP growth in the Second Five-Year Plan are generally a projection of past trends and do not imply the initiation of ambitious programs. More than a simple awareness of existing constraints, including limited natural endowment, this also reflects an appreciation of certain sets of values inherent in Khmer society. Social development takes precedence over material production. Buddhism supports a quietist attitude to exterior circumstances in life. Awareness of poverty and dissatisfaction with the absence of modern technology and gadgets are not widespread. There is no urban proletariat to speak of. And the Khmer farmer is widely known for his remarkable self-sufficiency, pleasant nature, and happiness.

213. The typical Cambodian peasant still lives and works within a set of beliefs and convictions within which the supernatural has a place in the facts of daily life, and events relating to it appear of longer lasting consequence than the satisfaction of new material wants. There are many who submit more easily to the laws of nature than to the demands of modern technology. Ploughing the field with internal combustion engines, or spraying foreign industrial chemicals over vegetation that has been beneficent and delicious to man (giving nourishment to those who respected the laws of nature) meets with an instinctive mixture of interest and caution. Reticence towards the adoption of modern cultivation practices is thus a factor to be reckoned with in Cambodia. But the Chief of State, while respecting religious values and, in fact, forming part of them, has incessantly advocated agricultural modernization and, more than that, propagated farm mechanization, seed improvement and fertilizer use by personally donating tractors, pumps, seeds and the like to large numbers of selected villagers. This has not been without effect in moderating prejudice against modernization.

214. Agricultural development commands top priority in the thoughts of the Government. While rubber (6 percent of Cambodia's agricultural value added and 2 percent of world natural rubber exports) has the highest yields in the world, paddy (a third of Cambodia's agriculture) is cultivated with traditional methods and low yields (1 ton per hectare). One-fifth of rice production or about 500,000 tons continues to be exported, but to maintain this source of foreign exchange in the future, the achievement of higher yields will be a precondition because the growth in domestic consumption would otherwise sooner or later eliminate the export surplus.

215. One reason for the Government's giving highest priority to agricultural development is that the Khmers who represent over 90 percent of the population have not yet taken to non-farming activities on a scale that would yet alter Cambodia's national complexion as a farming society. Unlike e.g. in Malaysia, the foreign minorities, predominantly devoted to trade and other money-making activities, are too small to play an active role on the national scene. This is not to say that their influence is negligible in the capital, but the extreme hesitancy of the Government in the recent past to adopt any measure of trade liberalization that could be construed as a favor to Chinese business, gives a measure of the bias in the ruling class in favor of Physiocratic concepts.

216. At the same time, prime emphasis has traditionally been placed on social advancement by the Government. This is reflected in the fact that social expenditures in the last 15 years have been increasing two and a half times as fast as total revenues of the National Budget, of which they absorb today 35 percent. While the bulk is absorbed by education, part of this effort is directed at improving government services in the villages to improve living conditions. The ministries of public works, education, and health are all in some degree involved in helping the villagers to improve their sanitary conditions, introducing more healthy concepts for housing construction, building village roads, dispensaries and schools,

and introducing modern means of communications including radios - and probably at some future stage television as well. There is indeed a whole philosophy about gradually reducing the difference not only in the living standard between the cities and the countryside, but of the difference in the way of life. The objective is to stop migration from the country into the towns, and the most radical way to achieve this is the provision, in the villages, of all the amenities that have so far made the people move to city agglomerations; in other words, transform the "rural habitat" up to city standards. From a cursory glance at the villages, it would seem that such an objective is lacking in realism. Indeed, the difference in urban and rural living standard has kept increasing so far. But radical proposals of this kind form part of the local scene and indeed, of the charm of Cambodia.

217. The objective of agricultural development as such has, perhaps inevitably, been approached with a degree of paternalism in past years. In other words, the Chief of State donated farm equipment while travelling through the country, and the government attempted to lift ex-farm prices by subsidizing government procurement operations for paddy and other crops. Price control in general has been rather widespread, and prices for most agricultural inputs as well as for manufactured goods for general consumption have been kept at a low level. In the case of imports, this has been achieved until the devaluation by permitting essential goods to be imported at the official exchange rate which was about half the free rate.

218. In many countries, price incentives are an effective means of stimulating agricultural production. In Cambodia also there are examples where this approach has been successful, such as for jute. On the whole, however, and particularly as regards paddy and maize, it has failed to produce results, and since the early sixties agricultural production has shown signs of stagnation. There is no lack of reasons that can be advanced to say that it is in the nature of things for Cambodian agriculture to move only very slowly; however, it should be remembered that Cambodian agriculture did move very rapidly in the second half of the fifties. Rice production increased from an average level of 1.5 million tons up to 1955, to 2.4 million tons in 1960, at which level it has remained throughout the sixties. The reasons for this are not well understood and would no doubt deserve some study.

219. For the future, the government's approach is to rely much more than in the past on irrigation, including some large-scale projects. As pointed out in Chapter II, there is significant potential in developing water management in Cambodia to achieve higher crop production, in combination with better seeds and with fertilizer. A systematic approach to introducing the Khmer farmer to modern agricultural techniques and, in particular, to making the best use of future availabilities of water, has not yet been found. It is in this area that the government will have to devote much effort and perseverance to the creation of an organizational framework to carry the message to the farmers along with the inputs. At the same time, the message itself needs further improvement through research before it can be expected to produce results. This is particularly true with respect to fertilizer use.

220. In the light of the very uneven distribution of Cambodia's population and the availability of agricultural land in virtually unpopulated provinces, particularly those east of the Mekong river, colonization has quite an important objective and continues to be so, particularly once the problems of military insecurity are overcome with the end of the Viet Nam conflict. Since voluntary migrants for colonization of new land are not forthcoming in great numbers, part of the effort has in the past been carried by the military forces, and not unfrequently, surrendering groups of rebel elements, after obtaining pardon from the Chief of State, have been implanted into settlement areas.

221. Given the objective of "peopling the land", there is no sense of urgency about restraining population growth in Cambodia. No initiative has yet been taken to promote family planning.

222. Manufacturing industry was given priority second only to agriculture in the Second Plan. As noted, bilateral capital assistance has been obtained to build a nucleus of manufacturing industries in Cambodia. There are several reasons, however, why industry is not foremost in the minds of the government. One is that the size of the market and scarcity of industrial skills limits the scope for realistically-sized import substitution industries in certain fields. Second, it is realized that a big push for export industries would not be a realistic goal for an agriculture-based economy like Cambodia particularly if it is state enterprise oriented, although processing of agricultural products would well be envisaged for export. Third, industry is a politically cool issue given the fact that most industrial workers are non-Khmer, and that promising Khmer private entrepreneurs are far outnumbered by Chinese. Fourth, and connected with the preceding point, industries implanted in a small market as infant industries are expected both to be in need of protection, and of acquiring monopoly power, and both ideas are unattractive.

223. As outlined in the preceding chapter, new industries are envisaged in several fields, all in some way tied in with agricultural development. Regional development of industries is given considerable emphasis; the policy is to attract industries to Sihanoukville and to discourage industrial concentration in Phnom Penh. For this purpose a Free Zone is proposed in Sihanoukville with the idea of attracting foreign business and creating an international entrepot center. There is not much that could be said against a free zone, but the locational or other advantages which Sihanoukville could offer, if any, are outweighed by the generally unfavorable climate for private enterprise as well as nationalized banking, etc. to say nothing of the difficulty of finding industrial labor, and one does not see how Sihanoukville, even if the port was expanded as is now suggested.

224. Tourism has been given increased attention. Cambodia does have significant potential for expansion of tourism, and past bottlenecks like flight connections, landing rights, and hotel accommodations, are in process of being removed. On the future development of Siem Reap (Angkor), some open questions remain regarding the coordination of tourist facilities, infrastructure, and the protection of monuments, and it is hoped that a study will soon be undertaken.

225. Besides these sector objectives, several questions and issues should be highlighted, some of which have already been discussed in some detail, or will be treated later on. They related to (a) foreign trade liberalization, (b) exports, (c) taxation, (d) education, and (e) economic information.

226. Trade liberalization has been discussed within the government throughout the past year. It is almost universally agreed that SONEXIM has not fulfilled the hopes that went along with its creation. In exports, it has been initially successful in rice, but the impact of government procurement on production levels has not been evident. For some other exports, SONEXIM has been a failure and the trade function has in effect already returned to the private sector. For imports, SONEXIM appears not to have achieved anything except add to procedural delays and costs. A program for partial dismantling of SONEXIM, leaving it with the sole function of exporting rice, rubber and maize, has been under consideration for a long time and may be adopted sometime in the near future. Such a move could not only contribute to more efficient use of foreign exchange resources and more rational operation of industries using imports, but it would also be taken by the private business community as a sign that the government is serious about a new and more open economic policy in general, and thus contribute to a beginning of renewed confidence.

227. As regards exports, the government does not regard this a policy issue except that the generally poor export prospects are a source of concern. In official statements the promotion of exports occupies considerable space, but the only way of achieving a faster growth rate, as visualized for the immediate future, is to import more fertilizer to increase the yields of rice for export. There might be no alternative to rice at present, but long-term world market prospects for rice are not particularly favorable, and for the long term therefore the government would be well advised to undertake a much more systematic study of other export possibilities.

228. Taxation is another field where rather little effort has been made to identify new sources, in spite of frequent reference to the government's present and future financial squeeze. In fact not only new taxes but a fiscal reform is likely to become more and more inevitable as time passes.

229. Education is the one sector which has substantially contributed to the government's financial problems. It seems to be generally recognized that the time has come to put some financial limits on the rapid growth of general education facilities, and the 1970 budget seems to imply a significant slow-down. More fundamentally, the time has also come to take stock of past achievements and reappraise the direction in which the educational system should move in the future.

230. Finally, there is a great need to improve the quality of information on the whole economy. Data available are much poorer than what they could be with a relatively modest additional effort. This will be further elaborated at the end of this chapter.

C. Planning

231. Economic planning has been given a role to play in Cambodia at a relatively early stage. Already in 1956 a Two-Year Plan was prepared and a High Plan Council established under the chairmanship of the Prime Minister and composed of the principal ministers, the governor of the Central Bank and other members including representatives of the private sector.

232. The Two-Year Plan 1957-1958 consisted mainly of a list of projects for the public sector and served as an experiment to gain experience. Two Five-Year Plans have since been prepared, the first (1960-1964) being followed by the second with an interval of three years. Cambodia is now in the third year of its Second Five-Year Plan (1968-1972).

