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Cambodia's Private Sector: Its Engine of Growth

A new World Bank study - Toward a Private Sector Development Strategy for Cambodia - is nearing completion. For this issue the World Bank newsletter had the opportunity to interview Magdi M. Amin of the World Bank's headquarters in Washington DC, who is Task Team Leader for the study.

Q - You are working on a study called "Toward a Private Sector Development Strategy for Cambodia: Investment Climate Assessment. What is the main purpose of this study? What do you hope to achieve by doing this study?"

A: Thank you very much for focusing on private sector development. About two years ago, during a Consultative Group meeting co-chaired by the World Bank and the Government of Cambodia, there was a mutual recognition between donors and the Government of the need to shift the focus of our effort from rehabilitation to sustainable development and growth. It is well understood that the private sector is the engine of growth and employment creation, and it is one of the main pillars of

the National Poverty Reduction Strategy and the evolving World Bank Country Assistance Strategy. So what we would like to do is to help both the private sector and Government identify ways first, to con-

tribute to growth; second, to broaden the base of economic opportunity, ie to increase the range of sectors and activities that are able to hire and pay good wages;

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PHOTO: CHHOY PISEI

Garment workers sewing in one of Cambodia's many clothing factories.

"This is Cambodia", country I've reclaimed as my homeland

Mittpheap You is a Junior Professional Associate, working in the External Affairs Unit in World Bank headquarter in Washington DC. She recently returned to Cambodia after leaving in 1979 and contributes her account of her journey back.



Mittpheap and her father at Angkor.

My eyes swelled with tears when the plane touched the runway of Phnom Penh International Airport. All I could see from the airplane window were the lazy palm trees and the barren rice paddies.

It had been 25 years since I left Cambodia. My only previous memory of the country was a blur. I was only four years old when my family escaped the civil war in 1979. I can still recall sitting on my dad's shoulder and holding tight as he ran away from bombs in the distance.

My father and his friend named me Mittpheap (Friendship) at a refugee camp on the Thai/Cambodia border while he prepared the necessary papers to live in United State of America.

In the United States, to support a family of six my father worked as a cab driver and my mother as a housekeeper. Through these jobs they sent their four children to college, two to graduate school.

At home, my parents taught me the Khmer language and traditional Cambodian values. As a girl I had to learn how to cook and clean, and was not allowed to have boyfriends, or attend after-school activities. I had to come home each day after school and study, study, study. Education was the most important aspect in our family.

During my visit to Cambodia my par-

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and third, to enhance the private sector's role in delivering public services like infrastructure. So, it's important to understand in great detail why the private sector isn't contributing as much as it could in these three areas – to identify the specific constraints, and how the enabling environment compares with other countries that compete with Cambodia.

We are fortunate to have a strong team who have done innovative work on value chains and on trade facilitation. As a team, we would like to achieve two things. First, we would like to improve the quality of the dialogue around the private sector issues by contributing to the fact base. Often, in the past, little progress could be made on removing constraints for private sector development because people

has been rapid in only two areas – garment and tourism. In total, the formal manufacturing sector employs less than 9% of the work force. Cambodia's successful entry into the WTO creates opportunities for growth and job creation by opening up new markets on favorable terms. The ASEAN-China Early Harvest program, for example, provides an opportunity to sell nearly 300 product categories tariff-free to China. But to convert these market opportunities into jobs, the private sector needs the confidence to invest and a business environment that allows them to grow. This study, along with the Value Chain analysis we supported last year, will hopefully help point to a reform path that will allow the average Cambodian firm – most of which are small and related to agriculture – to participate.

tative sample of the Cambodian economy and the basis to compare with others.

Q – How important is the role that the private sector does and can play in Cambodia's development?

A: The private sector is absolutely critical in development, because the private sector can create jobs that pay high enough wages to reduce poverty on a sustainable basis. We have observed that those families headed by someone with a job in industry had a very low incidence of poverty – only around 4%. For those families still employed in the agriculture sector the poverty rate is still very high, around 80 percent. So we know that good quality jobs in the private sector, and manufacturing in particular, can play a huge role to move people out of poverty. Over the past decade growth has been strong. The garment sector has grown from around \$20 million in exports to over \$1.4 billion. But other sectors have not done so well, and so the benefits are not yet broadly based. The other role is delivery of services like electricity, water, health-care education. The private sector provides many of these services, but this role can be improved. We've found that in most cases the private sector has not been engaged through competitive processes, so the key benefit of the private sector – its efficiency – has been lost. So there are many positive things to point to about the private sector, but clearly the best days have yet to come.

Q – What are some of the main messages of the study? Do you think people in Cambodia will be receptive and open to these messages?

