# CAMBODIA ECONOMIC UPDATE

## ROAD TO RECOVERY

## SPECIAL FOCUS
## GOVERNMENT-TO-PERSON (G2P) PAYMENTS FOR SOCIAL BENEFITS

**JUNE 2021**

WORLD BANK GROUP

# CAMBODIA ECONOMIC UPDATE

JUNE 2021

# ROAD TO RECOVERY

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# ACKNOWLEDGEMENTS

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# ABBREVIATIONS

| | |
|---|---|
| **ADB** | Asian Development Bank |
| **ASEAN** | Association of Southeast Asian Nations |
| **BRGS** | Business Recovery Guarantee Scheme |
| **CCFTA** | Cambodia-China Free Trade Agreement |
| **CEU** | Cambodia Economic Update |
| **CGCC** | Guarantee Corporation of Cambodia |
| **COVID-19** | coronavirus disease 2019 |
| **CR** | Cambodian riel |
| **CSS** | Cambodian Shared Switch |
| **DSA** | debt sustainability analysis |
| **EAP** | East Asia and Pacific region |
| **EBA** | Everything But Arms |
| **EC** | European Commission |
| **EU** | European Union |
| **FDI** | foreign direct investment |
| **FOB** | Free on Board |
| **FTA** | free trade agreement |
| **G2P** | government-to-person |
| **GDP** | gross domestic product |
| **GFT** | garment, footwear, travel |
| **GPPs** | Government Payment Programs |
| **GSP** | Generalized System of Preferences |
| **HFPSH** | High-Frequency Phone Survey of Households |
| **IDPoor** | identification of poor |
| **MDI** | Micro Deposit-taking Institution |
| **NBC** | National Bank of Cambodia |
| **NPIs** | nonpharmaceutical interventions |
| **NPL** | nonperforming loan |
| **NPS** | National Payments System |
| **P2G** | person-to-government |
| **PIMSRS** | Public Investment Management System Reform Strategy |
| **PSI** | Payment Service Institution |
| **RCEP** | Regional Comprehensive Economic Partnership |
| **RGC** | Royal Government of Cambodia |
| **RPS** | Retail Payments System |
| **SMEs** | small and medium-sized enterprises |
| **UK** | United Kingdom |
| **U.S.** | United States |
| **US$** | United States dollar |
| **y/y** | year-on-year |

# EXECUTIVE SUMMARY

## Recent developments

**After contracting by 3.1 percent in 2020, Cambodia's economy has gradually recovered.** The recovery is, however, uneven, partial, and volatile in part due to the re-introduction of a domestic lockdown, triggered by recent flare-ups of coronavirus infections. Like many countries in the region, Cambodia has been hit hard by global demand shock and coronavirus-related shutdowns which have had predictably uneven economic impacts across sectors. The agriculture sector has been relatively resilient in the face of the coronavirus shock. In addition, it has been boosted by increased investment, thanks to good prospects of the newly signed Cambodia-China Free Trade Agreement (CCFTA) and Regional Comprehensive Economic Partnership (RCEP). The manufacturing sector sharply contracted last year, but appears to have gradually recovered since, as it has adapted to changing external conditions. The easing of the traditional manufacturing industries, namely garment, footwear, and travel (GFT) goods has been partly offset by the expansion of the newly emerging manufacturing (electrical, electronic and vehicle parts including bicycles) and agroprocessing industries. Parts of the services sector such as accommodation, restaurants and transport continue to be hit hard by slowdown in domestic and international tourism, while wholesale and retail trade has managed to slowly recover, supported by a gradual revival in domestic economic activity.

**The government has the ability to provide further fiscal and monetary support as the pandemic intensifies.** In 2021, the budget for COVID-19-related relief and recovery intervention is US$719 million, compared to US$823 million in 2020. The central bank has extended its accommodative monetary policy. The National Bank of Cambodia decided in its Monetary Policy Committee meeting held in February 2021 to: (i) continue to maintain exchange rate stability via its exchange market intervention; (ii) provide riel liquidity via Liquidity-Providing Collateralized Operation facilities according to riel exchange rate and liquidity conditions; and (iii) maintain the reserve requirement ratio at 7 percent for both riel and U.S. dollar deposits and borrowings until the end of the first semester of 2021, and as necessary. Subsequently, in May 2021, the central bank issued its third round monetary easing measures which include, among other things, (i) a decision to maintain a reserve requirement ratio at 7 percent for both riel and U.S. dollar deposits and borrowings until further notice; and (ii) a permission to allow the banking and microfinance sectors to continue to restructure loans until the end of 2021. The COVID-19 vaccination program began in February 2021 and has quickly accelerated. A national COVID-19 vaccination strategic plan was introduced in May 2021.

**Goods exports have recovered.** Merchandise (excluding gold) exports grew at 12.2 percent in the first four months of 2021. Despite rising shipping costs, exports of GFT products, which bottomed out in January 2021, contracting by 13.2 percent y/y, have recovered since, growing at 10.2 percent and 27.8 percent in March and April 2021, respectively. In the first four months of 2021, exports of bicycles and combined vehicle, electrical, and electronic parts grew at 32.3 percent and 16.4 percent, respectively. Exports of garment and textile products no longer accounted for the majority of merchandise exports. The share of garment exports in total goods (excluding gold) exports declined to 45.6 percent in the first four months of 2021, down from 52.2% in 2020 (and 57.6% in 2019). Although a small segment of the housing market–low and affordable residential property–remained resilient, the downturn in the construction and real estate sector continued. In the first four months of 2021, approved construction permit value plummeted, contracting by 41.5 percent, while cement imports contracted by 19.2 percent. However, imports of steel and cooling equipment such as air conditioners grew by 5.4 percent and 24.1 percent, respectively.

**Resilient FDI inflows helped sustain the external sector.** In 2020, FDI inflows reached US$3.4 billion or 13.6 percent of GDP, compared to US$3.5 billion or 13.2 percent of GDP in 2019. In 2020, the current account deficit was fully financed by FDI, while gross international reserves accumulated further, reaching to US$21.5 billion or more than 10 months of prospective imports. Despite rising retail prices of petroleum products, inflation remained contained, declining to 1.7 percent in February 2021, compared to 2.9 percent at the end of 2020, partly supported by the easing of food prices and a broadly stable exchange rate which reached riel 4,072 per U.S. dollar at the end of May 2021, compared to riel 4,042 per U.S. dollar at the end of 2020.

**Monetary conditions continued to be accommodative.** Broad money growth remained sustained, expanding at 15.2 percent as of February 2021. Thanks to the central bank's accommodative monetary policy, domestic credit provided to the private sector accelerated, growing at 19.5 percent as of February 2021, compared to 17.7 percent at the end of 2020, as economic activity improved. The credit-to-GDP ratio increased to 142.2 percent in 2020, up from 114.2 percent in 2019. Deposit growth remained held up, expanding at 15.4 percent as of February 2021, mirroring continued strong capital inflows.

**The overall fiscal deficit is estimated to have widened but remained at a moderate level of 2.7 percent of GDP in 2020.** Notwithstanding unprecedented increase in COVID-19 related spending, estimated at 4 percent of GDP, efforts were made to contain expenditure with a reduction in spending on goods and services and other non-priority spending. Total expenditure increase is, therefore, estimated to have been modest, rising to 26.8 percent of GDP in 2020, up from 25.5 percent of GDP in 2019. In addition, impacts of the pandemic on domestic revenue were lessened by ballooned profit taxes for 2019 which were collected in April 2020.

**The new cash transfer scheme for poor and vulnerable households has seen increased demand.** As of January 2021, more than 710,000 households, or 19.5 percent of all households, have received a cash transfer from the government. Employment activity is showing signs of recovery. According to the survey of households, the percentage of respondents who were employed in December 2020, returned to the level recorded in May and August 2020, but remained below its pre-pandemic level.

## Outlook

**Cambodia's growth outlook remains highly uncertain** as the actual shape and pace of recovery is largely dependent on the course of the virus and the pace at which the vaccine can be rolled out. Therefore, we explore two scenarios: a baseline scenario, which is based on more optimistic assumptions on infection and vaccination; and a downside scenario, which assumes the realization of most of the downside risks.

**Under the baseline scenario, the economy is projected to grow by 4 percent in 2021,** supported by a gradual recovery in domestic demand following the vaccine deployment and improvements in external demand and capital inflows. The projections assume that market confidence is restored, while the current community outbreaks, which began in February 2021 remain under control, resulting in a staged easing of the lockdown restrictions without significant mid- to long-term adverse impacts on the corporate or banking sector. FDI inflows are steadily returning. Under the baseline, it is expected that the authorities are taking steps to attract further investment and promote trade by introducing a new investment law in the second half of 2021, boosted by the recently signed free trade agreements. Under Cambodia's economic recovery plan, efforts are underway to boost competitiveness through investment climate reforms and leveraging of digital technologies. The authorities pursue a countercyclical fiscal policy with a continued social protection program, while boosting public investment. Public debt and budget pressures have risen sharply and are likely to persist, and the authorities will need to consider options for restoring fiscal discipline once the recovery takes hold.

**Under the downside scenario, the economy is projected to grow at 1.0 percent in 2021.** The downside scenario assumes a deterioration in domestic economic conditions caused by repeated lockdowns and travel restrictions as efforts to contain the outbreaks are not successful, preventing economic recovery from taking hold, regardless of improvements in external conditions. Containment efforts drain public resources while deployment of the vaccination program is assumed to have progressed slowly. Consequently, market confidence is subdued, leading to a marked slowdown in FDI inflows, while the main export-oriented manufacturing sector such as GFT goods is disrupted by repeated lockdowns and impacted by the partial withdrawal of the "Everything But Arms" arrangement and temporary expiration of the Generalized System of Preferences. The fiscal deficit widens, as spending pressures rise, while domestic revenue declines sharply, caused by prolonged and sluggish domestic economic activity. As public debt and budget pressures persist, external borrowing and drawdown of the government's current savings increase, requiring more time before fiscal discipline can be restored.

**In the post-pandemic world, Cambodia's economy will likely follow a new trajectory** (a new normal), expanding rather moderately in the short-term. Cambodia's economy is tourist-dependent. Regardless of a recovery in domestic tourism after the easing of lockdowns, global tourism is expected to remain below pre-pandemic levels until 2023. Global economic recovery, supported in part by the significant U.S. stimulus, will revive trade in goods and could provide an external boost to growth of as much as 1 percentage point on average, but global tourism is expected to remain below pre-pandemic levels until 2023, which will delay economic recovery in tourism-dependent economies. A structural change, driven by a diversification of FDI projects which were earlier concentrated largely in the construction and real estate sector to non-garment manufacturing and agricultural commodity exports appears to be emerging, adapting to changes in domestic economic and external demand conditions.

## Challenges and risks

**Risks to Cambodia's growth outlook have intensified as the current wave of coronavirus outbreaks lingers.** Domestic economic activity has recently been disrupted by the reintroduction of lockdown during the second half of April 2021. The lockdown which was imposed on the two largest urban centers–-Phnom Penh and Takhmao, the second-most-populated city in Kandal province–-was necessary and saved lives, though may also been economically damaging. The current high infection rate is also threatening the public health system. Factories and businesses were affected, while domestic demand, especially for services products such as domestic travel, tourism, and hospitality services, were once again hit by travel restrictions, travel avoidance, and declining incomes. This will likely be a drag on growth until wider vaccine deployment.