233. A general feature of planning in Cambodia is the relative remoteness of the planners from the field of action. The experts who have prepared Plan documents have not directly participated in the decision-making process except for having the Plan adopted by the government.

234. Plan execution is today still limited, by and large, to the sanctioning and coordination of investment projects in the public sector. This is of course much less than what both Five-Year Plans purported to be. The Second Plan stated a number of macro-economic and financial targets as well as production goals for the different sectors. However, the sector plans and the general plan were poorly linked, mainly because the phasing and the financing of investment projects would not be projected with sufficient accuracy, and the macro-economic framework was based either simply on trend extrapolations modified on grounds of general considerations, or on statements of desiderata not backed up with an analysis of their practicality. The Plan was explicit on overall priorities, but these were translated into sectoral resource allocations only in the form of lists of projects to be undertaken during the Plan period, without translating these into five-year expenditure targets. Nor was the description of the financial resource constraints, and possible remedies, part of the Plan. As a result, the annual budgeting of development expenditures has been carried on generally without reference to the Five-Year Plan.

235. Project preparation is a special weakness in the development effort, and this is not unrelated to the fact that in the past, foreign assistance, e.g. from France or the People's Republic of China, has been sought - and received - for projects for which there was neither an economic feasibility study nor a government agency equipped to judge on their merits within an overall resource and investment pattern. The High Plan Council sanctions all projects beyond a minimum size, both public and private, but all important decisions are referred to the Chief of State, who also takes action unilaterally. The Ministry of Plan today exists only in name and is virtually devoid of staff.

236. The First Five-Year Plan proposed an economic growth rate of 5 percent per annum which was modest if compared with the 9 percent ^{1/} per annum achieved in the preceding five years. However, only 3.4 percent were realized in the Plan period. The investment target which was put at CR 12 billion for the five years, was exceeded by more than half, but while the Plan had foreseen CR 8 billion in the public sector, only about CR 5.5 billion was achieved. Foreign resources which had been projected at CR 2.4 billion, were disbursed in the amount of CR 1.5 billion. Private investments went beyond CR 13 billion, or 55 percent of the total, and 3 times as much as projected. Private investment went very largely into construction, not anticipated on that scale in the plan, and a quarter was for production equipment. In the public sector, less than two-thirds of the amount proposed was invested in the productive sectors. In the social sectors on the other hand, investment fell short only by 10 percent.

237. At the outset of the Plan, it had been decided that all investments would be centrally administered by the Ministry of Plan, including foreign assistance. This was not implemented and the National Budget had its own investment funds allocated side by side with Plan outlays. Furthermore, substantial portions of Plan funds were utilized for current expenditures. About 30 percent of the CR 1.5 billion of foreign aid were also made available for current expenditures.

238. The disappointing performance of the economy under the First Plan has to be seen in the context not only of the failure to reach public sector investment targets in the productive sectors, but also of the decline in foreign aid and the financial austerity program announced simultaneously with the economic reforms of 1963. Paddy production stagnated, value added in forestry declined, and livestock advanced very slowly.

239. For the Second Five-Year Plan starting 1968, the same 5 percent annual growth target was adopted. Accordingly, GDP is expected to increase by CR 178 billion between 1968 and 1972. Given a capital/output ratio of 3.6:1, the achievement of the set target calls for an investment equal to 18 percent of GDP, or CR 32 billion, during the entire period of the Plan. Agriculture was given the highest priority, followed by industry, tourism, transport, and social services, in that order. This clearly reflected the realization that past efforts had gone too far towards the promotion of social goals and infrastructural assets and not far enough towards increasing production.

240. Of the proposed total investments of CR 32 billion, a quarter each was proposed to go into agriculture and industry. Such global allocations were rather theoretical since there were neither past data on actual investment by sectors, nor did the Plan itself specify how these sectoral investments would be shared between the public and the private sectors. As shown below, CR 14 billion or 44 percent of aggregate invest-

^{1/} Somewhat lower if adjusted for crop variations (failure in 1955 and record crop in 1960).

ment was proposed to be in the public sector (compared to 29 percent during the First Plan). Net of foreign aid, this would have meant an increase in domestic public resources from CR 4 billion to CR 8.3 billion between the two Plans. The implications of this for taxation and the credit structure are not, however, dwelt upon in the Plan, except that the domestic effort is described as perhaps too large, and an alternative target for 4 percent GDP growth a total investment of only CR 25.2 billion is envisaged.

	<u>First Plan 1960-64</u>		<u>Second Plan 1968-72</u>			
	<u>Target</u>	<u>Actual</u>	<u>Targets</u>		<u>Increase over First Plan</u>	
			(A) <u>1/</u>	(B) <u>1/</u>	(A)	(B)
Total investments	12.0	19.0	32.0	25.2	69%	33%
Public	8.0	5.5	14.0	10.7	155%	95%
of which: Foreign aid	n.a.	1.5	5.7	nil	285%	
Private	4.0	13.5 <u>2/</u>	18.0	14.5	33%	7%
Of which:						
Agriculture	1.7 <u>3/</u>	0.8 <u>3/</u>	8.0	n.a.		
Manufacturing	1.1 <u>3/</u>	0.7 <u>3/</u>	8.0	n.a.		
Power	0.5 <u>3/</u>	0.4 <u>3/</u>	4.8	n.a.		
Transport/Communications	2.2 <u>3/</u>	1.9 <u>3/</u>	6.4	n.a.		
Social & other sectors	1.9 <u>3/</u>	1.1 <u>3/</u>	3.2	n.a.		
Government	0.6	0.6	1.6	n.a.		

- 1/ Alternative targets, based in the case of (A) on the assumption of 5% per annum growth of GDP, and 4% per annum for (B).
- 2/ Of which 32 percent residential (including rural) construction, 29% other construction, 25% machinery, about 10 percent livestock, and 4% other agriculture.
- 3/ Public sector only (Plan did not give global targets, and actual figures for both sectors combined not available). Data are from Second Plan.

241. One clear policy implication of the Plan was a continuation, if not further tightening, of measures favoring State enterprises and discriminating against the private sector. The financial targets shown above, with private investments of about CR 3.6 million (A) or CR 2.9 million (B), compare with actual private investments, during the three years preceding the Plan, of CR 3.3 billion per annum on average (see appendix table 8.5). Even if we assume that the planners were working on the basis of inadequate information, the proposal that private investments should grow so slowly (or decline) can only be understood in the context of very unfavorable policy assumptions vis-a-vis private enterprise, including presumably the policy, so far in effect pursued, of denying adequate bank credit to the private sector and thus effecting a transfer of private savings through the banking system into the public sector.

242. The total cost of public sector projects inscribed in the Plan adds up to CR 11.7 billion (see appendix table 5.6) but this figure of course includes expenditures for projects carried beyond the Plan period. The implied investment strategy, as noted, is to concentrate on the productive sectors. In agriculture the aim is to increase production and productivity through irrigation and flood control systems, mechanization, colonization of sparsely populated regions, etc.; to promote cattle raising; to promote production of industrial raw materials; and to reduce the difference in the standard of living between urban and rural areas.

243. In the industrial sector, the Plan proposes the establishment of new industries processing domestic raw materials and producing agricultural inputs, such as fertilizer, pesticides, agricultural implements in substitution of imports. A major conditioning factor in the fulfillment of these goals is the attitude of the entrepreneurial class, and the planners express their apprehension in this regard.

244. The major part of the investment envisaged for power will be absorbed by the Prek Khnot dam, already in construction. Finally, the investment in social services purports to create poles of attraction in sparsely populated regions with high development potential, by providing public health, education, community centers and other amenities, to keep population on the land and prevent a migration to the towns.

245. As of the moment, feasibility studies have been prepared only for very few projects listed in the Plan, and none at all for those to be undertaken by public and mixed enterprises. Projects in the government sector which appear well advanced or which are under study have been referred to in Chapter II. It is clear, if only for this reason, that public investment will fall short of the planned level for the period of the Plan; but it is also a matter of financial resources as discussed further below in paragraph 295.

246. The sectoral growth targets of the Plan are somewhat difficult to pin down. Since no adequate data for the national accounts had been available when the Plan was drawn up, tentative 1964 benchmark data for GDP were used, and the overall target growth rate of 5 percent per annum was assumed, as a working hypothesis, to have been realized from 1964 to 1968, the first year of the Plan. In other words, an 8-year period was used to project GDP at 1964 prices, assuming no price changes. On that basis, the following picture can be reconstructed from the Plan document.

Value Added By Sector
(CR billion)

	Actual 1964 <u>1/</u>	Target 1972 <u>1/</u>	Plan Annual Rate of Increase 1964-1972 %	Actual 1964 <u>2/</u>	Actual Annual Rate of Increase 1964-1969 <u>2/</u> %
Primary sector					
Agriculture	10.8	14.8	4.0	11.2	2.2
Secondary sector	4.8	8.6	7.7	4.1	8.7
of which: Power	1.6	1.9	2.2	0.3	9.6
Industry	1.8	3.9	10.2	2.6	9.6 <u>3/</u>
Construction	1.3	2.8	10.2	1.3	12.5 <u>3/</u>
Tertiary sector	10.8	15.6	4.7	11.1	4.6
of which: Trade	5.2	7.8	5.2	5.9	2.8
Government	3.6	4.7	3.4	3.6	8.2
GDP	26.4	39.1	5.0	26.4	4.2

1/ Reconstructed on basis of percentage breakdown, given in Plan, using current price GDP of 1964.

2/ Derived from appendix table 2.1 giving mission estimates for 1969.

3/ Up to 1968.

247. As seen in the above table, Plan expectations for growth in industry and construction as well as for total services, appear to have been realized in the last five years, including two years of the Plan. The growth in construction is, however, only a recovery from sharp decline in 1964 compared with 1963. In two important respects the Plan has turned out unrealistic, namely (a) in the projection of a 4 percent growth rate of agriculture, and (b) in the proposal that government should be expanding less fast than GDP. Also, the trade sector grew only a third as fast as expected, but this is a consequence of deliberate policies.