A: Among the key measures we look at for Cambodia are total factor productivity and labor productivity. Labor productivity, or high value added per worker, is what allows wages to be high. In order to move as many people out of poverty as possible, we need to help the government identify ways to increase the value added. We found that in Cambodia the value added is very low, much lower than China, and also lower than countries like Bangladesh and Pakistan. The paper explores why labor productivity is low, and some of the main issues are corruption; crime, theft, disorder; anti-competitive or informal practices by other companies that may gain an unfair advantage by not paying taxes. There are too many inspections, licensing requirements, and steps re-

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PHOTO: TANG CHHIN SOTHY

A worker busy at his machine in a small private enterprise in Phnom Penh.

would disagree, deny or blame others. The Government blamed the private sector and the private sector blamed the Government. Progress couldn't be made because it wasn't a factual discussion. We need the fact base to contribute to the quality and honesty of the dialogue. Two, we would like to help the Government develop its reform program – to examine the questions and help prioritize what are the most important reforms that can increase productivity, broaden opportunities, and strengthen the role of the private sector from a service delivery standpoint.

Q – Why do you think this study on the private sector is needed in Cambodia?

A: The Government requested this work because of its focus on reducing poverty, which requires growth. Growth

Investment climate assessments are an increasingly useful tool for the World Bank. Our former Chief Economist, Nick Stern, visited Cambodia last year, and raised the question of the investment climate with the authorities. This year the World Development Report will focus on investment climate issues. Our methodology is based on a firm-level survey (the Productivity and Investment Climate Survey) that includes a core set of questions that are common in every country. In Cambodia we asked an experienced firm to first survey 500 firms in the five largest cities, then 200 rural firms and 100 in the informal sector. Industries covered under the survey include garment, agro-industry, water providers, construction, retail and electricity providers. So we have a represen-

quired to trade products.

The survey also resulted in estimates of the share of firms that pay bribes and found that the level of unofficial, registering businesses is a key impediment. These unofficial costs are mostly associated with exporting and importing, registration businesses, getting construction permits, registering land and inspections of all types. Firms react to all of these costs by staying in the informal sector. The informal firms are less constrained by problems faced by formal firms like corruption and excessive inspections, licensing, and registration. But you can't raise the value added on the basis of the informal sector.

There are two more messages I would like to highlight.

The first is on broadening and diversifying the economy. From a cost standpoint, it looks like Cambodia has a comparative advantage in agro-industry. But agro-industry is constrained by a lack of market-supporting institutions to support trade – in addition to the high cost of doing business. There are insufficient linkages between buyers and sellers, and no institutions that would enable a rural agribusiness to find trade partners, to prove the quality of their products, to price their products competitively, or to resolve disputes that may arise.

The second message to come out from this relates to the participation of private sector in infrastructure. Many large deals lack transparency and competition because of the unclear legal environment, institutional overlap and a large number of processes and approvals that often get ig-



The school construction workers, hired by the private sector, are building a new school in the remote areas at Preah Vihear province.

nored because of lack of clarity in the environment of contracting in private sector. Instead of using the legal environment, the people tend to find the loophole and work around it, or instead get a signature from high level authority to provide them some comfort. Around the world, when we see direct contracting without competition, we see high prices and low quality of services. Tax payers and service users are losing. So we think the government and the people can get more from private sector participation by improving the legal and regulatory environment for private participation.

Q – How has the government reacted to the study?

A: The Government's reaction has been productive. There is broad consensus among all concerned that the problems exist at some level and need to be addressed in a cross-ministerial forum. The Government is preparing to take action. First, the Government arranged a high-level meeting between the Bank team and nearly all Ministries to discuss the report. Second, the Prime Minister issued a Decision of the Royal Cambodia Government on March 22nd that establishes a Interministerial Working Group for Improving the Investment Climate and Trade Facilitation. This Working Group has the task of proposing immediate measures to reduce trade facilitation costs, reduce duplication and simplify the process, reduce the time required, and increase official Government revenue. We will meet again in sixty days to listen to what this Working Group has proposed, and hopefully incorporate the measures into a revised chapter on reforms.

Q – Are you planning on discussing it with others, such as the private sector, donors, etc?

A: We have consulted extensively at each stage with the private sector and donors and once the reports are finalized,

they will be shared even more widely. The World Bank and Asian Development Bank co-chair a donor working group of donors with programs of support in private sector development and trade. During a recent informal meeting of those donors, several expressed support for the directions outlined in the report and would like to see the recommendations incorporated into a shared donor program of assistance. This would allow much more efficient coordination of donor effort in support of the implementation of the Government's reform program.

Q – What will yo do next?