**Cambodia's growth model—characterized by a narrow export base with a high degree of concentration of products and markets—exhibited weaknesses years before the pandemic hit.** While the country has a well-established, labor-intensive, and export-oriented garment industry, the manufacturing sector has for decades remained largely engaged in the "cut-make-trim" process, the lowest value-added section of the entire value chain. The country's external competitiveness eroded, partly caused by rapidly rising wages—made worse by a dollarized economy—and exacerbated by challenges in doing business and investment climate reforms. The vulnerabilities, however, were masked by a surge in capital inflows in the pre-coronavirus crisis period to largely finance the construction and real estate sector. With the collapse of the tourism sector and a stalled construction boom, the pandemic has exposed Cambodia's structural weaknesses.

**Along with domestic weaknesses, an uncertain global outlook remains a key risk to Cambodia's recovery.** Delays in global vaccine distribution could lead to the persistence of the pandemic, while outbreaks trigger more lockdowns. Cambodia's merchandise exports will likely be further impacted by partial withdrawal of the "Everything But Arms" arrangement and temporary expiration of the Generalized System of Preferences. In addition, Cambodia is increasingly dependent on China in trade, investment, and official development assistance. High credit growth in the banking sector, particularly to the construction and real estate sector, remains a key risk to Cambodia's financial stability.

**Following a local outbreak that started on February 20, 2021, Cambodia has experienced rapidly rising reported coronavirus cases and deaths.** As of May 31, 2021, there were 30,094 cases and 214 deaths. The pandemic threatens to reverse years of extraordinary development gains in the country. In the absence of significant mitigation measures, the COVID-19 pandemic could result in sharply rising unemployment and increased poverty. Poverty simulations based on macroeconomic projections show that a sharp economic slowdown would produce a substantial increase in poverty of between 5.4 and 6.0 percentage points. This translates into between 859,000 to 950,000 additional poor and a reversal of six years of progress against poverty. Of these, households relying on non-agricultural wages, particularly construction workers, will be hit hardest by the outbreak.

### Policy options

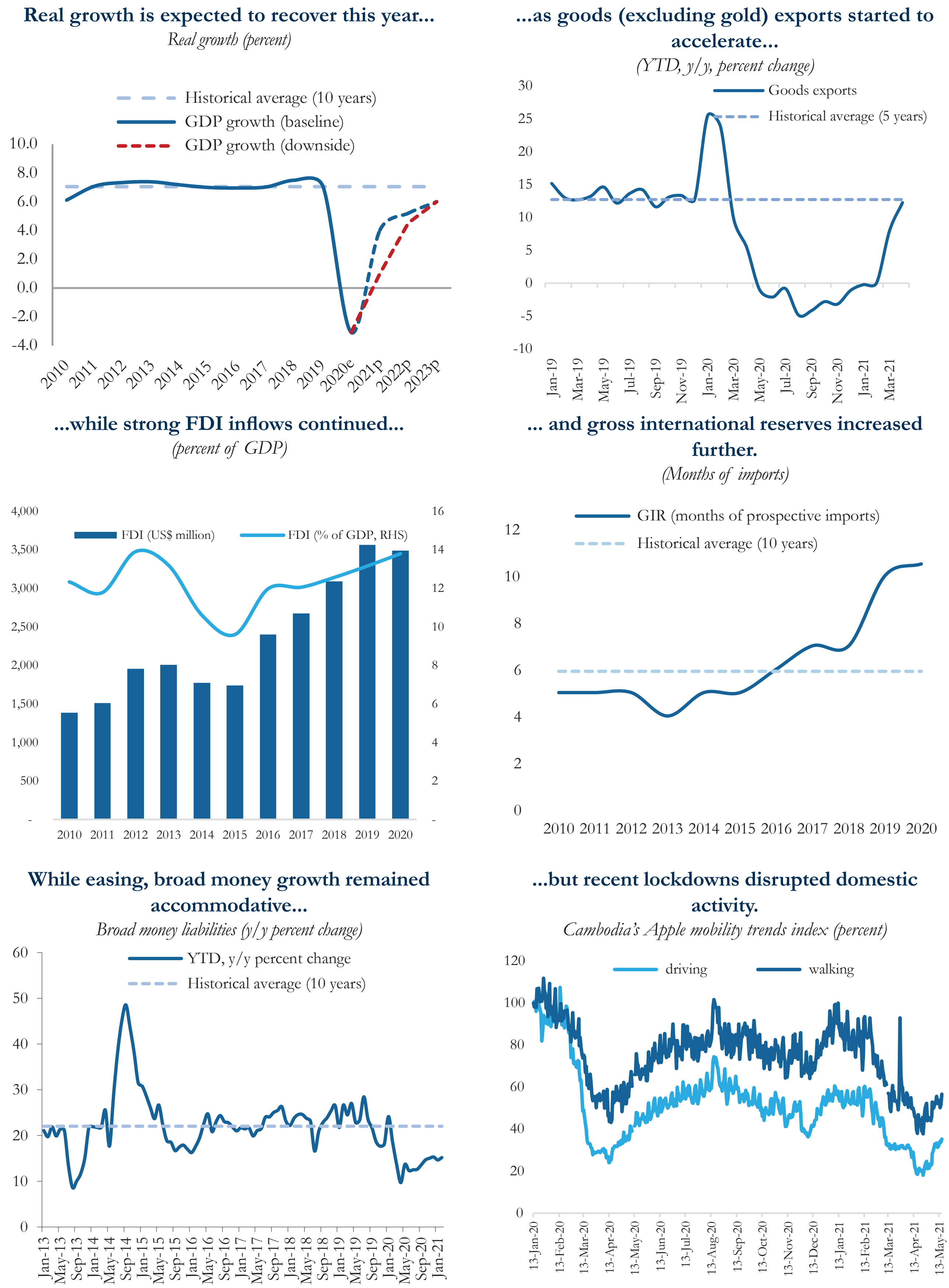
**It is urgent to accelerate implementation of the vaccination program, while continuing to effectively contain the rising infection cases and deaths.** Given potentially lingering outbreaks across the country, the benefits of rapid vaccination in reducing growing numbers of hospitalization and deaths, while relieving pressures on the struggling health system will outweigh its costs. Non-pharmaceutical interventions can also play a complementary role in the containment of the disease. Of a Cambodian population of more than 15 million, over 10.1 million are aged 18 and older and may need to be vaccinated. Thus, Cambodia needs over 20 million doses of coronavirus vaccines for this age group alone. Based on the authorities' national COVID-19 vaccination strategic plan, the country expects to obtain 13.5 million doses, or about 66 percent of the needed vaccines for the age group by September 2021. The plan targets to fully vaccinating about 5 million people under the first priority group during May to November 2021, a period of seven months, with about 10 million doses of coronavirus vaccines. As of end-April 2021, about 2.4 million doses of the vaccines have deployed. So, the plan should achieve an average of 1.1 million doses per month during May to November 2021 to completely deploy the remaining 7.6 million doses. A masterplan for COVID-19 vaccination published in March 2021 by the Ministry of Health targets vaccinating 10 million people by mid-2022.

**Given the country's relatively large fiscal space, further boosting pro-poor and growth-enhancing public investment including cash-for-work projects, is critical for economic recovery.** In this regard, the 2021 budget has boosted domestically financed public investment which, for the first time, exceeds externally financed public investment. More efforts are, however, needed to improve the business and investment climate, especially to facilitate the structural change as the construction boom has stalled and more investment is now going into production to serve mostly exports, while shoring up confidence with introduction of the new investment law, taking advantage of the CCFTA and RCEP. As the economy is highly dollarized, fiscal policy will continue to be a sole macroeconomic instrument to support relief, recovery, and growth. Relief continues to be needed, especially for poor and vulnerable households. Recovery requires improvements in investment climate and incentives to spur investment and to boost exports because the COVID-19 shock threatens to lock the economy into an underemployment equilibrium. Growth requires further public investment to improve the quality of both hard (physical) and soft (regulatory) infrastructure to reduce transport and logistics costs in order to boost external competitiveness.

**It is imperative to continue to closely monitor vulnerabilities arising from a prolonged property boom and the increase of credit provided to the construction sector during the pre-pandemic period.** The loan-to-deposit ratio already reached 120 percent in 2020, up from

78.7 percent a decade ago. This is particularly crucial as current community outbreaks linger and the numbers of factories and firms being severely affected are rising. Such events are likely to further diminish the ability of businesses and households to repay loans, putting the entire financial sector under increased stress. The authorities recently called on housing developers to accept delays in mortgage payments. The total value of loans and affected borrowers' accounts that need to be restructured will likely increase further this year, from last year's reported 285,000 accounts with a total of US$4.2 billion or 11.2 percent of total outstanding credit of the banking and microfinance sectors. Of the US$4.2 billion, US$1.73 billion, or 41.5 percent, was provided to affected borrowers engaged in the construction, tourism, and transport (and logistics) sectors combined. As these sectors continue to be hit hard by lingering local outbreaks, demand for loan restructuring from the sectors will certainly increase further. Non-performing loans are expected to rise from their current low levels of 2.7 percent and 1.8 percent for the banking sector and microfinance sector, respectively, in 2020. The central bank needs to continue to closely monitor financial risks, focusing on liquidity conditions, capital, and quality of credit together with the current macroprudential measures in place as discussed in the monetary section in the main report.