248. The performance of agriculture gives rise to concern, since during five years it has been growing less fast than the population. A breakthrough in rice is nowhere in sight and the trend seems to be for the export surplus to decline. The same is true for maize which in neighboring countries has been promoted with remarkable success for export. It will be necessary for the government to face up with some hard facts regarding agricultural growth and revise some of the concepts about what the existing institutions can and should do. Without a much more far-reaching study of the agricultural sector than has been possible in this report, it would be misleading to make specific suggestions, but the general impression emerges

that in building up the institutional framework, e.g. OROC and the cooperative system, economic considerations have been too much intermingled with political and social objectives, placing emphasis on social justice rather than on incentives for production. It should be hoped that the new Agricultural Bank for example will not be forced to serve as another agency to reward deserving groups or areas with additional funds.

249. Regarding the rapid growth of government services, this is in minor part the result of the government having taken over some of the functions of the private sector in this period. More importantly, it reflects the rapid expansion of education, health and social welfare services. As will be pointed out in the following chapter, a change in this policy will probably be inevitable, but on the other hand it would be wrong to continue severely to restrain current expenditures for general administration and economic services, given the need to improve salaries (for which the first steps in more than 15 years were taken in 1969) and to strengthen those departments in the government which are in charge of preparing future investment projects, and of operating those which are completed.

D. Economic Information

250. Statistical material in Cambodia is comparatively scarce, and of what is available very little is processed and published, so that material from different sources has been used e.g. in this report without much possibility of cross-checking and reconciliation. Various parts of the government or even of a ministry are not aware of facts known to individual officials in other parts, and on the whole, there is no systematic channeling of economic information to a central agency on which to draw, although such an agency exists.

251. The National Institute of Statistics and Economic Research (INSERE) is part of the Ministry of Planning; it collects statistical data from different ministries but is not responsible for the quality and consistency of these data; nor has it authority to improve them, and the agreement of each ministry has to be sought when editing them. INSERE is in charge of preparing National Accounts. However, such accounts could be prepared only for the years 1962-1966 while a foreign expert was available, after whose departure they were discontinued. The director of INSERE is the only professional statistician in Cambodia to carry out statistical work. Some clerks have been trained on the job and they attempt to process data which are coming in from the ministries.

252. One problem is that statisticians have no official status, and pay scales are totally unattractive to persons trained abroad. Also, the Ministry of Planning itself to which INSERE belongs, at present exists only in name, and there has been no following-up on the Second Plan since it was produced in mimeographed form in 1967.

253. It is not surprising in these circumstances that statistical information produced by the ministries is often of poor quality, sometimes fragmentary, and inconsistent. In the case of agricultural crops, the Ministry of Agriculture is a comparatively reliable source for production data of paddy, groundnuts, maize and a few other items. It is based on regular crop surveys with sample measurements of yields and estimated acreages. However, the quality of the estimates is uneven because of staff shortages, and crop yield figures sometimes originate in top government instructions by which statistical clerks are to abide. In 1970 an agricultural census is to be undertaken with technical assistance from FAO. Preparations have been nearly completed, and there seems to be good chance for a successful execution.

254. The only demographic census so far was carried out in 1962, and the results have been published. On demographic growth, various experts using different adjustments to the census data, have come up with estimates ranging between 2.2 percent and 3.6 percent per annum. Civil registration is very poor, and in census work it is difficult to translate the people's concepts used e.g. in describing their age into numerically usable form. The agricultural census of 1970 should be used to help improve on this unsatisfactory situation.

255. Statistics on manufacturing industry are particularly spotty and often of little utility. There is no legal obligation to reply to questionnaires issued by the ministry. Foreign trade data have to be obtained from SONEXIM as regards its own transactions, and compared with customs data which are collected regularly but, besides not recording unrecorded trade, also display large variations in individual unit prices for imports as well as exports which cannot be otherwise corroborated. Also, data on the volume of goods imported or exported are always in tons, whether it is rice, fountain pens or motorcycles.

256. To improve on public finance information would require a reorganization of public finances, e.g. integration and reclassification of various taxes, a consolidation of the multitude of independent "special accounts" of the Treasury, and in expenditures, a systematic separation of current and capital accounts. The complicated system of transfers between different accounts and agencies is another problem. Perhaps with some justification there is at present lack of interest in improving financial statistics as long as there is no intention of reforming the financial system itself.

257. Monetary and credit statistics are regularly compiled and the information is quite reliable since there are only two commercial banks, wholly owned by the Central Bank which puts out the statistics. The concepts used in processing and presenting these data will need to be re-organized, since the form in which e.g. monetary tables are set up does not permit this material to give much guidance on monetary policy.

258. In summary, the collection, processing, and use of statistical information will need to be much improved if the government is to take the right economic policy decisions in future efforts to revive various sectors of the economy. It seems fairly evident that past failures in this respect were perhaps not caused, but at least conditioned by the absence of adequate knowledge of short- and medium-term changes in the structural development of the economy. This is particularly true for the money economy and its financial interrelations.

259. Considerable improvements are possible with a relatively modest investment, however, provided a decision is taken to improve the standing of, and to expand the role to be played by, INSERE. Not the least of its present problems is the lack of authority even in technical matters, and its low profile in public relations with government ministries. A more independent status will be necessary while avoiding a too conspicuous position exposing it to political influence. The Institute should be enabled to carry out a training program for statisticians working in the various ministries, as well as to supervise the production of all statistical data. For its own work of compilation, analysis, and edition of economic information including the national accounts, the methodological framework will need to be improved and expanded. For this purpose, some further technical assistance is required.

CHAPTER IV

PUBLIC FINANCE

A. Agencies

260. Public finances are here understood to be those of the government itself and its affiliated institutions, some of which are themselves revenue generating (such as local governments, national lottery and other "special accounts") while others depend entirely on transfers from the national budget and other funds (e.g. the Plan, National Investment Fund, etc.). State industrial and other enterprises like SONEXIM can be treated as part of the public sector in the context of investment and savings, particularly since some of them use their monopoly position (e.g. the Societe Khmère des Distilleries) to generate their own fiscal revenues; however, for present purposes they are treated as being outside of the public finance system.

261. Thus circumscribed, public finance embraces seven principal agencies (or groups of agencies) with independent budgets, but inter-linked with numerous lines of financial transfers, which in total amounted to just under half of government revenues in 1966. These agencies are the following:

1. National Budget
2. Special Accounts of the Treasury (15 agencies)
3. Plan (Ministry of Planning)
4. Local Entities
5. Public Administrative Agencies
6. Pension and Security Funds
7. National Investment Fund

262. A few additional agencies, partly dependent on voluntary contributions and partly on transfers from the budget, should be mentioned but their activities are of relatively minor scope and in any case cannot be included for lack of information. They include (a) the Sangkum Fund which supports the activities of the sole political party in Cambodia, (b) the Oeuvre Nationale d'Entraide (O.N.E.) and (c) the Caisse d'Edification Nationale (C.E.N.), both of which are controlled by the Chief of State and used for purposes of relief donations in the case of O.N.E., and for direct investment aid in the case of the C.E.N. mostly to farmers - and finally (d) the Red Cross.

263. By far the most important entity is the National Budget where about two-thirds of total government revenues and over 80 percent of taxes are collected. The budget is voted each year by the National Assembly, and it includes both current and capital transactions. However, only a part of

capital expenditures is listed separately. Each chapter (corresponding to a ministry) is divided into expenditures for salaries and for goods and services including capital, without specifying the purpose. Expenditures from foreign grants and loans are not inscribed in the budget, nor are their accounts kept in the Ministry of Finance, and information has to be obtained from the executing agencies. The budget does, however, indicate transfers proposed to other agencies. One shortcoming of the budget documents is that no data of actual expenditures for previous years are shown, so that comparisons can be made from year to year only as between the amounts voted each year. Detailed data on expenditures as they are authorized by the Treasury are recorded in the Ministry of Finance but actual outlays have not been registered for many years. However, differences between authorizations and actual payments are reportedly small and the former can be used as a fairly accurate guide.

264. The number of Special Accounts not subject to parliamentary control but administered under the control of the Treasury, has varied over the years. An account is usually closed and the assets transferred to the National Budget whenever its volume of transactions is considered to have become too small. There were 15 Special Accounts in 1968, of which the most important was the Exchange Compensation fund established to collect import surcharges and provide export subsidies (Caisse de Compensation). The rationale for these transactions arose with the overvaluation of the exchange rate, and after the devaluation the volume of these transfers is bound to diminish greatly (for the operation of this system see paragraphs 303-4). In recent years the collection of import surcharges has substantially exceeded payments of subsidies by SONEXIM; part of the net balances have been transferred from year to year to the National Budget.

265. The National Lottery constitutes another Special Account producing regularly a surplus available for transfer to the Budget. Another Special Account is held for government participation in state enterprises as well as Budget transfers to the National Investment Fund (Fonds de Participation et de Souscription Publique). Among the remaining twelve Special Accounts, some are themselves revenue producing while others depend entirely on funds provided by the National Budget. 1/

266. Information on the transactions of some of the Special Accounts is highly unreliable. For example, the national accounts for 1965 and 1966, prepared in the Ministry of Planning, show indirect taxes collected by Special Accounts of some CR 900 million in excess of what SONEXIM and

1/ (1) Fonds d'Investissement économique et Social - (2) Charges des emprunts extérieurs (payment of debt) - (3) Opérations de Cadastrage - (4) Opérations commerciales des domaines - (5) Aide à la production agricole - (6) Agent judiciaire du Trésor - (7) Amendes et confiscations des Changes - (8) Redevances forestières de la coupe - (9) Fonds d'Assurances des produits pétroliers - (10) Amendes et pénalités fiscales - (11) Amendes et confiscations en matière des pêches - (12) Fonds spécial pour la sécurité.

Ministry of Finance records indicate, with the result that public savings are shown as nearly CR 400 million or over a third larger than public investment, in contrast to official figures which indicate a deficit of over CR 600 million in each of these years. No way has been found to reconcile these data because the author of the National Accounts had departed in 1967.

267. The Ministry of Planning was made a separate financial agency when Cambodia started its first Five-Year Plan in 1960. It was to be the executing agency for all public investment expenditures under the Plan, financed from budget surpluses, special accounts and foreign aid, and the National Budget would have covered only current expenditures. In fact such a centralization was never achieved and after a few years the volume of funds channelled through the Plan diminished greatly, while the other Ministries again obtained investment funds directly through the National Budget. For the Second Plan 1968-1972, no Plan expenditures are allocated separately from the National Budget and the Special Accounts of the Treasury.