A: Now we have two studies in our contribution to the Government's Private Sector Development Strategy: Value Chain Analyses and Investment Climate Assessment. The third part will look at private sector participation in infrastructure. Those three reports will complete the analytical phase. Over the next six months, we would like to pull together the recent studies on the public sector, private sector, rural sector, legal and judicial reform, education and health, in order to provide an overarching Development Policy Review on the sources of future growth. But more importantly now we are beginning the implementation phase. We are prepared to support implementation of a credible program of reforms produced by the Interministerial Task Force on Investment Climate and Trade Facilitation. Other donors are also prepared to join us in a coordinated, integrated program. But, the ball is in the Government's court.

Let me close by saying that I've enjoyed this process tremendously, and am excited by the process of analysis and mutual learning with the Government and private sector. But today, we believe it is time to focus on implementation and results.



A boy offers his goods in Phnom Penh after school hours.

LETTER FROM READER

Dear Sir:

I am a student at National Institute of Management and at the Institute of Foreign Languages, at the Royal University of Phnom Penh.

I have read most publications of the World Bank, especially its newsletters, in its library in Phnom Penh, and I am very interested in those publications. All those publications are very important for me,

students, and other people who want to enlarge their knowledge.

I would like to express my appreciation for your kindness and all the activities of the World Bank in sharing and providing information that is most valuable to the public.

Yours sincerely,

Yuk Sothirith

We Welcome Your Opinions and Comments

We welcome your opinions, comments and questions. Please send them to: Bou Saroeun, Communications Specialist, at 113 Norodom Blvd., Phnom Penh, email: sbou@worldbank.org. We very much appreciate your valuable assistance.

“This is Cambodia”, country I’ve reclaimed as my homeland

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ents were my tour guides. We would pass by monks in their vibrant orange robes, naked children swimming in the creek, 50 people piled in an Isuzu pickup truck, houses made of straw and mud, the faded glory of Angkor Wat and its surrounding temples, the prevalence of more mopeds than cars, a woman digging a ditch in her sarong and flip-flops, landmine victims at the Central Market, an eight-year-old child selling crackers at the beach, the resplendent palm trees and skinny cows grazing on dirt, the glass cases of skulls and bones at the genocide museum, a young Cambodian boy posing under a waterfall just for laughs.

I was getting to know the country through these moving images. As we passed these scenes my father would say “This is Cambodia”. It was as if by saying these three words would explain all of Cambodia’s beauty, darkness, humor, glory, and sadness.

I could see that Cambodia’s struggles lie in its past. During almost four years of Khmer Rouge regime, all the institutions of society (schools, hospitals, religion, libraries, museums, banks, newspapers) were destroyed. It is estimated that between 1 to 3 million people were killed; most were educated men and women: teachers, students, doctors, nurses, engineers, monks, artists, musicians, journalists, and bankers.

Now, after 29 years of civil war, Cambodia is still wrestling with its violent history as it tries to confront a tumultuous present. Many Cambodians are living on less than \$1.00 a day. I met my uncle for the first time in Takeo Province (45 minutes’ car ride from Phnom Penh). He lives in a hut that does not have electricity or running water. He has an outhouse for a bathroom. He works from 5am to 6pm bicycling over 100 kilometers to sell ice cream for less than \$2.00 a day. Though he is my father’s younger brother, the years of work have aged him faster than his time.



People piled into a pickup truck on a new road financed by the World Bank.

His daughter is 14 years old. She helps her mom make the ice cream, and the daily chores at home. School is an hour’s walk; she only attends when she has the time and energy.

Despite the problems, most Cambodians remain optimistic. Touring its cities and countryside, speaking my Khmer with an American accent, the consensus was that things are better than they used to be. People are able to travel to places that were once Khmer Rouge strongholds and there is a steady decrease of landmine victims.

While in Cambodia I visited the World Bank Cambodia country office and met Ms. Nil Vanna, a Social Development Specialist. She said she believes that after three decades of civil war, Cambodia is finally at peace. She believes that with peace comes stability and opportunities.

“We are able to pave roads to reach remote villages and provide them access to health care,” Ms. Vanna said. “Merchants are able to use these roads to sell goods. Children are able to attend school. Yes, Cambodia is behind, but it

is on the road to recovery. If we work together to fight against poverty and have continued support from the international community, I predict a positive future for my country.”

One of the greatest experiences in Cambodia was visiting the famed Angkor Wat. We woke up at 5:00 in the morning to see the sun rise over the temple. It was the most amazing sight I had ever seen, so magnificent, gracious and serene. It was like going back in time. Seeing Cambodia today, and looking over at Angkor’s glory, I wondered if Cambodia could ever rise and be that great again. I hope that it will.

Catching glimpses of the city, countryside, Angkor Wat, meeting my relatives for the first time, talking with people about their daily struggles and triumphs, gave me a sense of Cambodia’s bittersweet beauty; the timelessness of its culture, the repercussions of war and destruction, and the indestructible spirit of its people. Perhaps my father summed it up best when he said “This is Cambodia”, the country I’ve reclaimed as my homeland.