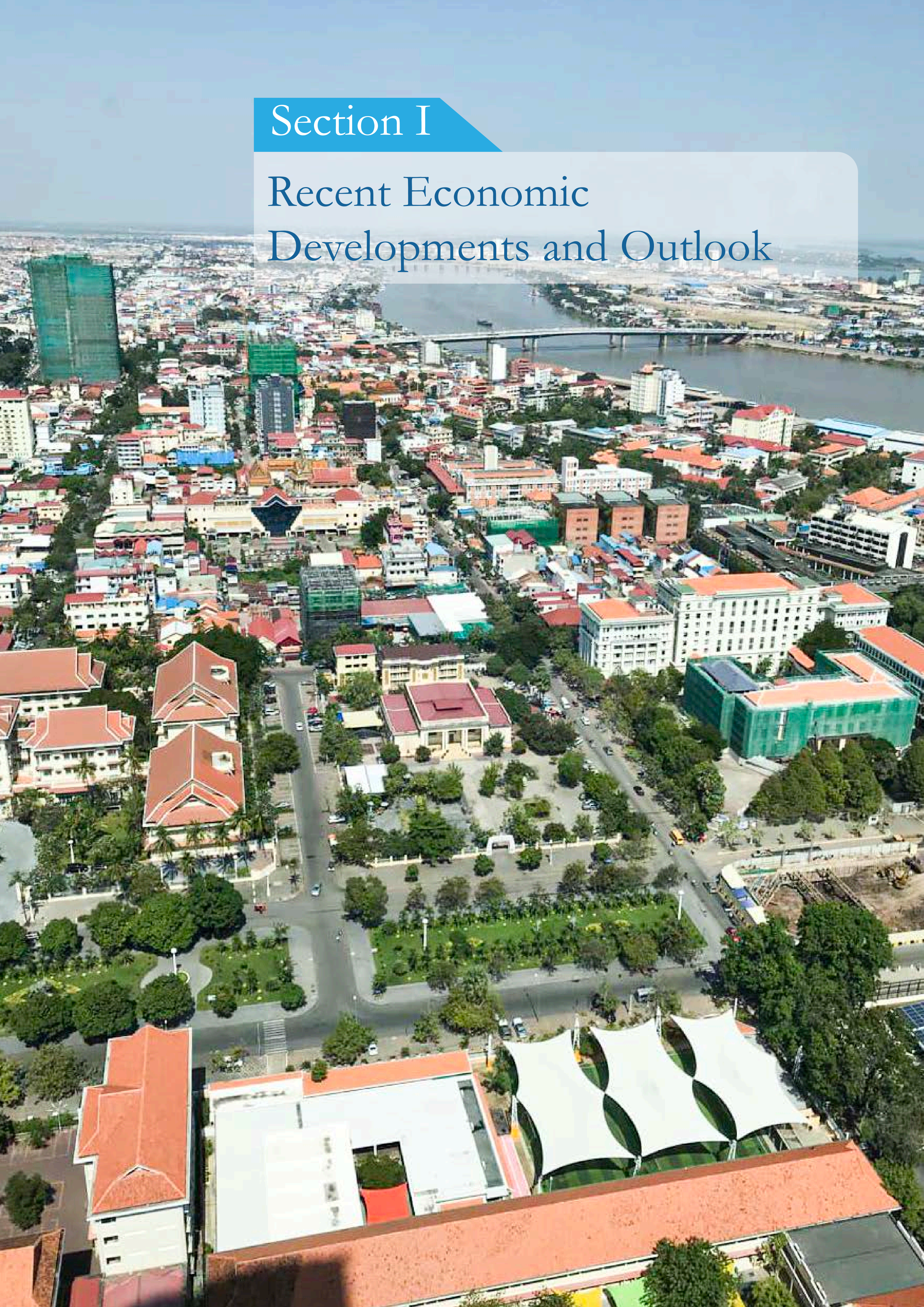
## FIGURE ES.1: CAMBODIA'S RECENT DEVELOPMENTS AT A GLANCE




*Sources:* Cambodian authorities; World Bank staff estimates and projections.
*Note:* e = estimates; GIR=gross international reserves; p = projection; RHS = right-hand scale; YTD = year-to-date; y/y = year-on-year.

# Section I

# Recent Economic Developments and Outlook



# Recent Economic Developments and Outlook

## Recent developments

### Despite vigorous containment efforts, local outbreaks resurged

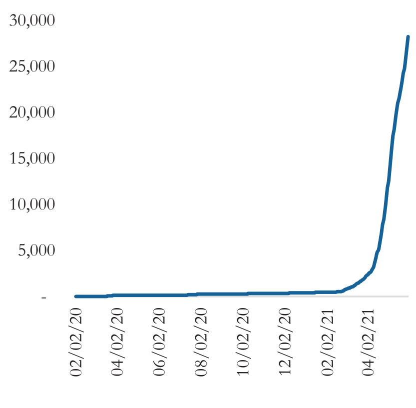
**Cambodia successfully contained the spread of the coronavirus until the first quarter of 2021.** It was among the countries with the fewest coronavirus cases in Asia, with just 1,753 infections (of which 967 have fully recovered and three deaths) recorded as of March 22, 2021, after the first confirmed case was found on January 27, 2020.[1] However, the country has recently experienced flare-ups of coronavirus infections that could potentially cripple the country's public health system. As of May 31, 2021, there were 30,094 cases and 214 deaths (figure 1). In response, the authorities have intensified contact tracing by identifying all people that a COVID-19 patient has come in contact with, opened up new quarantine facilities, increased the number of hospitals to treat the rising number of coronavirus patients, and procured for additional medical equipment and ambulances. Among the most affected areas are the main urban centers which include Phnom Penh, Kandal, Siem Reap, Sihanoukville and Prey Veng provinces. In April 2021, the authorities imposed lockdown in two largest urban centers-– Phnom Penh and Takhmao, second-most-populated city in Kandal province.

### Coronavirus vaccination program has started

**The coronavirus vaccination program began on February 10, 2021,** after the country obtained 600,000 doses of the Sinopharm vaccine from China on February 7. As of end-April 2021, there have been 1.3 million doses administered (figure 2). During the same period, Cambodia received more than 4.0 million doses of coronavirus vaccine, of which 324,000 doses were of Covishield, obtained through the COVAX facility, while the rest were the Sinovac and Sinopharm vaccines from China. In April 2021, the last shipment of 400,000 doses of Sinopharm arrived on April 28. Of a Cambodian population of more than 15 million, over 10.1 million are aged 18 and older and may need to be vaccinated under the current vaccine availability for this age group. So, Cambodia needs over 20 million doses of coronavirus vaccine.

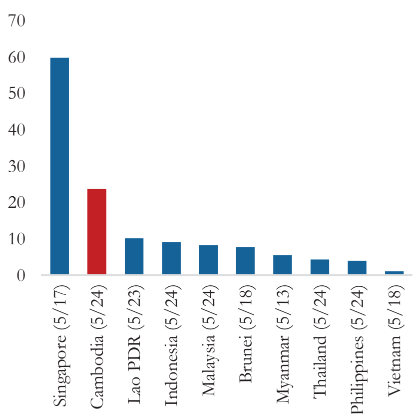
**A national COVID-19 vaccination strategic plan was introduced in May 2021.** Based on

**Figure 1: Coronavirus cases have surged**
(7-day moving average, as of May 31, 2021)



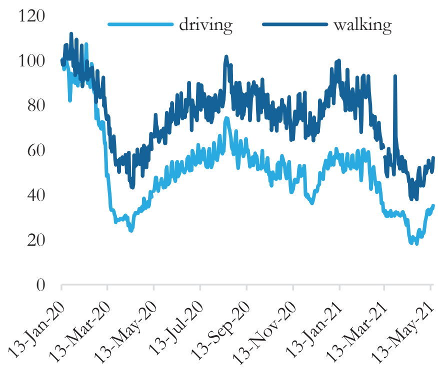

*Source:* Our World in Data.

**Figure 2: Vaccinations accelerated**
Doses given per 100 residents




*Source:* Our World in Data.

**Figure 3: Cambodia's mobility Apple trends index deteriorated**
(percent as of May 16, 2021)




*Source:* Apple mobility trends, Apple.

1 Ministry of Health press release, November 5, 2020.

their place of residence that has the highest population density, the heaviest concentration of non-farm activity, and the most economic significance, about 5 million people aged 18 and older (or 49 percent of the population in this age group) is prioritized to be vaccinated first under the plan. Of this group, 2.5 million people residing in the capital city of Phnom Penh and Kandal province will receive vaccinations in the first phase, the duration of which will be May to mid-July 2021. The remaining 2.5 million people under the prioritized group residing in the rest of the country will be vaccinated in the second (mid-July to September) and third (October to November 2021) phases, which cover 2.0 million people and 0.5 million people, respectively. Under the plan, all 5 million people are targeted to be fully vaccinated within a period of seven months (May to November) with 10 million doses of coronavirus vaccine. As of end-April 2021, about 2.4 million doses of the vaccines have deployed, so, the plan should achieve an average of 1.1 million doses per month during May to November 2021 to completely deploy the remaining 7.6 million doses. A masterplan for COVID-19 vaccination published in March 2021 by the Ministry of Health aims to vaccinate 10 million people by mid-2022.

**A resurgence of community outbreaks triggered a countrywide travel restriction.** Businesses, schools, colleges, and museums were temporarily closed during March and April 2021. A recovery of domestic demand, supported by gradually improving domestic consumption until the first quarter of 2021 has been interrupted as domestic economic activity has once again been curtailed (figure 3), especially in the main urban centers, which include, among others, Phnom Penh and the provincial capitals of Kandal, Siem Reap, Sihanoukville, and Prey Veng provinces.

### Notwithstanding uneven containment, economies of the region bounced back

**The coronavirus has proved difficult to suppress since the first case was confirmed in Wuhan in December 2019.** China and Vietnam, which had largely contained the disease, saw occasional local outbreaks.[2] Malaysia witnessed a significant resurgence, while Myanmar, Mongolia, and Thailand have seen more limited spurts in infections. Of the countries in which the virus raged a few months ago, the situation has improved in Indonesia and the Philippines, but the number of cases remains high. The emergence of more transmissible variants of the virus, however, poses new challenges to the containment of the disease globally.

**Economies in the East Asia and Pacific (EAP) region have begun to bounce back.** However, among major economies in the region, only China and Vietnam have followed a V-shaped recovery path, with output surpassing pre-pandemic levels in the second half of 2020. Most of the other countries have not seen a full-fledged recovery in terms of either output or growth momentum. By the end of 2020, the output in four major economies (Indonesia, Thailand, the Philippines, and Malaysia) remained on average around 5 percent below pre-pandemic levels, with the smallest gap in Indonesia at 2.2 percent and the largest gap in the Philippines at 8.4 percent. Global economic recovery (see box 1), supported in part by the significant U.S. stimulus, is expected to revive trade in goods and could provide an external boost to growth of as much as 1 percentage point on average, but global tourism is expected to remain below pre-pandemic levels until 2023, which delays economic recovery in tourism-dependent economies.

### Exports are gradually recovering, thanks to revitalization of global demand

**Some countries have benefited from robust global demand for the products in which they specialize.** The recovery of global demand will be further boosted by the U.S. stimulus package. Countries like China, Thailand, and Vietnam did not simply ride the wave of sustained demand for their exports but increased their share in world exports of these products.[3] Supply disruption was not severe in these countries, thanks to limited disease conditions. Merchandise exports of China and Vietnam

2 World Bank 2021a.
3 World Bank 2021a.

**Box 1:**

## Global economic developments and outlook[1,2]

Global growth is gaining momentum despite the resurgence of COVID-19 in certain countries. Global Purchasing Managers' Index indicators registered a broad-based increase in March, signaling a continued pickup in global growth momentum. The strong recovery of global manufacturing is supporting a recovery of goods trade. Air transportation has risen in the first few months of the year but remains 25 percent below its pre-crisis level.

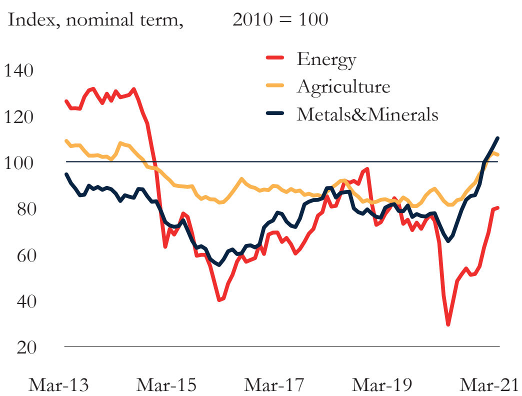
Global financing conditions continue to be favorable overall, with low credit spreads on corporate bonds restraining increases in private borrowing costs. Commodity prices have risen in 2021 with most now exceeding their pre-pandemic levels (figure B1.1). Nonetheless, COVID-19 cases are on the rise globally, with more infectious variants establishing themselves as dominant strains (figure B1.2). Global mobility declined in early April, as many countries moved to tighten pandemic restrictions.