268. Local Entities (17 provinces, 4 independent municipalities, and 16 Khums) collect some 7 percent of total tax revenue but the major part of their expenditures is financed by transfers from the National Budget. Their expenditures consist mainly of civil servants' salaries, but some investments are also carried out by them, including some works supported by local voluntary labor.

269. Public Administrative Institutions include the universities, hospitals, the national tourism office, and the budget of the Crown, and their expenditures are in most part financed from the National Budget. Pension and Social Security Funds on the other hand receive premium payments from households as well as the government. They have been accumulating funds for a number of years and the government in 1969 reduced its premium payments from 14 percent to 6 percent of civil and military servants' salaries.

270. The National Investment Fund (Caisse Nationale d'Équipement) was created in 1965 and its role combines the functions of a public development bank with those of a financial agent for the government in the execution of its own projects, e.g. the railway line from Phnom Penh to Sihanoukville, as well as projects by public or mixed enterprises, e.g. the petroleum refinery. Its financial resources, besides budget allocations, are foreign and are dividend earnings from investments in public enterprises. A special tax, the dividend remittance tax imposed on private foreign enterprises (taxe exceptionnelle d'équipement) prior to 1963, was earmarked to CNE for public enterprise investments.

B. Government Revenues

271. Although a large number of agencies form part of the public finance sector, the collection of taxes is very centralized. For instance in 1966 of a total tax revenue of CR 4.9 billion, the National Budget collected 86 percent, the Special Accounts 7 percent, and the Local Entities the remaining 7 percent.

272. This does not mean to imply that the structure of taxation by the National Budget is simple. In fact more than fifty taxes are collected, and some are said to be known only to the payee and the tax collector. Much of this complex system has been inherited from the time of the French Protectorate and a number of new taxes has been added since. However, 75 percent of tax revenue is derived from the four most important taxes, i.e. excise, turnover tax, import duties, and income tax.

273. Consolidated revenues in 1968 were 22.7 percent of GDP at factor cost compared with about 21 percent five years before; total tax revenue is equivalent to about 19 percent of GDP and not much different from what it was in the early sixties, but with a temporary decline in the intervening period. Considering the fact that agriculture is hardly taxed and accounts for about 80 percent of the population, such a rate of taxation is not low. Considering, on the other hand, the dominating role which the public sector has taken on itself to perform for the development of the economy, it is hardly sufficient.

274. The evolution of tax and other revenues of the National Budget during the last 12 years is shown below. Consolidated public finance data are available only since 1962 and are given in Appendix tables 5.1/5.2.

282. The entire increment of government revenues through the six-year period since 1962 was used up for current expenditures, which would therefore have grown at about the same pace as GDP had it not been for a gradual reduction in deficit financing. Capital expenditures declined in absolute amounts. This appears surprising in the light of the 1963 reforms which attributed a more important role to state capitalism and in effect for a number of years caused a decline in the ratio of private investment to GDP. Even if investments by state and mixed enterprises are added to government investments, their total declined from CR 1,823 million (7.1% of GDP) in 1962 to CR 1,787 million (4.9% of GDP) in 1968. Three factors help to explain the failure of the government to increase its contribution to the domestic capital formation. Firstly, foreign aid declined as planned. Secondly, the preparation of projects proved to be a serious constraint. Thirdly, the pursuit of a conservative financial policy was combined with an expenditure policy that gave priority to social rather than economic objectives.

283. Consolidated current expenditures are shown in the table below for the years 1962-1968. Data for previous years are not available.

<u>Consolidated Revenues and Expenditures</u>			Compound Annual rate of increase %
(CR million)			
	<u>1962</u>	<u>1968</u>	
CURRENT EXPENDITURES			
<u>Economic services</u>	405	549	5.1
of which: Agriculture	187	313	9.0
Transport/communications	171	171	--
<u>Social services</u>	1,289	2,590	12.4
of which: Education	958	1,903	12.2
Health	293	471	8.2
Defense	1,818	1,780	-0.3
Debt service	6	139	69.0
Administration	1,033	1,230	2.9
Transfers	540	863	8.1
TOTAL CURRENT EXPENDITURES	5,091	7,151	5.8
REVENUES	4,276	7,481	9.7
BALANCE	- 815	+ 330	
PUBLIC AND SEMI-PUBLIC SECTOR FIXED			
INVESTMENT /a	1,823	1,787	

/a Including state and mixed enterprises.

Revenues of National Budget
(CR million)

	<u>1956</u>	<u>1960</u>	<u>1964</u>	<u>1968</u>	<u>Compound Annual rate of increase %</u>
Income tax	184	283	468	678	11.5
Other direct taxes	674	603	614	1,267	5.4
Import duties	413	1,049	1,056	1,198	9.3
Turnover tax	275	670	794	1,223	13.2
Other indirect taxes	414	419	622	1,157	9.0
Total tax revenue	1,960	3,024	3,554	5,523	9.1
Non-tax revenue	994	823	676	957	-
Total	2,954	3,847	4,230	6,480	6.4
Extra budgetary revenues	n.a.	n.a.	827	1,001	4.9 <u>/1</u>
Consolidated revenues	n.a.	n.a.	5,057	7,481	9.4 <u>/1</u>

/1 Last four years only. The difference between Budget and Consolidated revenues constitutes, in essence, household contributions to pension funds, local taxes, and import surcharges collected by the Caisse de Compensation.

Source: Appendix table 5.3.

275. The performance of the various taxes has been quite different. Income tax has been growing fairly steadily at an average rate of 11.5 percent a year. The major part of it (61 percent in 1968) is the tax on profits. Other direct taxes stagnated in the first two periods shown above but doubled in the next four years. They include a small amount of taxes on capital registration taxes, licenses, etc. Recovery of tax arrears in 1968 gave a temporary boost to these "other direct taxes".

276. Indirect taxes, accounting for two-thirds of total tax revenue, have all been growing fairly rapidly except import duties which tended to stagnate after 1960, but the picture would be different if import surcharges after 1963 were included; whereas the volume imported of non-capital goods increased by only one-fifth from 1962 to 1968, import duties and surcharge combined increased by over 50 percent.

277. Turnover taxes are imposed both on imports and on the first sale of local products, and have been growing at over 13 percent a year. An even faster rate was achieved in the case of excise duties which are charged on salt, alcoholic beverages, tobacco, matches, and hydrocarbons.

278. On the whole, tax performance over the years has been fairly steady. Since 1963 GDP at current prices increased on average 7.8 percent a year; this compares with a growth rate of consolidated tax revenues of 7.9 percent a year. Only very minor changes have been made during the whole 12-year period in the field of taxation; no attempt was made to either simplify the system or introduce new taxes, with the exception of the import surcharge in 1963, but the import surcharge is partly offset (and in the early years more than offset) by export subsidies, and its yield will in any case decline after the devaluation since it had been designed principally to correct the overvalued exchange rate.

279. To meet increasing financial demands of the public sector, the policy in the past appears to have been to rely on new extra-budgetary resources more than on taxation. Appendix table 5.1 shows that consolidated non-tax revenue increased from only CR 295 million in 1962 to an estimated CR 2,050 million in 1969. Since the national lottery did not show adequate growth in financial results, a casino was commissioned in 1969 in Phnom Penh to produce CR 400 million of revenue in that year. It has operated successfully during the first half of the year, but later it appeared that gamblers were running out of funds at least in Phnom Penh, so that visitors from more remote parts of the country were induced to this activity. It appears that this operation will be discontinued in 1970.

C. Expenditures

280. Total expenditures through the National Budget increased very rapidly from 1956 to 1962 at a rate of over 20 percent a year. From 1962 to 1968 the rate of increase came down to only 3.6 percent a year (5.8 percent in the case of consolidated current expenditures). This change in tempo reflects the fact that in the early period the government started off from a position where the existing tax system produced more funds than the administration of the newly independent government was geared up effectively to use. Once this constraint was overcome, however, surpluses quickly disappeared, and by 1959 substantial deficits were produced that were covered with foreign assistance, largely from the U.S. As a result, defense expenditures increased fivefold from 1956 to 1963 to reach 5.5 percent of GDP (since then reduced to 4.7 percent), education outlays increased about three times, and the same was true for general administration and for economic services.

281. With the determination, since 1963, to do without assistance from the U.S. and at the same time maintain monetary stability, an austerity program was announced and in fact, as noted, total budgetary outlays since then have expended only about half as fast as GDP in current prices.

284. The most striking change in the pattern of expenditures is the rapid increase in expenditures for education which in 1968 reached a level in excess of total investments in the public and semi-public sectors combined. Similarly, large increases were allowed in the health sector which by 1968 absorbed nearly as large an amount as all economic sectors combined. It is particularly noteworthy, if capital and current expenditures are combined that the total government effort in the field of agriculture as late as 1966 amounted to only CR 323 million and less than what it was in the field of health 1/, and this situation probably still prevails today in spite of the continued pronouncements at the top level of government regarding the high priority of agriculture. This is not to say that education or health are not deserving important financial allocations in Cambodia; in relation to resource availabilities, however, the claims of the social sectors have been excessive, and the implicit priorities reflected in the above rates of expenditure growth are not unrelated to the disappointing performance of the economy.

285. An interesting fact is that total salary payments of the government during this period increased at 8.2 percent a year or more than a third faster than total current expenditures. All of this increase was for expansion of the number of civil servants, particularly teachers. 2/ The level of salaries has not changed since 1953, and only in 1969 was an adjustment of about 10 percent voted by the government to lessen the expected effects of the devaluation on the cost of living. Still, salaries are much too low to attract qualified people into the civil service. (Salaries paid by private enterprises are approximately three times those paid by the government.)

286. Expenditures for general administration have expanded at less than 3 percent a year. This appears offhand to be surprisingly slow. It is difficult to judge, however, whether or not general administration was overbuilt in earlier years. In 1968 it absorbed two and a half times the amount allocated to economic services. The relationships between the needs of these two types of services would require a thorough study to determine their requirements of future expansion.

287. The basic policy of eliminating the current deficit by keeping the expansion of current outlays at a rate persistently lower than revenues has been a sound one and reflects well on Cambodia's overall financial management, quite irrespective of priorities. It so happened that the cautious financial approach was reinforced at a time when the economy was slowing down, and in theory a more expansionist policy would have appeared appropriate. For two reasons, such an argument loses much of its validity, however. The first is that the cause of the economic slowdown had much

1/ Sectoral breakdown of public investment is available only from 1962 to 1966 (see table 5.5).

2/ The total number of civilian employees of the government at present is about 55,000 of which 43,000 permanently employed civil servants, including nearly 30,000 teachers. The armed forces are believed to be about 35,000 strong.

more to do with institutional changes and the deliberate action against the private sector, than with changes in aggregate demand, and with the decline in business confidence an expansionist income policy might well have failed to achieve its purpose. The second is that reliable statistical information on investment and savings, as well as on changes in the monetary situation, was so lacking that intelligent conclusions could not be drawn on the amount of permissible deficit financing, and a cautious policy was thus pursued with some justification.

288. Developments in 1969 have again tended toward the creation of a small current deficit which is presently estimated at about CR 100 million for the consolidated public finance sector. Revenues have probably increased by about 5 percent but the principal cause for this increase is the CR 400 million contribution from the Casino which will probably be eliminated in 1970. Current expenditures, if the supplementary budget is included, will have increased by CR 914 million or over 12 percent. Over a third of the increase was again for the social sector, and nearly a third for defense. An amount of CR 155 million was for salary increases following the devaluation.

289. For future years the prospect is for an increase in the current deficit to anywhere near CR 500 million if no effort is made to generate additional revenues. The proceeds of import surcharges will decline quite sharply already in the latter part of 1969, and this is unlikely to be compensated by increases in non-tax revenue, e.g. in dividend receipts. Current expenditures will have to increase faster in the years ahead for economic services, and probably also the general administration, but an effort will have to be made to restrain what is generally referred to as the "explosion scolaire".

290. One way of increasing revenues would be to improve the efficiency of the tax system by simply abolishing or unifying a number of small taxes into a single one, enabling the administration more efficiently to combat tax evasion. One measure that would certainly deserve consideration is to give more tax autonomy to the Local Entities to reduce their dependence on contributions from the National Budget. Local taxes to finance local budgets are often more acceptable to the taxpayer because of the proximity of the benefits. Given the extreme complexity of the present fiscal system, it is difficult to evaluate the effects of any single change on total revenue collection, unless a survey of existing taxation is carried out. Such a survey will sooner or later have to be undertaken, and the sooner it will be the better.

D. Capital Outlays and Financing

291. During the last 8 years including 1969 for which estimates have been made, government investments averaged about CR 1,150 million a year, without any significant trend except a 50 percent decline from 1963 to 1965. If investments by public enterprises of about CR 170 million per annum as well as non-monetary investment were included, total fixed capital formation in the public sector would on average have amounted to about CR 1,440 million a year. This is also just the amount spent in 1968, the first year of the Second Plan, against a target of CR 2,500 million for that year.

292. As to the direction of these capital outlays, data are available for the 5-year period 1962-1966 and they show that approximately 60 percent was spent for infrastructure (public works, power, transport), about 14 percent for the general administration, 7 percent for education and health, 5 percent for agriculture and 14 percent for industry (of which over four fifths by state and mixed enterprises). In 1967 industrial investment received a substantial boost because of the petroleum refinery (semi-public) but otherwise the trend in this field has rather been downward since 1966. Similarly, there is little indication of an increase in outlays on agriculture except for the starting of construction for the Prek Thnot project. While the announced intention of shifting the pattern of investment in favor of the productive sectors has much to be commended, its realization will take time. With the completion of the Sihanoukville-Phnom Penh railway, transport investment will inevitably be reduced in 1970, but the general point should be stressed that at the current level of public investment, the proportion spent on infrastructure does not, in absolute terms, represent an excessive amount, and high priority projects are available that would justify a continuation of past levels or even more, if only total resources could be sufficiently increased, and projects be advanced, to permit a more adequate effort to be made by the government also in such fields as agriculture. This, again, is not to say that the government should try to follow the Plan and spend 25 percent of total resources each on agriculture and industry. At the present stage of technical and administrative capabilities, such attempt could only result in substantial waste. The alternative between infrastructure and the productive sectors at this point of time in Cambodia is not a real one. Particularly as far as the choice, for example, between public investment in power facilities or manufacturing industry is concerned, the present situation in Phnom Penh is paradigmatic, where the failure of the public sector to provide adequate power facilities is hampering private industry (among other things) and this observation should not be used to argue in favor of more public industrial enterprises.

293. In general, and instead of setting percentage targets for sector allocations, it would be more to the point to say that there is no limit for the government to pursue administrative, institutional and technical improvements in all services having to do with agriculture, and to devote

maximum resources to the preparation of an agricultural development program. Only as a result of such preparation will it be economically possible gradually to speed up public investments in this sector in a significant way. In the meantime, Cambodia will still need substantial investments in its economic infrastructure, and as far as industry is concerned, policies conducive to greater private initiative and enterprise appear to command greater urgency at the present moment than the immediate execution, by the government, of new industrial projects whose economic feasibility remain uncertain or dubious.

294. Looking ahead, however, and in projecting present trends of government revenues and current expenditures into the future, the overriding problem looms in the form of a financial gap. Already in the past eight years, foreign aid on a net basis has financed 80 percent of government investments. It can be argued that three quarters of this aid has been in the form of military assistance, payments for expatriate teaching personnel and other non-investment expenditures, and that a good deal of these expenditures would simply not have been incurred in the absence of this aid, but the fact remains that public domestic savings have been persistently negative. The financing pattern for these years is shown below:

	F i n a n c i n g					
	Govt. Invest- ment /1	Current Surplus (+)	Foreign Grants (Current)	Foreign Grants/Loans (Capital)	Central Bank Credit (+)	Use of Assets (+)
1962	1,414	-815	1,269	204	+400	+356
1963	1,653	-475	1,248	257	-	+623
1964	1,399	-1,230	832	82	+600	+1,115
1965	857	-318	516	39	-230	+850
1966	1,155	-337	520	362	+660	-50
1967	780	-537	430	121	+10	+756
1968	1,240	+330	524	318	+120	-52
1969	<u>1,730</u> /2	<u>-107</u>	<u>400</u>	<u>300</u>	<u>+470</u>	<u>+667</u>
Total	10,228	-3,489	5,739	1,683	+2,030	+4,265

/1 Excluding non-monetary investment and investment by state enterprises.

/2 Including CR 400 million subscription to international organizations.

295. To make long-term forecasts of Cambodia's government revenues and current expenditures would be a difficult undertaking; all that one can say is that on the present tax base total revenues will probably not grow much faster than GDP at current prices - tax elasticity to GDP in the past has been very close to unity; while some taxes, e.g. the import surcharge, will decline after the devaluation, this may be slightly more than compensated by the increase in customs receipts on the enhanced CIF value of imports. As far as current expenditures are concerned, one may say that their growth

rate will be influenced by the need to improve the salaries of civil servants, and the growing recurrent changes on the economic services as a consequence of present and future investments. Even if the social sector expenditures are restrained and defense expenditures kept at a rate of less than 5 percent a year, the current deficit is likely to remain in the neighborhood of CR 300-500 million a year, unless significant new tax resources are found.

296. If capital outlays are to expand, as they should, to a level of at least CR 2.5 billion within three to four years, there will be an evident need for a larger volume of foreign official capital. Such a need will be reinforced by the realization that the past continuous reliance on central bank advances and drawdown of assets, including foreign reserves since 1967, to fill the budget deficit, has been reconciled with monetary stability by extraordinarily tight credit restraint for the private sector. A continuation of this approach is certainly not in the interest of economic development.

CHAPTER V

BALANCE OF PAYMENTS

A. The Foreign Trade Regime

297. Cambodia's exports have historically (date are available since 1952) been growing at only 3.5 percent a year. On the other hand, GDP grew 5.1 percent in real terms but services and industry, which have a higher import dependency than agriculture, have grown at 7.2 percent a year, compared with 2.7 percent for agriculture. These figures suggest that Cambodia's balance of payment has been in structural disequilibrium, resulting in constant pressure on the shadow rate of exchange, even without a rate of monetary inflation out of line with the rest of the world. As noted, monetary expansion has been very moderate and the changes in the price levels that did occur are indicative of increases in import prices rather than for domestic goods. As seen in appendix table 6.5 the consumer price index for the working class in Phnom Penh since 1956 rose 3.2 percent a year; for the middle class by 4.3 percent, and for foreign residents by 5.3 percent a year. For the rural population the change has probably been very small.

298. The parity of the Cambodian riel has not been changed until August 1969 when it was changed from 25.4 to 16 mg. of gold. Prior to the devaluation, a broken cross rate existed between the French Franc and all other currencies, the former being fixed at CR 10 (disregarding successive devaluations of the French Franc) and all others as the equivalent of CR 35 for US\$ 1. Since 1969 the rate is unified at CR 55.4/\$. The free rate for foreign exchange moved gradually upward in the early years, and reached a peak with the cessation of U.S. financial assistance when the U.S. dollar was sold at around CR 100 or three times the official rate. Since then it has come down under the combined influence of monetary restriction and, more recently, growing demand in limited markets for contraband activities.

299. Exchange control and quantitative import restrictions have been in force virtually since independence, and since 1963 foreign trade is nationalized and is carried out directly by the Societe Nationale d'Exportation et d'Importation (SONEXIM), newly created for this purpose.

300. The Foreign Exchange Office (Office National des Changes - ONC) was established in 1955 as an agency of the Banque Nationale du Cambodge to control all transactions in foreign exchange. Export proceeds had to be surrendered to the ONC at the official rate (CR 35/\$ and CR 10/FR.) with the exception of 10 or 13 percent, depending on the currency, of the officially computed value of exports. This percentage, plus the excess of export proceeds over the official value computed on the basis of government quoted export prices, was freely convertible in the "parallel market".

The freely convertible accounts were known as EFAC accounts ("Exportations - Frais Accessoires"). Finally, for exports to Bangkok, Hong Kong and Singapore, certain goods were freed from the requirement of exchange surrender altogether, and a declaration was sufficient. The proceeds of these exports were kept abroad and used for imports under what was called Exchange Compensation (Echanges compenses).!