Following a sharp contraction in 2020, a stronger-than-expected global recovery is envisioned in 2021 supported by a large fiscal expansion in the United States. Growth in the East Asia and Pacific (EAP) region is projected to accelerate to 7.4 percent in 2021, led by a strong rebound in China. The recovery in the region excluding China is expected to be protracted and expand by 4.4 percent in 2021 on average, with significant cross-country variations. The projected growth would not be sufficient to fully undo the pandemic-related output losses in many regional economies, with output in many of them expected to remain below pre-pandemic levels until 2022.

There is high uncertainty around the global growth forecast. The sustainability of the recovery depends on the duration of the pandemic, the effectiveness of policy actions in achieving widespread vaccination and preventing financial meltdowns and resuming global travel. The global recession would be deeper than the baseline forecast, if bringing the pandemic under control took longer than expected, or if financial stress triggered cascading defaults. Thus far, an extraordinary policy response has prevented the slowdown in activity from becoming a financial crisis. Nonetheless, financial conditions will remain fragile for many market participants. A prolonged disruption to economic activity could exacerbate financial stress, which could lead to widespread financial crisis.

The pandemic is likely to have a durable impact through multiple channels, including lower investment, weak confidence, and erosion of human capital. The long-term damage related to the pandemic will be particularly severe in economies that suffered most from extended outbreaks of COVID-19 and the collapse of global tourism and trade and those that suffered financial crises (World Bank 2021 forthcoming).

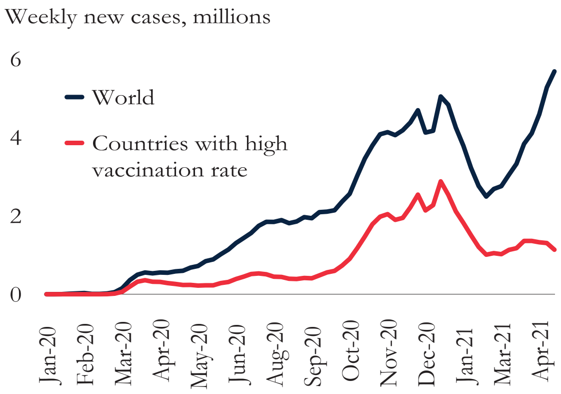
**Figure B1.1. Commodity prices**




*Source:* Haver Analytics; World Bank.

*Note:* Last observation was March 2021.

**Figure B1.2. Global weekly new infections of COVID-19**




*Source:* Bloomberg; World Bank; World Health Organization.

*Note:* Red line indicates aggregated weekly new infections of COVID-19 for countries in which, on April 25, more than 20 percent of the population had received at least one dose of vaccine.

1 This box was prepared by Ekaterine Vashakmadze, Prospects Group.

2 Draws on the WB January Global Economic Prospects (GEP) report and April 2021 EAP update. The updated global forecasts will be published in the June 2021 GEP.

accelerated quickly, surpassing their pre-pandemic growth rates (figure 4). Vietnam's exports have performed exceptionally well, especially to the United States, in part due to the trade diversion effect resulting from U.S.-China tensions.[4] China and Vietnam are expected to grow strongly in 2021—by 8.1 percent and 6.6 percent, respectively—while the rest of the region is expected to grow by only 4.4 percent. Conversely, countries with the weakest performance were the ones that depend on earnings from tourism rather than exports of manufactured goods, especially electronics.

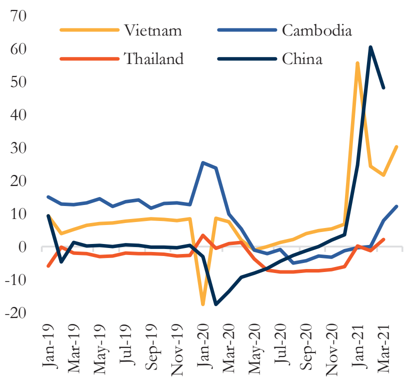
**Cambodia's merchandise exports have adapted to changes in external demand conditions and the share of garment exports in total goods** (excluding gold) **exports declined to 45.6 percent in the first 4 months of 2021,** down from 52.2 percent in 2020 (and 57.6 percent in 2019) (figure 5). Exports of garments (and textiles) no longer accounted for the majority of Cambodia's goods exports as of April 2021. As the country's goods exports adjusted, the decline in GFT goods exports in the second and third quarters of 2020 was partly offset by rising exports of agricultural commodities, processed agricultural products, newly emerging manufactured products (electrical, electronic, and vehicle parts, including bicycles), and the rest (figure 6). This helped maintain a 16.7 percent year-on-year growth rate of Cambodia's (recorded) merchandise exports in 2020, if gold exports were included. While having a relatively small share of 3.2 percent of total merchandise exports (excluding gold), exports of electrical parts, wire and accessories, and vehicle parts reached US$456 million, growing at 18.1 percent in 2020. Exports of bicycles also accelerated, reaching US$527 million, expanding at 27.7 percent in 2020.

**Goods exports have recovered.** Merchandise (excluding gold) exports grew at 12.2 percent in the first four months of 2021. Despite rising shipping costs, exports of GFT products, which bottomed out in January 2021, contracting by 13.2 percent y/y, have recovered since, growing at 10.2 percent and 27.8 percent in March and April 2021, respectively. Exports of bicycles grew at 32.3 percent during the first four months of 2021, compared to 27.8 percent in 2020. During the same period, combined vehicle, electrical, and electronic parts exports grew by 16.4 percent and 18.2 percent, respectively.

### Cambodia's manufacturing exports to the United States rose

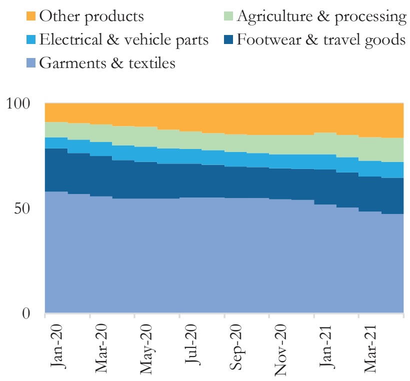
**The United States** (U.S.) **remained Cambodia's number one export market which continued to expand in 2020.** The U.S. market captured

**Figure 4: Goods exports in the region accelerated[1]** (YTD, y/y percent change)



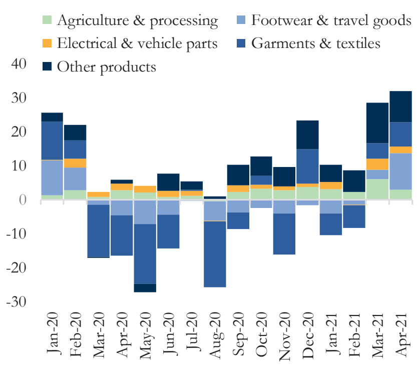

*Source:* Haver Analytics.
*Note: 1.* Cambodia's exports exclude gold exports; YTD =year-to-date.

**Figure 5: Declining share of garment exports in total goods** (excluding gold) **exports** (percent)




*Source:* Cambodian authorities.

**Figure 6: Cambodia's exports[1] recovered** (contribution to export growth, percentage point)




*Source:* Cambodian authorities.
*Note: 1.* Cambodia's exports exclude gold

4 World Bank 2021a.

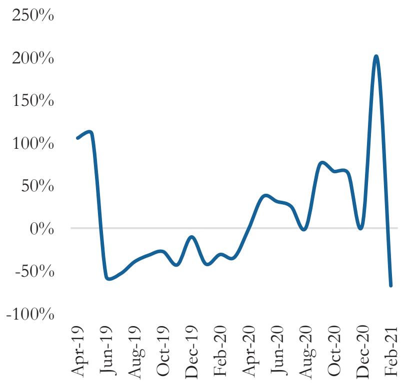
36.7 percent of total GFT exports in 2020, up from 31.9 percent in 2019. Total GFT exports to the U.S. market rose to US$3.5 billion or 3.6 percent y/y increase, boosted in part by the duty (and quota) free access provided by the U.S. Generalized System of Preferences (GSP) program. The GSP program, granted in 2016, has boosted Cambodia's exports of travel goods such as luggage, backpacks, handbags, and wallets.[5] However, legal authorization for the GSP program expired on December 31, 2020, and is pending U.S. congressional approval.[6]

**In contrast, total GFT goods exports to the EU market fell significantly, contracting by 35 percent, reaching only US$2.6 billion in 2020.** The E.U. market accounted for 27.5 percent of combined GFT exports, down from 38.2 percent in 2019 (and 42.6 percent in 2018). The combined EU and UK market accounted for 34.9 percent of total GFT exports, remaining below the share of the U.S. market of 36.7 percent. The negative impact of the pandemic and the partial withdrawal of the EU's Everything But Arms preferential treatment, effective since August 12, 2020 (affecting approximately 20 percent of Cambodia's exports to the EU)[7] is mainly behind the sharp decline of Cambodia's exports to the market. Similarly, while Cambodia's exports of bicycles to the U.S. market doubled, reaching US$147 million in 2020, bicycle exports to the EU market declined by 3.9 percent, reaching US$275 million.

## FDI inflows started to recover

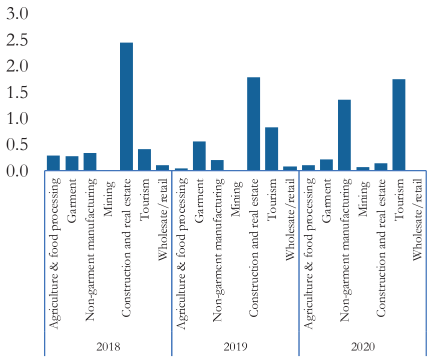
**Attracted by the newly signed free trade agreements, the value of approved projects in the real sector financed by FDI expanded.** The expansion underpinned a diversification of FDI projects, which were earlier concentrated largely in the construction and real estate sector to the energy, healthcare, telecommunication, garment, travel goods, and agriculture sectors (including agroprocessing industries), adjusting to changes in domestic economic and external demand conditions. The tourism sector, however, continued to receive a relatively large portion of (approved) FDI projects. In 2020, total approved project (fixed asset) value financed by FDI in Cambodia's real sector rose to US$3.6 billion, or a 4.3 percent year-on-year increase (figure 7). China

**Figure 7: Approved FDI project value expanded**
(YTD, y/y percent change)



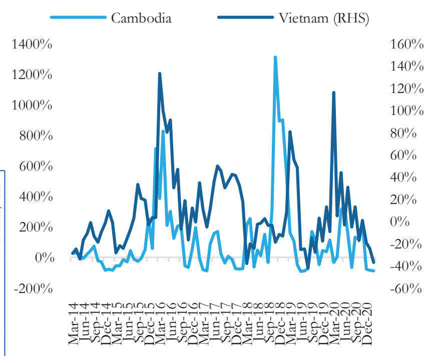

*Source:* Cambodian authorities.
*Note:* YTD = year-to-date.

**Figure 8: Rising FDI projects going to non-garment industries**
(US$ billion)




*Source:* Cambodian authorities.

**Figure 9: FDI inflows to Cambodia and Vietnam followed a similar trend**
(3mma, y/y)




*Source:* Cambodian authorities and Haver Analytics.
*Note:* RHS = right-hand scale; 3mma = 3-month moving average.