301. Most imports were subject to licensing through the Ministry of Commerce and based on a foreign exchange budget, enabling importers to purchase foreign exchange from the ONC at the official rate. Two other types of imports were possible. First, by using free foreign exchange through EFAC, certain types of goods under an official list could be imported without license. Secondly, exporters of goods eligible for Exchange Compensation could also use their foreign exchange for imports without license. In fact, of course, the system of Exchange Compensation also gave rise to free buying and selling of foreign exchange but outside of Cambodia. These markets (EFAC "parallel" market, market abroad, as well as "black" market sustained by smuggling) were sufficiently permeable to cause all free foreign exchange to be transacted at more or less the same rate, so that imports were subject to one basic rate in addition to the free rate.

302. Merchandize exports and imports were conducted by a half-dozen large firms, mostly European, as well as a large number of small businesses, most of which were owned by Chinese. With the creation of SONEXIM in 1963, foreign trade was nationalized and all imports conducted through the new state corporation, with the exception of a relatively small amount under the regime, not mentioned before, of "imports without foreign exchange" ("sans devises"). This was meant originally to be for personal imports by non-residents, but later came to include a certain number of other imports, including automobiles and machinery which were probably illegal (if financed with foreign exchange purchased in the parallel market) but tolerated. With all other imports being conducted, in form, by SONEXIM, the EFAC accounts were abolished (along with the Echanges Compenses which however were later revived) since the overvaluation of the currency could now be dealt with directly by SONEXIM, and there was no need any more to offer a specific blend of par rate and free rate foreign exchange to private exporters. The new device took the form of graduated surcharges on imports, levied through SONEXIM into a special fund (Caisse de Compensation) which was used, again through SONEXIM, to subsidize exports. SONEXIM was thus enabled to procure commodities for exports (mainly rice, rubber and maize) at prices substantially higher than the official par equivalent of world market prices. Depending on the yield of the import surcharges and the degree of subsidizing exports decided each year, the Caisse de Compensation either was in deficit (1964 and 1965) or produced a surplus from which transfer payments were made to the Treasury. The transactions of the Caisse de Compensation are shown in Appendix Table 3.8.

303. The import surcharges are known under the name "taxes de péréquation" but the term applies both to import surcharges (péréquation positive) and export subsidies (péréquation negative). The former have been, and

are still applied to three different lists of goods with three different rates of surcharge, as shown below.

List	Exchange rate for US\$1		Import Surcharge 1/		Effective Rate for US\$1
	Old	New	Old	New	
A	35	55	45	25	80
B	35	55	40	20	75
C	35	55	35	15	70

1/ "Taux de compensation" or "peréquation".

304. It is to be noted that the guiding principle is the effective exchange rate to be achieved, and not an ad valorem tax on the CIF price, so that the 1969 devaluation affected the rates of surcharge and not the effective rate for these imports. Since the old parity with the French Franc was not changed (instead, the gold parity and the dollar rate were adjusted to the Franc rate of CR 10/Ff on the basis of the post-August 1969 gold parity of the Franc), the rates of surcharge on imports from the Franc zone remained unaltered and now correspond roughly to the new rates shown above.

305. These import surcharges were relatively high, but they are not by any means applied to all imports. In fact only about 25 percent of total import allocations to SONEXIM were goods under Lists A, B and C. The greater part of the balance was imported at the official rate without surcharge; these being "essential" imports. (In procedural jargon they are described as "importations finançables".) Another part (List D) is subject to an ad valorem surcharge, and finally, a large number of items are imported by SONEXIM on account of the final users, including industrial State enterprises, at the official rate but with a domestic price fixed by the government. Iron and steel products, cement, motors and certain textiles fall in this category.

306. Since some of these lists are partly overlapping as far as types of goods are concerned, this system is to a considerable extent subject to administrative decision, and consequently open to fraud. Also, substantial time is wasted on procedures. For example, a private industrial enterprise importing raw materials, machinery or spare parts needs a recommendation from the Ministry of Industries before being able to request a license from the Ministry of Commerce, which is then handled by SONEXIM for the purchase abroad, to be sold to the final user either at a price fixed by the government or after payment of duties, import surcharge and fixed ad valorem commercial margin due to SONEXIM, plus a turnover tax which is applied to all imports.

307. The sale price of an imported article, e.g. is composed of the following elements (plus freight, storage charges, interest on bank credit, and 3 percent stamp duty):

	<u>Riels</u>	<u>Riels</u>
CIF price \$1,000	35,000	
Import surcharge (List A)		45,000
Import duty on CIF (40%)	<u>14,000</u>	
	49,000	
Turnover tax (14%)	<u>6,720</u>	
	55,720	
Wholesale margin (20%)	<u>11,144</u>	
	66,864	<u>66,864</u>
Sale price		<u>111,864</u>

308. The rates used in this case are those applicable e.g. to a private automobile. Using the old exchange rate, the sale price turned out about 320% of the CIF price; with the new par rate, the import surcharge is less but all other charges increase correspondingly with the adjusted Riel CIF price, and the sale price is CR 130,336 or about 16 percent higher than before the devaluation. By contrast, of course, all imports not subject to surcharge became more expensive in the full amount of the devaluation or by 58 percent, with the exception of (a) imports from the Franc zone, and (b) imports with fixed domestic prices.

309. In the wake of the 1963 reforms, several public agencies were set up to work in association with SONEXIM in the field of import by purchasing goods from SONEXIM and distributing or retailing them. SONAPRIM (Societe Nationale des Produits Importes) used to be the most important, operating as a wholesale firm and handling such things as textiles, condensed milk and building materials. In recent years, MAGETAT operating both in wholesale and retail fields (with its own department store) has taken over much of textiles and condensed milk in addition to general food products and miscellaneous consumer goods. Other major customers of SONEXIM are OROC for goods imported for rural consumption, SONATRAC, SONAPNEU, as well as private industries, and finally, the government itself.

310. Neither SONEXIM nor the new public wholesaling agencies started off with much business competence; the fact that their commercial margins were officially fixed at very adequate levels (varying between 8% and 23% depending on the commodity) did not do much to promote their efficiency, or to avert the possibility of goods being imported far below requirements, or alternatively, far in excess of needs, with the result that commodities were not available in the official market, or differences arose between SONEXIM and SONAPRIM and others about paying the cost of keeping unsaleable inventories.

311. It is acknowledged by the government that the experience with SONEXIM has not been a happy one, particularly with regard to its importing function. Proposals have been advanced to reintroduce direct purchases abroad, by government agencies and state enterprises, of raw materials and equipment used by themselves, on the grounds that they would be better equipped to select among offers from foreign bidders the type of equipment best suited for their purposes. As far as private industrial as well as commercial imports for general consumption are concerned, it is recognized that in most cases bidding documents have continued to be prepared, and orders were placed, by the industrial users or private wholesalers themselves, so that the function of SONEXIM was limited to that of an unnecessary intermediary - the Ministry of Commerce continuing to issue import licenses and ONC to grant foreign exchange permits.

312. In the field of exports, the picture is less clear. As discussed further below, exports mainly of rice have substantially increased after the creation of SONEXIM, and in spite of what can be said about other contributory factors, it is felt by the government that for Cambodia's two largest export items SONEXIM has performed a useful function. Also, it cannot be denied that a state trading corporation has certain advantages in conducting trade with Eastern bloc countries. The argument most frequently used is that without SONEXIM, agricultural producers would be exposed to the sharp changes in world market prices (both rubber and rice) with undesirable consequences on production.

313. For a variety of minor exports, SONEXIM has been a conspicuous failure. Firstly, it did not have the necessary knowledge of the markets, which were scattered in the region and for which the personal contacts of the traditional Chinese merchants were indispensable. Secondly, SONEXIM's price policy in procurement was inept and purchasing agents failed to locate the goods, partly for similar reasons. As a consequence, the system of Exchange Compensation was reintroduced in 1967 (exemption from exchange surrender requirement) and for all practical purposes these exports today are private exports except for SONEXIM's rubber stamp.

B. Exports

314. Exports are about 10 percent of GNP at factor cost. During the 16 years between 1952 (prior to independence) and 1968, the total value of exports increased from CR 1,778 million to CR 3,098 million at an average rate of 3.5 percent a year. This growth rate is less than that of GDP but higher than agricultural growth in the same period - and virtually all exports are agricultural products. However, with the sole exception of rubber, half of this growth rate is due to increases in world market prices, particularly as regards rice. Over the whole period, the principal exports showed an average annual growth rate, expressed in volume, of 1.7 percent for rice, 1.6 percent for maize, and 7.0 percent for rubber. Again,

these figures do not convey the complete picture because there had been a temporary boost, in the early sixties, in the case of rice, maize, and livestock, which has been followed by an absolute decline since about 1964. Data on exports in volume and in value are shown in appendix table 3.3.

315. Rice has always been the most important earner of foreign exchange, accounting for about a third in the later fifties, about 60 percent in 1964, and about 40 percent in recent years. Again there is a problem in interpreting the available figures because of changes, during the period, of exchange regulations and therefore of prices recorded by the customs. The pricing of rice exports has in fact been one of the major issues that led to the reform of 1963. Prior to that date, exports were conducted by private merchants who were entitled to retain foreign exchange earned above a government posted export price (as well as 13 percent of the posted price) and this foreign exchange was worth twice the official rate at which the remainder had to be surrendered. It is interesting to compare the export price implied in Cambodia's customs records (equivalent to the government posted price) shown below as (a), with the world price quoted in Bangkok (B).

Export Prices Of Rice
(US \$ per ton)

	<u>1957</u>	<u>1958</u>	<u>1959</u>	<u>1960</u>	<u>1961</u>	<u>1962</u>	<u>1963</u>	<u>1964</u>	<u>1965</u>	<u>1966</u>	<u>1967</u>	<u>1968</u>
(A)	89	95	105	64	87	98	115	116	110	135	178	183
(B)	112	136	112	103	111	128	119	114	112	130	154	175

316. It appears that Cambodia's prices were consistently below world prices by a substantial margin up to 1963 when SONEXIM took over exports and the system of posted prices was abolished. The resulting upward change in official exchange earnings is often quoted as proof of SONEXIM's success in rice exports and this point is seemingly reinforced by the substantial increase in volume from an average of about 250,000 tons per year prior to the reform to over 450,000 tons in 1964 as well as 1965. The latter, however, is a result of two very favorable crops - yields in these two years were about 15 percent higher than before or after. It is clear that the introduction of SONEXIM did increase official exchange earnings per unit of exports, but it did not increase Cambodia's import capacity, since under the previous system the method of recording did not reveal all of the country's export proceeds, as posted prices evidently were influenced downward by subtle means on the part of exporters. It can be argued that the present system, even if it does not in itself increase export earnings, nevertheless prevents capital flight through under-invoicing of rice. This is no doubt true, to judge from the above price comparisons, but it would be a gross mistake to assume that it prevents capital flight per se.