5 See https://kh.usembassy.gov/duty-free-access-travel-goods-made-cambodia/
6 See https://www.cbp.gov/trade/priority-issues/trade-agreements/special-trade-legislation/generalized-system-preferences
7 For more details, please see https://trade.ec.europa.eu/doclib/press/index.cfm?id=2113.

continued to account for about half of total (approved) FDI project value.

**In 2020, FDI inflows appeared to consist largely of "forward-looking" projects, targeting short- to medium-term investment returns.** This reflects the reality that the pandemic lingers. So, quick return projects such as those invested in the retail, wholesale, and real estate sectors did not receive much attention. The largest component of approved FDI project value in 2020 went to the tourism sector (a five-star hotel, a theme park and a trade center), accounting for US$1.75 billion, although the tourism sector has been hit hard by the pandemic. The second-largest component of approved FDI project values went to the "non-garment" industries, accounted for US$1.36 billion (figure 8). They comprised mainly energy, including renewable energy (US$588 million), healthcare (US$358 million), and telecommunication (US$102 million). The garment sector was next, receiving US$220 million, followed by the agriculture and agroprocessing sectors (US$110 million). Approved FDI project value going to the construction and property sector plummeted, accounting for only US$140 million in 2020, down from US$1.79 billion in 2019.

**As discussed, Cambodia's manufacturing exports remained heavily reliant on the garment industry,** which for decades has largely engaged in the "cut-make-trim" process, the lowest value-added section of the entire value chain. In contrast, Vietnam has been able to rapidly diversify its manufacturing export base and more importantly, it has successfully moved up to high-value-added electronics exports (see also box 2). While China continued to account for about half of total FDI inflows to Cambodia, Chinese FDI covers only 11 percent of total FDI inflows to Vietnam. Vietnam has a long list of main FDI country origins. In addition to China, Republic of Korea, Japan, Singapore, Taiwan (China), the British Virgin Islands, Malaysia, and Thailand account for 18.7 percent, 16.3 percent, 13.7 percent, 8.9 percent, 6.0 percent, 3.5 percent, and 3.0 percent, respectively of FDI stock as of 2019.[8] About 60 percent of FDI inflows to Vietnam go to manufacturing, followed by real estate activities (16.0 percent), and electricity, gas, steam and air conditioning supply (6.1 percent). Nevertheless, FDI inflows to both Cambodia and Vietnam appear to follow a similar trend (figure 9), likely reflecting external demand conditions underpinning foreign investors' decision to invest in emerging economies.

## Challenges in investment climate reforms remained

**Besides changes in trade policy, changes in the efficiency with which goods can be produced are likely to lead to changes in the composition of goods that a country exports** (and imports).[9] Cambodia and Vietnam are both members of the World Trade Organization (WTO) and Association of Southeast Asian Nations (ASEAN), and have maintained relatively liberal trade policies. Vietnam has, however, succeeded in improving the efficiency as reflected in a relative high ease of doing business ranking which means the regulatory environment in Vietnam is more conducive to the starting and operation of firms and businesses. In 2020, Vietnam's doing business ranking was 70th and Cambodia's was 144th (out of 190 countries).[10] Lowering barriers to firm entry and a favorable environment attract new investment. Streamlining rules and regulations relating to exports, while reducing transports, customs, ports, and administrative costs underpins trade growth and export diversification. In 2018, Vietnam ranked 39th and Cambodia 98th (among 160 countries) on logistic performance indexes.[11]

## Construction continued to be subdued due to excess supply

**For several years preceding the pandemic, Cambodia experienced an unprecedented construction and real estate boom, which created excess supply.** External demand for the country's commercial and residential

8 Foreign direct investment projects licensed by main counterparts (accumulation of projects having effect as of December 31, 2019) by main counterparts (General Statistical Office of Vietnam).

9 Kehoe and Ruhl (2003): How Important Is the New Goods Margin in International Trade? Federal Reserve Bank of Minneapolis Research Department Staff Report 324.

10 See World Bank Doing Business report at https://www.doingbusiness.org/en/data/exploreeconomies/cambodia

11 See more detailed logistic performance index at https://lpi.worldbank.org/international/aggregated-ranking

## Box 2:

### Factors behind Vietnam's robust economy growth

**Vietnam was one of only a few economies that grew during the pandemic.** Vietnam's GDP expanded at 2.9 percent in 2020, due to exceptional resilience in Vietnam's export and domestic sectors, although this growth performance was significantly lower than the 7 percent growth rate in 2019. During the two decades prior to the pandemic, the country experienced a more than tenfold increase in share of exports of electronics and machinery (computers, electronics, telephones, mobile phones, still image and video camaras, machinery, equipment, tools, instruments, other means of transportation, and insulated wire and cables), rising to 60.3 percent of total merchandise exports (US$146 billion) in 2018, up from 5.9 percent of total merchandise exports (US$3.6 billion) in 2008 (figure B2.1). This allowed Vietnam to weather the COVID-19- induced global demand shock.

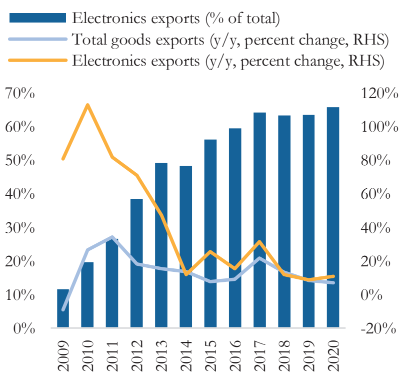
**In contrast, Cambodia's exports continue to be heavily dependent on low-value-added garment products although they no longer accounted for the majority of goods exports as of April 2021.** (figure B2.2). While the country has a well-established, labor-intensive, and export-oriented garment industry, the manufacturing sector has, as mentioned, for decades remained largely engaged in the "cut-make-trim" process, the lowest value-added section of the entire value chain. Cambodia's narrow export base was hit hard by external demand shocks in 2020. Cambodia's real growth contracted by 3.1 percent in 2020, plunging the economy into a recession for the first time in three decades.

**While exports of most countries in the region plummeted due to the pandemic, Vietnam's successfully diversified exports performed exceptionally well,** especially those to the United States, due in part to the trade diversion effect resulting from U.S.-China tensions (figure B2.3). In 2021, Vietnam's economy is set to grow 6.6 percent on the back of strong performance by export-oriented manufacturing, and a robust recovery of domestic demand.

**To reach upper middle-income status by 2030, Vietnam's development model is set to change to a knowledge-based, digitalized, green economy.** In the transition years, the country will need to see major investments in human capital, innovation, and green infrastructure to increase productivity, pursuing an even more resilient and knowledge-based economy. Vietnam is committed to: (i) improving the quality of market-economy institutions and governance; (ii) developing human capital, science, technology and innovation; (iii) further integrating into the global economy; and (iv) continuing to improve the transport, energy and IT infrastructure and green and resilient megacities.

**Cambodia's economy is projected to recover, expanding modestly at 4 percent in 2021.** However, Cambodia's growth model—characterized by a narrow export base with a high concentration of products and markets, masked by a pre-crisis surge in capital inflows which fueled a construction and real estate boom may no longer be sustainable in the short to longer term. Unless the country's structural weaknesses are addressed, the economy will likely follow a new trajectory (a new normal), expanding only moderately in the post-pandemic world.

**Figure B2.1. Vietnam's exports diversified, consisting largely of high-value-added products**




*Source:* Haver Analytics.

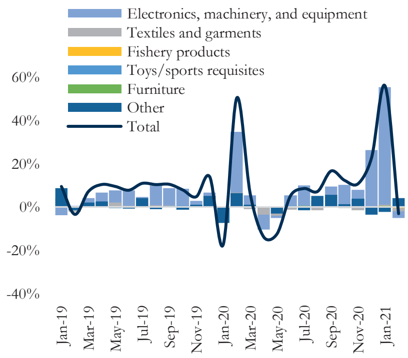
*Note:* RHS = right-hand scale.

**Figure B2.2. Cambodia's exports remain heavily dependent on garments**


*Source:* Haver Analytics.

**Figure B2.3. Driven by electronics, Vietnam's exports performed very well**

Contribution to exports growth (percentage point)




*Source:* Haver Analytics.

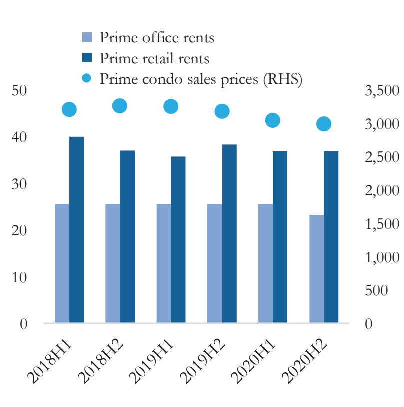
property partly contributed to the boom. When the pandemic hit together with lockdowns and tightened international travel restrictions including a required 14-day quarantine period among others, external demand was interrupted, and most FDI-financed property investment, especially in high-rise development projects in the urban centers such as Phnom Penh and Sihanoukville, was suspended. Although a small segment of the housing market—-low and affordable residential property—-remains resilient, evidence of a subdued property market is mounting, and real estate prices have been declining (figure 10). Condominium prices have been hit particularly hard.[12] In 2020, depressed construction activity was reflected in the decline in the country's imports of steel, cement, and other basic construction materials. The value of steel, and cement imports mainly used for the construction industry contracted by 34.5 percent and 48.6 percent, respectively, year-on-year in 2020 (figure 11).

**Excess supply may have resulted in lower foreign investor appetite for investing in property development projects.** Consequently, the value of approved construction permits plummeted, contracting by 63.8 percent in 2020 (figure 12), while approved construction area (in square meters) declined by 24.3 percent. The real estate industry expects supply and average property prices to slip further in 2021,[13] while a recovery in the demand for commercial and residential property will likely take time, as it is dependent on the return of external demand, given Cambodia's relatively small domestic market. Relaxation of international travel restrictions and the eventual lifting of the compulsory 14-day quarantine, once community outbreaks are under control, may pave the way for the return of foreign demand, which should help to once again propel the property market. However, it is unclear how long external demand will last, if returns, given the limited opportunities for a good return on investment for holding property in Cambodia. (Sihanoukville, experienced a rapid construction boom during 2017–19, with an influx of Chinese investment due to a prospect of a high investment return from tourism activities backed by a short-lived casino industry.)

## Agricultural production remained resilient

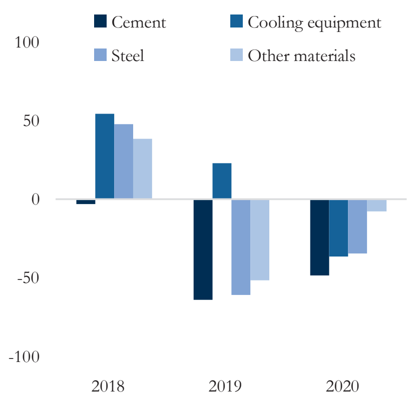
**Total rice production expanded, thanks to improved dry season rice production during the 2020–21 rice production year.** The cultivated (and harvested) area of dry season rice rose to 0.65 million hectares or a 9.0 percent increase in 2020 (figure 13). In addition, the yield

**Figure 10: Real estate prices declined**
(US$ per square meter)



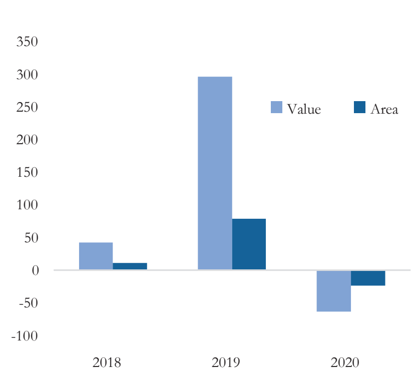

*Source:* CBRE, Cambodia.
*Note:* RHS = right-hand scale.