Total Recorded Exports
(CR million)

	<u>1955</u>	<u>1960</u>	<u>1965</u>	<u>1968</u>
Rice	79	727	1,817	1,249
Rubber	628	978	961	657
Rice flour	35	84	118	56
Maize	151	289	178	156
Cattle	29	61	25	110
Timber	43	58	49	84
Other	<u>437</u>	<u>244</u>	<u>542</u>	<u>786</u>
Total	1,402	2,441	3,690	3,098

317. Since 1965 Cambodia's export earnings had been stagnant or declining. In the case of rubber, up to 1968 this is of course due to the decline in world prices, and in 1969 a further decline in earnings, in spite of improved prices, is caused by a decline in production following defoliation of rubber plantations by U.S. forces. In the case of rice, world market prices have been at a record level in 1968, and the decline from the 1965 level reflects a decline in yields of production. This problem has been discussed elsewhere in this report. As regards maize, it is difficult to explain the declining trend if not by the inefficiency of the existing export regime and the lack of incentives. Area planted with red maize (the exported variety) declined from 117,000 hectares in 1965 to 85,000 hectares in 1969. A substantial promotional effort would appear warranted for this crop, including the introduction of non-traditional varieties.

318. Reportedly, there has been a significant increase in smuggling to Viet Nam (which goes both ways but there is probably a considerable surplus in the balance of illicit trade). Contraband exports to Viet Nam are mainly rice, beef on the hood, and vegetables, but also some fruit, and cigarettes. It may be assumed that with peace being established in Viet Nam such exports might become legalized. It is not likely, however, that Viet Nam would offer a growing future market from Cambodia exports. Particularly for rice, vegetables and fruit, present demand is clearly caused by the war and will again disappear in due course. Possibilities might exist for beef. On the other hand, rice presently supplied on clandestine channels to Viet Nam might become available for export to other markets.

319. The present "trade surplus" in illegal transactions with Viet Nam appears to give rise to a peculiar problem of monetary policy. Part of the net earnings no doubt find their way to Hong Kong and Singapore dollar accounts abroad. However, payments by Viet Cong and North Vietnamese troops for Cambodian rice and other products seem to be effected with Cambodian currency, which is thus extracted from domestic circulation and increases the supply of foreign exchange in the domestic free market.

(The free market rate of the Cambodian riel has strengthened considerably in past years from near CR 100/\$ in the early sixties to below CR 60 at present.). Large working balances in Riel notes may have been built up outside the country, as well as rural hoards in the supplying areas of Cambodia. Fears are entertained that peace in Viet Nam might release a large amount of currency, thus held, into domestic circulation, and this is a factor in the reluctance, on the part of the Central Bank, to relax its very restrictive credit policy.

320. The outlook for exports for the immediate years ahead is not very favorable. Rubber may recover from the low 1969 level if no more defoliation takes place. In the case of rice, present price prospects are not particularly encouraging; nor are there clear indications that production will grow at a pace faster than domestic consumption. Much will depend for other exports on the type of export regime that the government may ultimately adopt, but even with optimal incentives it will take time for maize, pepper, beans and miscellaneous agricultural products to respond with increasing supplies.

321. In the longer term Cambodia still has significant potential for expanding present agricultural export crops as well as producing new ones. Also, processing of such products for export is a field where a beginning has hardly been made. Cases in point are maize, copra, tobacco, cigarettes, canned fruit and juices, processed vegetables, groundnuts, edible oils, starch, and canned or frozen meat as well as shrimp. Also, with the large forest resources and the growing rubber replanting operations, there would seem to be a good case for producing pulp and paper for export, as well as for expansion of timber exports. For several of these products, proposals, to say nothing of their implementation, has been very slow. Two factors have been responsible for this. One is the ambivalence of government policies regarding private industry. The other factor, much more intractable, is the difficulty in approaching agricultural development in general. This applies to export crops as well as to locally consumed crops.

322. One hopeful element in the picture is tourism, which is given high priority by the government and where there is a possibility within the next five years for an increase in the accommodation of tourists, from the 1968 number of bednights in the order of 120,000 to nearly four times as many in 1975. This would result in net exchange earnings, at present about US\$ 2.3 million, to increase to perhaps US\$ 10 million or CR 550 million in 1975. This is about 13 percent of present export earnings after adjustment to the new exchange rate.

323. Trade agreements. Already since 1956 Cambodia has pursued a policy of promoting trade with bilateral trade and payments agreements, in particular with Eastern European countries and China, but also with Japan, Laos and Viet Nam (provisional revolutionary government). All of these agreements are based on the principle of trade equilibrium, and the

agreements as a rule consist in mutual pledges to facilitate mutual trade, with lists of goods to be traded in both directions attached, and in many cases with a total target value indicated. The agreements are normally for one year but have been regularly extended. Sixteen such agreements have so far been concluded, as listed below.

People's China	1956	(R 5 million)	Yugoslavia	1960	($\text{\$}$ 2 million)
Czechoslovakia	1956	(R 0.5 million)	Japan	1960	(-)
USSR	1957	(-)	U.A.R.	1960	(R 0.5 million)
Poland	1957	(R 0.7 million)	Bulgaria	1961	($\text{\$}$ 2 million)
North Viet Nam	1958	(R 1.5 million)	North Korea	1963	(R 0.5 million)
Laos	1959	(R 2 million)	Albania	1966	(-)
West Germany	1960	(-)	South Viet Nam	1969	(R 1 million)
East Germany	1960	(R 0.8 million)	Singapore	1969	(-)

324. Details on Cambodia's exports by destination and of imports by countries of origin are shown in appendix tables 3.4 and 3.6. Exports to Eastern bloc countries have increased from only CR 91 million in 1956 to over CR 600 million in 1968. (However, in 1953 they had amounted to CR 1,195 million.) The increase has been fairly steady and half of it today is accounted for by People's China.

325. Imports from Eastern bloc countries increased gradually from about CR 300 million in 1956 to a maximum of CR 1.2 billion in 1966, after which there was a decline to below CR 500 million in 1968. Throughout the period up to 1965 Cambodia's trade deficit with Eastern bloc countries fluctuated between CR 120 and 290 million but increased to over CR 700 million in 1966. Since then, there has been a small surplus.

326. In the case of Japan, the trade agreement does not seem to have produced any effect on exports which are still in the neighborhood of only CR 100 million. The same is not true for imports from Japan which were already CR 515 million in 1960 and remained at about that level until 1968 when they increased to over CR 800 million.

327. It is not all certain that bilateral trade agreements have helped Cambodia to increase her exports or to improve her balance of payments position. Most of her bilateral exports consist of products easily marketable elsewhere, and prices obtained from bilateral partners are often less favorable than in alternative markets. Cases are mentioned where Cambodian exports were resold by bilateral partners in world markets. At the same time, state export organization of Eastern countries are known not infrequently to charge to charge high prices for low quality. The Czech sugar refinery, obtained under a credit, is a case in point. However, information is not available to reach a conclusive judgment in this matter.

C. Imports

328. Statistics on imports have to be viewed with a good degree of caution, not only because their Riel values reflect different exchange rates depending on the origin of the goods (French franc zone) but even more importantly because it is not possible to say which product in which year was imported at the official (French or dollar) rate and which at the free rate, and therefore what real values are believed the Riel values given in the customs records. Furthermore, customs invoices do not necessarily reflect the real prices paid, and it would be difficult to say whether this margin of error is always positive or negative.

329. Taking account of this, one can nevertheless say that total imports of Cambodia between 1954 and 1968 have grown at about 5 percent a year, which is the same as GDP growth in real terms but less if the latter is taken at current prices. This growth rate was much faster up to 1963 although that was the period when exports hardly expanded at all, but it is explained by the inflow of foreign capital and the comparatively more rapid growth of the economy. From the 1963 level of imports of CR 3.7 billion, there has not been any upward trend since, except in 1968 when they reached CR 4 billion.

330. Commodity details on imports are available since 1962. Between that year and 1967 there has been a change in the composition as shown below, which is probably a continuation of earlier changes in the same direction.

Imports By Groups Of Commodities
(in percent)

	<u>1962</u>	<u>1967</u>
Food, beverages, etc.	11.3	7.2
Pharmaceuticals	5.8	7.3
Textiles	11.4	7.9
Machinery, equipment and vehicles	31.3	34.7
Iron and steel	9.2	6.8
Cement	5.1	3.2
Fuels and minerals	6.2	10.2
Other	<u>19.7</u>	<u>22.7</u>
	<u>100.0</u>	<u>100.0</u>
Total Value (CR million)	<u>3,584</u>	<u>3,365</u>

331. First, as consequence of new industries going into production, there has been a degree of import substitution in foods and beverages, as well as in textiles, particularly for cotton cloth but also, starting in 1967, for gunny bags. Obversely, the establishment of new industries is reflected in the relative increase in imports of machinery and equipment. The relative decline in cement may be a reflection also of import substitution, but what is more relevant is that there has been a slump in private construction from which the recovery is still slight. These observations ought to be qualified to the effect that both total imports and their composition have been subject to erratic movements. About the only component with a more or less stable growth trend has been petroleum products, reflecting the growth of road transport.

332. It is only within limits that the causes for the stagnation of imports since 1963 can be looked for in the conditions of the economy, because import control is comprehensive (notwithstanding evasion, smuggling, etc) and laws of the market are operative only by default of the regulating authorities. Price statistics for imported goods are not available. The impression cannot be escaped, however, that import demand has in fact slowed up along with the economy, and may even have declined as a consequence of the setting up of SONEXIM with the attendant price increases (additional wholesale margins, imposition of import surcharges) and the interposition of procedural complexities. If this were not enough, the deflationary policy of the Central Bank helped to further dampen demand. Finally, the devaluation of the Riel in 1969 will probably increase import prices sufficiently to end what might have been a revival of imports starting on a modest scale in 1968. It is fair to say that 1969 was a difficult year for the balance of payments because of the decline in rice production and exports in that year, and foreign exchange reserves were drawn down to avoid a reduction in essential imports.

333. The future development of imports is very uncertain, depending on the timing as well as the nature of the proposed liberalization policy and the future function, if any, of SONEXIM in the field of imports. Further, the question is open as to whether the government will attempt to revive economic activity through changes in its policy vis-a-vis the private sector, and whether such policy will be supported by an appropriate revision of present monetary and credit policies. For the long run there can hardly be any doubt that the structure of Cambodia's economy will require a higher level of imports than at present, if a satisfactory rate of growth for the economy is to be achieved. The ratio of imports to GDP, which was in the order of 14-15 percent in 1962 and 1963, has since declined to around 11 percent. This decline is of course directly related to the decline in foreign aid.

D. Balance of Payments Outlook

General

334. The balance of payments is largely determined by merchandise trade, and other items on current account are relatively small. Total gross service payments have usually been about one-sixth of merchandise imports. Large changes in the balance of trade, e.g. due to good or bad rice crops, are directly translated into changes of exchange reserves. For example, when rice exports declined in 1966 by more than half or CR 1 billion, exchange reserves which had increased about CR 400 million in 1965 declined by CR 330 million in 1966. Again, it has to be noted that balance of payments data produced by the National Exchange Office have to be used with some reservation, through perhaps not as much as those of the Customs.^{1/} A summary of the balance of payments for the years 1963-68 is shown below:

<u>Balance Of Payments Summary</u>						
<u>(CR million)</u>						
	<u>1963</u>	<u>1964</u>	<u>1965</u>	<u>1966</u>	<u>1967</u>	<u>1968</u>
Exports	3,080	3,340	3,461	2,478	3,076	3,037
Imports	3,496	3,969	3,573	3,881	3,224	3,416
Trade balance	-417	-630	-112	-1,404	-148	-378
Services, net	-214	-261	-120	143	59	- 90
Current account balance	-631	-890	-232	-1,261	- 89	-468
Private capital	1	-9	115	2	35	13
Official capital	671	755	517	925	82	326
Reserves/clearing accounts	-41	144	-400	334	- 29	130

335. Imports and exports have already been discussed; as for services, the largest item is maritime shipping for which in the last 3 years average expenditures were between CR 200 and 250 million or about 7 percent of FOB imports. Expenditures for insurance are very small. Tourism with CR 75 million gross earnings in 1968 was still small. Interest and dividend payments, in the order of CR 100-150 million, have not been growing since 1965, and they were approximately balanced by receipts (on BNC foreign assets and probably dividends from the Societe Financiere du Cambodge, a Paris based company owned by the BNC, on which no information is available). Remittance payments have also been roughly in balance with receipts. Remittances

^{1/} There are large differences between trade data in the balance of payments (appendix table 3.1 and customs data on imports and exports (tables 3.3 and 3.5). For example, imports in 1964 according to customs were CR 2,863 million but according to the balance of payments they amounted to CR 3,969 million. A discrepancy of this magnitude can only be explained by gross destruction of customs records. SONEXIM in that year had just taken over foreign trade from the private sector.

abroad by local Chinese are seemingly small, within total remittances of CR 100 to 200 million a year. What is often referred to as large transfers of profits abroad by the Chinese, if it does take place, is not evident in the balance of payments as prepared by the Exchange Office (Appendix table 3.2). The amount under errors and omissions is not larger than rounding errors.

336. On the capital account, private foreign capital amounts to very little. Official capital inflow has come down from an average of CR 1.2 billion per annum in the previous five years to about CR 550 million ^{1/} per annum in the period shown above. A major part of this is grant aid from France (military and technical assistance, and provision of teaching personnel), from the USSR (Hospital, Technical Institute) and China. Foreign loans at present still in disbursement are negligible.

Projections

337. Any attempt at forecasting the balance of payments has to be based mainly on trade assumptions. In the case of exports, the outlook, as already discussed, is not very bright, given the recent declining trend for rice (although the current campaign is expected to produce a very good crop for export in 1970, due to favorable weather). In the case of rubber, a considerable number of young trees have been put into tapping in recent years and their yield should increase rapidly. On the other hand, substantial losses have been incurred through defoliation in 1969, and from the damage claims put forward the loss could be very substantial. For other exports, much will depend on whether the private sector is again authorized to export directly. It seems, therefore, that a 4 percent annual growth of export earnings from the 1968 level would be an optimistic assumption, and even under most favorable circumstances would be difficult to achieve for the years immediately ahead.

338. In the case of imports, the only useful assumption is that the government will take some action to reactivate the economy. Cambodia has potential for an economic growth rate well in excess of 5 percent, as demonstrated by the performance in the latter half of the fifties. Since then, a prime constraint for growth has been Cambodia's limited import capacity, although superimposed on this, there have been various other factors as well. It is clear that with total imports stagnating or even declining through the last 5 or 6 years, the ability of newly established enterprises to operate efficiently, or of established enterprises to reach optimum capacity utilization, has been hampered, and economic incentives for investment in productive assets were diminished to a low point.

^{1/} Balance of payments data on foreign aid are incomplete. For the period 1963-1968, data from the Ministry of Finance give a cumulative amount of CR 5,259 million, compared with the CR 3,276 million in the table above.

339. Given the prospects for exports, there is no choice for the government but to rely on increased foreign assistance, and the decision by the Chief of State to terminate the period of do-it-alone has been a timely one. There is no way of calculating the future requirements of capital inflow with any precision, but an illustrative projection of the balance of payments for 1973, on the basis of 3 successive five-year periods is shown below. The suggested growth rate of imports has been chosen after considering (a) that there is a backlog of requirements, (b) that imports need to grow faster than total GDP and at least in line with non-agricultural GDP which has been growing on average at over 7 percent a year in real terms over the last 17 years, but could grow faster than that, and on the other hand, (c) that aid from new sources, even in most favorable circumstances will take time for being actually disbursed, and that in the first few years the possibilities for relaxing import restrictions will be limited. In fact, the devaluation of 1969 will act as a further brake, and it has been earlier suggested that a relaxation of credit restrictions will be necessary if only to avoid a temporary slump in import demand. Balancing these considerations against each other, a 7 percent growth rate for imports appears a reasonable proposition. (It should again be noted that import data are different depending on the source; the figures used below for past years, while consistent with the balance of payments, are probably on the low side.)

Illustrative Balance Of Payments Projection
(US\$ million)

	<u>1958</u>	<u>Annual Increase</u> %	<u>1963</u>	<u>Annual Increase</u> %	<u>1968</u>	<u>Annual Increase</u> %	<u>1973</u>
Merchandise							
Exports	53.3	10.5	88.0	-0.3	86.8	4.0	106.0
Imports	<u>70.5</u>	7.3	<u>99.9</u>	-0.7	<u>97.6</u>	7.0	<u>136.6</u>
Balance	-17.2		-11.9		-10.8		-30.6
Tourism, net	0.1		1.0		2.1		7.5
Other services, net	<u>- 4.6</u>		<u>- 7.1</u>		<u>- 4.7</u>		<u>- 8.6</u>
Total goods/services	-21.7		-18.0		-13.4		-31.7
Private capital	- 1.6		0.1		0.4		1.0
Official capital	37.8		19.2		9.3		30.7
Monetary movements	-14.5		- 1.3		3.7		-

340. The resulting requirement for official capital in 1973 in the order of US\$ 30 million is still less than what was available in 1958 and, indeed, up to 1960, but the figure might be a reasonable average for the 1970-1975 period assuming it were on an ascending scale. The financing of the Prek Thnot project would be in addition to these projections. (Furthermore, the capital requirement would be higher to the extent that import projections are too low, as suggested at the end of paragraph 339.)

341. It may be assumed that grant aid from traditional sources for current expenditures in the fields of defense and education will continue to be available. Furthermore, a French credit offer for Fr. 125 million (US\$ 23 million) will shortly be negotiated for the financing of investment projects, and there are indications that other bilateral credit will be available. Between one-half and two-thirds of the balance of payments gap for the five coming years might thus be covered by having recourse to bilateral sources of credits and grants - provided that the rate of bilateral loan commitments can be stepped up from the present level.

342. While at present there are very few projects for which adequate studies have been completed, there is a considerable number of projects which appear prima facie well justified and for which preparatory studies are under way or should be taken in hand as soon as possible. Projects for agriculture and irrigation have been mentioned in Chapter II. In the field of power, transport, and tourism, available details are outlined in Part II of this report. A considerable amount of additional technical assistance will inevitably be required to bring an adequate number of new projects to fruition, but given that such assistance is forthcoming, the chances are good that a portfolio of projects will, over the years, be built up to match the volume of capital inflow as suggested above.

E. Terms of Aid

343. Cambodia's present external public debt is quite small, and is carried on relatively favorable terms. Total debt as of December 31, 1969 is US\$ 49 million, of which about half is due to France. Debt service payments in 1970 are US\$ 6.9 million, equivalent to about 8 percent of export earnings. Service payments on existing debt will gradually decline to US\$ 1.6 million in 1980.

344. Gold and foreign exchange reserves are still rather comfortable even though they have declined somewhat during the last three years, particularly in 1969. By the end of October 1969 they were still equivalent to US\$ 66 million (see appendix table 3.9 and covered about 8 months' merchandize imports.

345. Under these circumstances, there is certainly room for servicing additional debt on conventional terms. If it is assumed that Cambodia will continue to receive grant assistance for a third of the projected external gap of US\$ 30 million a year, half of the balance or about US\$ 10 million could safely be contracted from bilateral and other sources at more or less conventional terms. This is to say, if such terms were e.g. 6 percent interest and 12 years including 2 years of grace, existing plus new debt service obligations would reach about US\$ 13 million in 1980, which would be about 10 percent of exports, assuming exports to grow at 4 percent per annum. Such a ratio would certainly still be acceptable.

346. For several reasons, it would not be prudent to suggest a larger volume of hard-term borrowing. Firstly, it has to be remembered that a 4 percent export growth rate will be difficult to achieve. Furthermore, the average interest rate assumed above may be too low, considering the likelihood of a greater proportion of western-type suppliers credits than in the past. And thirdly, it is by no means assured that grant aid will continue to be available on the scale implied above.

347. On balance it follows that about half of the borrowing requirement, or perhaps \$10 million a year, should if possible be met on concessional terms. Since these figures are projected in balance of payments terms, the rate of commitment for project aid would have to be significantly higher, particularly since this type of assistance is starting from current disbursements of almost zero. Whether in fact a higher commitment rate can be achieved in the years immediately ahead will, of course, depend on whether a sufficient number of projects will be available, and this is by no means certain.