**Figure 11: Basic construction materials imports contracted**
(y/y percent change)




*Source:* Cambodian authorities.

**Figure 12: Approved construction permits declined**
(y/y percent change)




*Source:* Cambodian authorities.

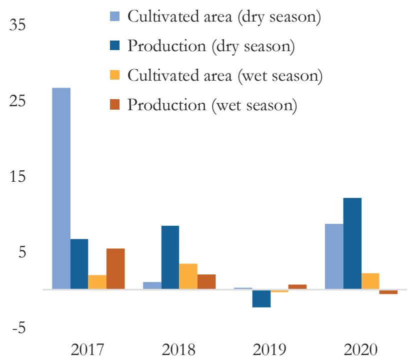
12 See https://www.globalpropertyguide.com/Asia/Cambodia/Price-History
13 2021 Fearless Forecast–Recession or Resurgence, CBR, Cambodia. See https://images.cbre.com.kh/2021/02/2021_Fearless-Forecast_For-Circulation.pdf.

of dry season rice also improved, reaching 4.5 metric tons per hectare or a 2.2 percent increase in 2020. As a result, last year's dry season rice production rose to 2.93 million metric tons or a 12.1 percent increase. Wet season rice production, however, remained subdued due to unpredictable weather conditions. Notwithstanding efforts to expand the cultivated area of wet season rice to 2.79 million hectares or a 2.2 percent increase in 2020, mid-season drought and end-season floods caused the harvested area to decline by 3.0 percent. Wet season rice production, therefore, dropped to 8.22 million metric tons or a 0.6 percent year-on-year contraction in 2020. Thanks to the increase in production of dry season rice, total rice production rose to 11.15 million metric tons or a 2.4 percent increase in 2020. While the cultivated (and harvested) area of dry season has steadily increased with efforts to expand the dry season irrigation system, the yield of dry season rice continues to fluctuate (figure 14), which likely indicates the continued challenges in using modern agricultural inputs and applying new cultivation technologies. In contrast, the yield of wet season rice has been less volatile and has gradually improved, reaching 3.1 metric tons per hectare or 70.3 percent of dry season rice's yield in 2020, up from 2.5 metric tons per hectare or 63 percent of dry season rice's yield in 2008. Rice is Cambodia's major crop, and value added of crop production accounted for 57.4 percent of the country's agricultural GDP in 2020.

## Domestic price volatility affected agricultural production

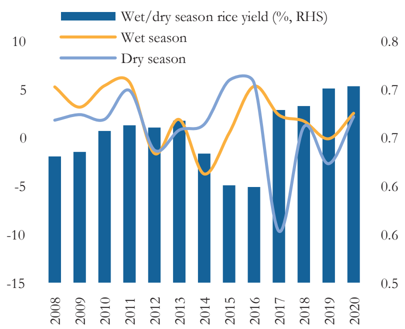
**Domestic agricultural commodity price volatility remains a challenge to the agriculture sector,** especially for (non-rice) agricultural products. While the agriculture sector has been benefiting from increased labor availability and additional investment, agricultural commodity price volatility, especially non-rice agricultural products produced for the domestic market, remains a critical constraint as do higher electricity and logistics costs. Agricultural production in Cambodia often faces under- or oversupply of products caused by seasonal factors and poor market diversification.[14] Weather conditions can be one of the biggest challenges: favorable weather can lead to oversupply, whereas unfavorable weather can lead to undersupply. Given Cambodia's relatively small domestic market, and the collapse of the tourism sector, volatile retail agricultural prices amplify (figure 15) and hurt overall (non-rice) agricultural production. The authorities have made further efforts to address this issue by establishing farmer organizations, geographical identification

**Figure 13: Wet season rice production was subdued**
(y/y percent change)



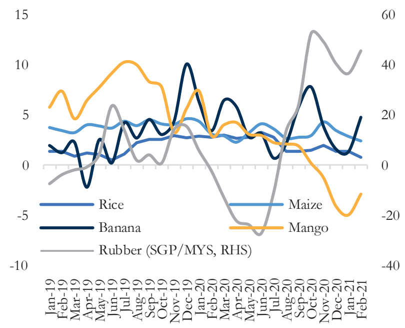

*Source:* Cambodian authorities.

**Figure 14: Dry season rice yields fluctuated**
(y/y percent change)




*Source:* Cambodian authorities.
*Note:* RHS = right-hand scale.

**Figure 15: Domestic agricultural commodity prices were volatile**
(y/y percent change)




*Source:* Cambodian authorities and the World Bank.
*Note:* RHS = right-hand scale.

14 Sreymom and Pirom. 2015.

agricultural products, expanding contract farming, and linking agricultural commodity producers with major food wholesalers and retailers in major urban centers, underpinning the (domestic) food supply chains.[15] A feasibility study on establishing ago-industrial parks has been conducted.

### The CCFTA is expected to boost agricultural performance

**The prospects of Cambodia-China Free Trade Agreement (CCFTA), which may go into effect this year, help further boost investment, and thus support overall agricultural production for exports,** especially to the Chinese market. This helps reduce the constraints the sector is facing due to Cambodia's small domestic market. China has already granted its import quota for Cambodia's (milled) rice exports of up to 400,000 tons a year since 2019. China is already Cambodia's top milled rice exports market (see below for more details on milled rice exports). In addition, new agricultural commodities such as mangos and bananas have already emerged. In 2020, Cambodia earned US$112 million or a 128 percent increase from banana exports alone. The first direct shipment of fresh mangos from Cambodia to China took place in May 2021, after Chinese Customs certified 37 mango plantations and five packaging factories on April 26, 2021. Cambodia and China signed a phytosanitary protocol for fresh mango exports to China in June 2020.[16]

### The first state-owned credit guarantee corporation was established

**In March 2021, the Guarantee Corporation of Cambodia Plc (CGCC), the first state-owned credit guarantee corporation, with initial capital of US$200 million, was established.**[17] The CGCC has launched the Business Recovery Guarantee Scheme (BRGS) which is its first credit guarantee scheme. The BRGS aims to support businesses including (micro) small and medium-sized enterprises (SMEs) and large firms to enhance their access to formal loans for both working capital and investment or business expansion. Agriculture including agroprocessing, food manufacturing and processing, is one of the priority sectors. The BRGS acts as collateral/ security for 70 to 80 percent of the loan amount borrowed by businesses from the participating financial institutions; thus, reducing the physical collateral required from borrowers. The credit guarantee scheme offered by CGCC will complement the existing loan facility provided by the Agricultural and Rural Development Bank to improve access to finance for the agriculture sector.

### Rising ocean freight rates slowed Cambodia's milled rice exports

**Cambodia's milled rice exports were struck by a surge in shipping costs as a temporary container shortage occurred.** According to the Cambodia Rice Federation, the shortage pushed up the cost of empty 20-foot and 40-foot containers several times in December 2020 and January 2021. The temporary container shortage affected rice exports, especially to Europe. Exports of agricultural commodities, especially rice, which is heavier and cheaper cargo, compared to other products such as garments and electronics, were hard hit by rising ocean freight rates. As a result, during the first quarter of 2021, milled rice exports contracted by 33.4 percent, reaching only 153,000 metric tons. While the trade safeguard measures imposed by EU on Cambodian rice will end in January 2022[18], saving rice exporters €125 per ton, high ocean freight rates will likely continue. According to the Cambodia Rice Federation, ocean freight rates stood at US$150 to US$250 per ton in May 2021, compared to US$40 to US$50 per ton in 2020.

**In 2020, Cambodia exported 690,000 metric tons of milled rice (of which 80 percent was jasmine rice) and earned US$538 million.** China is the largest market, capturing 41.8 percent of the total, up from 35.5 percent in 2019. In the first three months of 2021, China's market expanded

15 Contract farming in Cambodia increased in 2020; see https://www.phnompenhpost.com/business/hope-sprouting-growers-more-farming-contracts-inked and https://www.phnompenhpost.com/business/fifty-nine-communities-enter-agri-contracting

16 Chinese Embassy Facebook.

17 Guarantee scheme corporation of Cambodia; https://www.cgcc.com.kh/

18 The European Union imposed safeguard measures on rice from Cambodia. On January 18, 2019, the European Union reinstated the normal customs duty on Cambodia's rice products of €175 per ton in year one, progressively reducing it to €150 per ton in year two, and €125 per ton in year three; see https://trade.ec.europa.eu/doclib/press/index.cfm?id=1970.

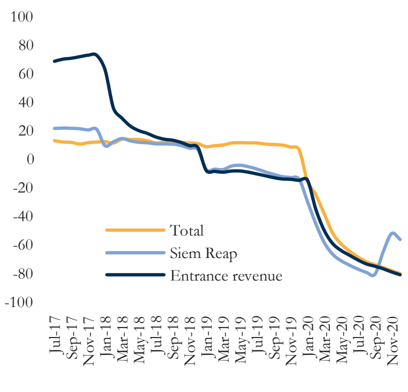
further, capturing 55.5 percent of Cambodia's milled rice exports. The EU market (including the U.K., Norway, Ukraine, and Serbia) is second. Regardless of the imposition of EU safeguard measures, the country's rice exports to the EU market marginally improved, reaching 203,000 metric tons, or 30 percent of total exports in 2020. As of end-March 2021, Free On Board (FOB) average prices of Cambodia's premium fragrant (Malys Angkor), standard fragrant, and long-grain white rice remained favorable, capturing US$820 to US$1,350, US$730, and US$540 to US$920 per metric ton, respectively.

### An unprecedented lockdown caused further detriment to the tourism industry

**The recent unprecedented lockdown has further hurt domestic economic activity, which has lately depended almost entirely on local demand after the collapse of international arrivals.** As of December 2020, international arrivals contracted by 80.2 percent year-on-year, reaching 1.31 million (figure 16). During March–April 2021, domestic travel restrictions and a lockdown were put in place due to the resurgence of community outbreaks of COVID-19. People were advised to stay home. As a result, the tourism, hospitality, retail, and transport industries have been hit hardest, given that the industries until recently depended almost entirely on domestic tourism. In 2020, more than a million local tourists visited attractions (coastal, cultural, and ecotourism zones) in the country during each major holiday, such as the Cambodian New Year, Pchum Ben, and the Water Festival, in the absence (or limited number) of foreign tourists.

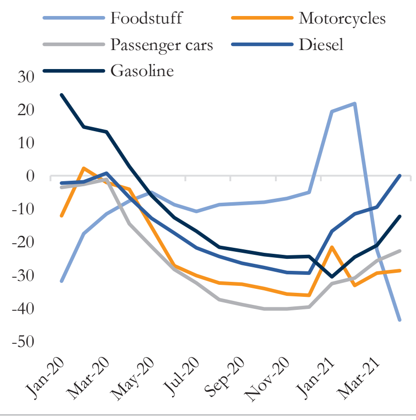
**International arrivals by air to Siem Reap, where the Angkor Temple Complex is located, contracted by 56.6 percent,** receiving only 0.7 million foreign tourists in 2020. Given the fact that the Angkor Temple Complex is the most popular destination in the country, the negative impact has been economically damaging. Consequently, revenue from entrance fees to the Complex, which reached more than US$100 million in the precrisis period, plummeted to US$18.6 million, or an 81.2 percent y/y decline. The coronavirus pandemic and local outbreaks are likely to continue for some time. Therefore, the services sector, in particular, the tourism, hospitality, retail, and transport industries, may be experiencing the longest decline in Cambodia's recent history. During the pre-pandemic period, the tourism sector was one of main drivers of growth. According to the Ministry of Tourism, tourism receipts accounted for 12.1 percent of GDP, while the sector provided 630,000 direct jobs in 2019.

**Figure 16:** **International arrivals and Angkor revenue collapsed**
(YTD, y/y, percent change)



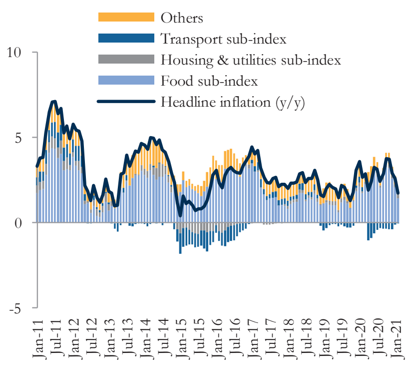

*Source:* Cambodian authorities.

**Figure 17:** **Imports of consumer goods slowly recovered**
(y/y, percent change)




*Source:* Cambodian authorities.

**Figure 18:** **Inflation was further subdued**
(Contributions to 12-month inflation (percent)




*Source:* Cambodian authorities.

### Subdued consumption was further hit by the recent lockdown

**Despite a relatively low number of coronavirus cases in 2020, domestic consumption remained weak.** In 2020, growth of imports of consumer goods and durable goods continued to be subdued and remained in negative territory. Domestic consumption was further hit by rising cases of coronarius in April 2021. As a result, imports of foodstuff contracted by 45.3 percent in the first four months of 2021, down from a 4.9 percent contraction in 2020 (figure 17), while imports of gasoline contracted by 12.2 percent and 24.4 percent, respectively. Similarly, imports of durable goods such as passenger vehicles and motorcycles contracted by 25.8 percent and 28.7 percent, respectively, in the first four months of 2021. In 2020, when travel restrictions and the lockdown were lifted, after the first wave of COVID-19 outbreaks hit Cambodia in April 2020, domestic economic activity returned, according to the findings of the Business Pulse Survey. Businesses reopened in June 2020, and by September 2020, 89 percent were open (see November 2020 Cambodia Economic Update). While more recent data are not available, it is likely that at least part of the gains reported in 2020 by the Business Pulse Survey may have been reversed, after the unprecedented lockdown was introduced in April 2021. However, contraction in imports of consumer and durable goods moderated during the first four months in 2021. Domestic consumption may be gradually recovering. As consumption accounts for about 70 percent of GDP, its recovery underpins economic growth.

### Inflation eased further as food prices decelerated

**As food prices eased, headline inflation declined further, dropping to 1.7 percent y/y in February 2020, down from 2.9 percent at the end of 2020.** In February 2021, the decline in the food subindex was largely behind the easing of headline inflation, while housing, utilities, transport, and other subindexes remained subdued. In February 2021, food prices (except for pork) eased across the food inflation basket of Cambodia's consumer price index, ranging from rice, beef, chicken, and fish to vegetables and fruit. Retail prices of petroleum products such as gasoline and diesel, however, edged up. In February 2021, the contribution of the food and non-alcoholic beverage subindex to inflation declined to 1.4 percentage points, from 2.59 percentage points during the same period in 2020, while the contribution of the housing (and utilities) and transport subindexes to inflation increased to 0.22 percentage points and a negative 0.05 percentage points, respectively, up from 0.16 percentage points and a negative 0.4 percentage points, respectively (figure 18).

**Stable exchange rates helped anchor domestic retail prices denominated in local currency.** Nominal values of the Cambodian riel vis-à-vis the U.S. dollar remained broadly within the targeted ±2 percent range (figure 19). The exchange rate remained broadly stable, reaching riel 4,072 per U.S. dollar at the end of May 2021, compared to riel 4,070 per U.S. dollar during the same period last year. In addition, nominal values of the Cambodian riel vis-à-vis the Thai baht, Vietnamese dong, and Chinese yuan were also stable. This has helped anchor prices of imported products, including those from Cambodia's neighbors, which are its main import partners.

### A surge in nontraditional exports partly helped stabilize the external position

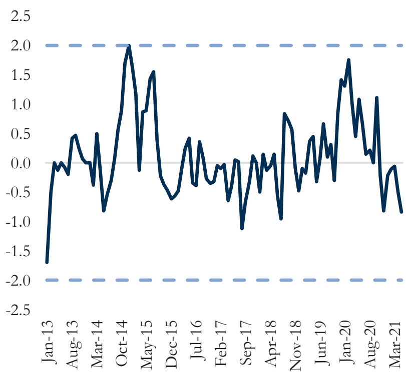
**In 2020, Cambodia's external position was stable, thanks in part to an increase in non-traditional exports.** Exports of goods (including gold) rose to US$17.2 billion or 16.7 percent in 2020. These exports included gold, agricultural commodities, bicycles, electrical parts, wire and accessories, vehicle parts and other exports. Gold exports skyrocketed to US$3.1 billion in 2020. Goods (excluding gold) exports marginally declined to US$14.5 billion, contracted by 1.1 percent in 2020. As discussed, Cambodia's exports of traditional products such as GFT products, have been affected by the global demand shock. At the same time, merchandise imports were constrained as imports of durable goods and construction materials dipped significantly as consumption eased and the construction boom stalled. As a result, the current accounts are estimated to have remained at 9.9 percent of GDP in 2020, compared to 9.7 percent of GDP in 2019. The deficit is estimated to have been fully financed by FDI inflows.

**Resilient FDI inflows fully financed the current account deficit.** In 2020, FDI inflows which reached US$3.4 billion or 13.6 percent of GDP, compared to US$3.5 billion 13.2 percent of GDP in 2019, helped sustain the external sector (figure 20). Net worker remittances, however, contracted by 13.5 percent in 2020. Cambodia's stable external position allowed the central bank to further accumulate international reserves. Gross international reserves rose to US$21.2 billion by the end of 2020 or 13.1 percent, equivalent to more than 10 months of prospective imports. Underpinned by continued capital inflows, foreign exchange reserves, which constitute the majority of Cambodia's gross international reserves, expanded in 2020. (figure 21).

## Monetary policy easing continued

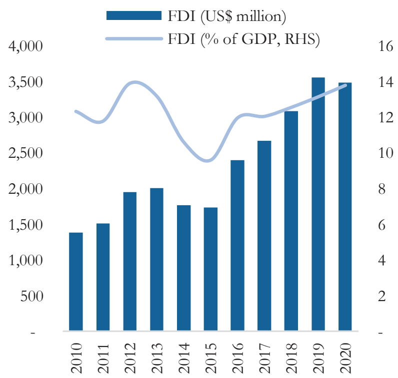
**The central bank continues to support liquidity.** The National Bank of Cambodia decided in its Monetary Policy Committee meeting held on February 10, 2021 to: (i) continue to maintain exchange rate stability via its exchange market intervention; (ii) provide riel liquidity via Liquidity-Providing Collateralized Operation facilities according to the riel exchange rate and liquidity conditions; and (iii) maintain a reserve requirement ratio at 7 percent for both riel and U.S. dollar deposits and borrowings until the end of the first semester of 2021, and as necessary. Subsequently, in May 2021, the central bank issued (its third round) monetary easing measures to: (i) maintain a reserve requirement ratio at 7 percent for both riel and U.S. dollar deposits and borrowings until further notice; and (ii) allow the banking and microfinance sectors to continue to restructure loans until the end of 2021,[19] In 2020, the central bank also postponed full implementation of the capital conservation buffer to maintain the 50 percent current requirement.[20] In March 2020, the central bank issued a directive to all banks and financial institutions to restructure

**Figure 19: Nominal exchange rate was broadly stable, within a ±2 percent range**
(riel per U.S. dollar, y/y percent change)



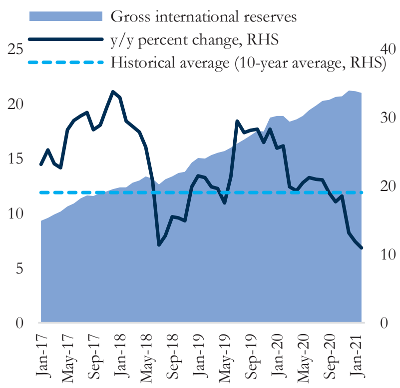

*Source:* Cambodian authorities.

**Figure 20: FDI inflows were broadly stable**
(% of GDP)




*Source:* Cambodian authorities.
*Note:* RHS = right-hand scale.

**Figure 21: Gross international reserves rose**
(US$ billion)




*Source:* Cambodian authorities.
*Note:* RHS = right-hand scale.

19 See May 21, 2021, announcement on policy easing measures (3rd round) by the National Bank of Cambodia.

20 The capital conservation buffer is designed to ensure that institutions build capital buffers under normal financial situations that can be drawn down when losses occur. See the Prakas dated February 22, 2018, and the National Bank of Cambodia's *2020 Semi-Annual Report*. See https://www.nbc.org.kh/download_files/legislation/prakas_eng/3.Prakas_on_Capital_Buffer_in_BFIs_ENG.pdf.

loans in order to maintain financial stability, while easing the burden of debtors facing major revenue declines caused by the pandemic.[21] In 2020, to mitigate the impact of the pandemic on borrowers, the banking and microfinance sectors restructured 285,000 loan accounts, amounting to US$4.2 billion.[22] Loan restructuring measures continue in 2021.[23]

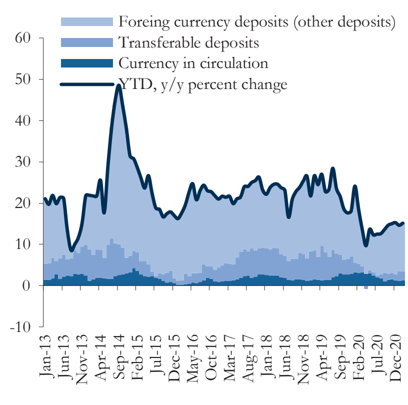
### Broad money growth remained strong as foreign currency deposits improved

**Foreign currency deposit growth, which significantly eased during the second quarter of 2020, has accelerated since, resulting in a gradual expansion of broad money (M2) growth.** Cambodia's M2 growth accelerated to 15.2 percent y/y as of February 2021, up from 9.7 percent y/y in April 2020. However, it remained below its pre-pandemic growth rate of 18.2 percent at the end of 2019. The initial recovery of broad money growth toward the beginning of 2021 was contributed mainly by rising foreign currency deposits. Of the 15.2 percent broad money growth as of February 2020, the contribution of foreign currency deposits (and other deposits) accounted for 11.7 percentage points, while transferable deposits and currency in circulation contributed only 2.2 percentage points and 1.3 percentage points, respectively (figure 22).

### Domestic credit and deposit growth stabilized as confidence improved

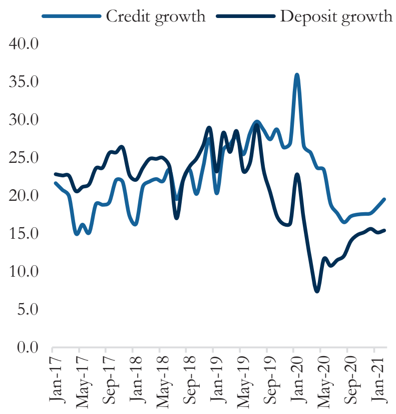
**Domestic credit growth, which fell quickly in the second and third quarter in 2020, has steadied,** likely showing increased demand for credit as the appetite for investment in the construction and real estate sector picked up (see discussion on credit by business undertakings below). Thanks to the central bank's accommodative monetary policy, domestic credit provided to the private sector picked up, expanding at 19.5 percent as of February 2021, compared to 17.7 percent at the end of 2020, as economic activity improved (figure 23). The credit-to-GDP ratio increased from 114.2 percent in 2019 to 142.2 percent in 2020. Deposit growth, which fell to 7.3 percent y/y in April 2020, picked up, increasing to 15.4 percent as of February 2021. As interest rates on deposits remained broadly stable, the recovery in deposit

**Figure 22: Broad money growth recovered**
Contribution to broad money growth (percentage point)



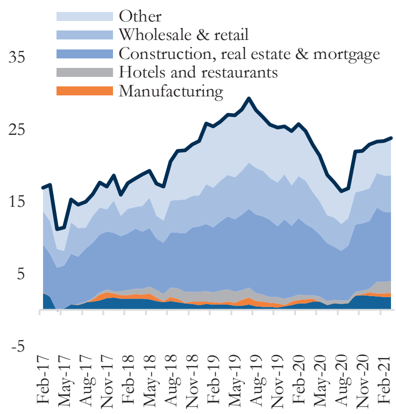

*Source:* Cambodian authorities.

**Figure 23: Domestic credit and deposits picked up**
(y/y percent change)




*Source:* Cambodian authorities.

**Figure 24: Contribution of construction to credit growth accelerated**
(percentage point)




*Source:* Cambodian authorities.

21 See Instruction Circular dated March 27, 2020, the National Bank of Cambodia. "Renegotiated loan" or "Restructured Loan" means any loan that has been rescheduled or refinanced in accordance with an agreement setting forth a new repayment schedule on a periodic basis occasioned by weaknesses in the borrower's financial condition and/or inability to repay the loan as originally agreed.

22 National Bank of Cambodia 2021.

23 Joint statement by the Association of Banks in Cambodia and Cambodia Microfinance Association, April 7, 2021.

growth likely reflected increased confidence and a recovery of economic activity that positively impacted liquidity of the corporate sector (and households), thus expanding their ability to save. In addition, domestic credit financing the construction and real estate sector accelerated, indicating a renewed appetite for investment in the construction and real estate sector. After hitting a 2.5-year low, dropping to 6.9 percentage points in August 2020, the contribution of the construction and real estate sector to domestic credit growth once again accelerated, accounting for 9.6 percentage points in March 2021 (figure 24). As of March 2021, there was a total of US$10.5 billion in outstanding credit provided the construction, real estate, and mortgage sectors.

**Agricultural lending rose—a healthy development—thanks to an increased appetite for investment in the agriculture sector driven by good agricultural commodity export prospects under the CCFTA** (and by efforts to contain imports during the pandemic). As of December 2020, there was a total of US$2.4 billion in outstanding credit provided the agriculture sector, up from US$1.95 billion at the end of 2019. In 2020, the contribution of agricultural lending to credit growth rose to 1.9 percentage points, up from 0.5 percentage points in 2019. As of March 2021, agricultural lending rose further to US$2.54 billion in outstanding credit, or 23.1 percent y/y. The sector also received US$50 million in financing from the state-owned Agriculture and Rural Development Bank in 2020. Under the 2021 budget law, US$82 million is allocated to the state-owned bank.

**Lending to the hospitality industry decelerated, mirroring the downfall of the tourism sector which has been hit hard by the pandemic.** In 2020, the contribution of the hotel and restaurant industry to credit growth eased to 0.5 percentage points, down from 0.9 percentage points in 2019, while the contribution of the manufacturing sector increased to 0.6 percentage points, up from 0.2 percentage points during the same period. At the end of 2020, the reported nonperforming loan ratios remained low at 2.7 percent and 1.8 percent for the banking sector and microfinance sectors, respectively.[24] However, given the continued loan restructuring process offered by banks and microfinance institutions, the reported nonperforming loan ratios may not correctly reflect the level of debt distress facing the banking and microfinance system.

**Interest rates of U.S.-denominated loans and deposits remained broadly stable as of March 2021.** The U.S.-denominated term deposit rates remained unaffected at 3.3 percent per year in March 2021, compared to 3.2 percent in December 2020. During the same period, the U.S.-denominated term loan rates stood at 8.9 percent a year and 9.1 percent a year, respectively. Due to Cambodia's highly dollarized economy, the central bank cannot influence interest rates, especially those of U.S.-denominated loans and deposits.[25]

## Poverty is estimated to have increased regardless of the government's response

**Negative impacts of the pandemic on poverty linger, while the authorities continue to help households smooth consumption and firms avoid bankruptcy.** The authorities' unprecedented cash transfer program has been supporting the livelihoods of the poor and the vulnerable. The new cash transfer scheme for poor and vulnerable households has seen increased demand. As of January 2021, 710,929 households, or 19.5 percent of all households, have received a cash transfer from the government. In early June 2020 when the program began, there were only 560,000 households eligible. As of October 2020, more than 640,000 households had received a cash transfer.[26] However, employment activity is showing signs of recovery. According to the survey of households, the percentage of respondents who were employed in December 2020, returned to the level recorded in May and August 2020, but remained below its pre-pandemic level (see box 3 for more detailed findings of the survey. While the share of households reporting declines

24 National Bank of Cambodia 2021.

25 However, the central bank introduced a lending rate cap at 18 percent per year in March 2017. See Prakas number B7-017-109 PK dated March 13, 2017. See https://www.nbc.org.kh/download_files/legislation/prakas_eng/Prakas-on-Interest-Rate-Cap-Eng.pdf

26 Presentation by the Ministry of Social Affairs, Veterans and Youth Rehabilitation on October 22, 2020.

Box 3:

## Impacts of COVID-19 on households—results from the High-Frequency Phone Survey of Households[1]

**Employment has yet to return to pre-pandemic levels,** according to the High-Frequency Phone Survey of Households. Prior to the COVID-19 outbreak, 82 percent of respondents were working. Following the onset of the pandemic, 71 percent of respondents were working in May 2020, and this remained relatively unchanged until October, when there was a further decline in employment to 65 percent. Employment increased to 72 percent in December 2020.

**The negative impacts of the COVID-19 pandemic on non-farm family businesses remain substantial, with weak consumer demand driving the losses in business revenues** (figure B3.1). In December 2020, more than half of households operating non-farm businesses (58 percent) reported having made "less" or "no revenues" relative to the previous month. Although there was a significant reduction in the share of non-farm business households reporting having "less revenues" or "no revenues" in May 2020 (81 percent), there has been no further reduction since October 2020 (54 percent).

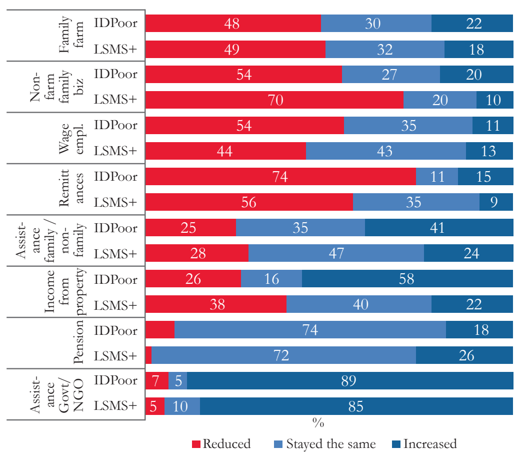
**While the share of households reporting declines in household income has slowed since May 2020, about one in two households continued to report that their household income had declined relative to the last survey.** Slowing declines in labor income and the provision of the government's cash relief transfers to assist poor and vulnerable households during the COVID-19 crisis appear to have helped mitigate some of the losses.

**Since the launch of the nationwide COVID-19 relief transfer program in June 2020, there has been a marked increase in the share of Identification of Poor Households (IDPoor) receiving social assistance from the government, mostly in the form of cash transfers.** By December 2020, 93 percent of eligible IDPoor households had received relief cash transfers, and most of them had received multiple payments. Beneficiaries of the COVID-19 cash transfers largely spent their cash on food.

**Food insecurity remained unchanged between October and December 2020.** Among the Living Standards Measurement Study Plus (LSMS+) sample, the prevalence of moderate or severe food insecurity was 17 percent in December, which includes 0.5 percent of the population affected by severe food insecurity. This is compared to 17 percent of moderate or severe insecurity and 0.7 percent of severe food insecurity in October. Among IDPoor households, there was a statistically insignificant (at the 95 percent confidence interval) decline in the prevalence of moderate or severe food insecurity from 39 percent in October to 34 percent in December.

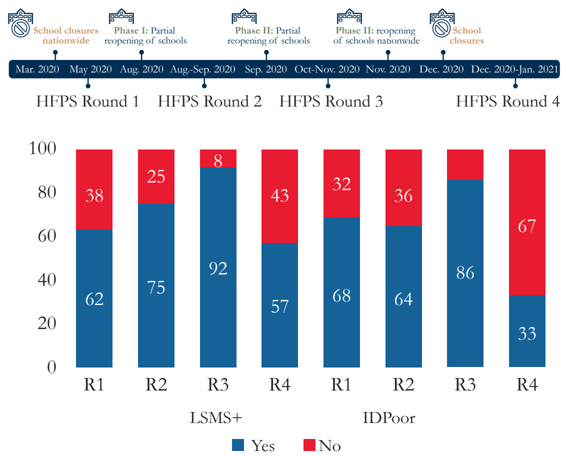
**Children's engagement in learning activities declined due to the school term holiday and the second nationwide closure of schools on November 30, 2020, following a local COVID-19 outbreak** (figure B3.2). The proportion of households with school-age children aged 6–17 engaged in learning activities declined from 92 percent in October—when it had reached pre-pandemic levels—to 57 percent in December 2020. Unlike the first nationwide school closure where instruction shifted to remote settings while the academic term progressed, the second school closure cancelled the remainder of the 2019–20 academic year for public schools and suspended in-person instruction for private schools for two weeks while e-learning was applied during this period.

**Figure B3.1. Changes in income by source since November 2019**
(percent)




*Source:* High-Frequency Phone Survey of Households in Cambodia.

**Figure B3.2. Children engaged in education or learning activities in the last 7 days**
(percent)




*Source:* High-Frequency Phone Survey of Households in Cambodia.
*Note:* R = round.

*Note: 1.* Karamba et. al (2021), The Socioeconomic Impacts of COVID-19 on Households in Cambodia: Results from the High-Frequency Phone Survey of Households Round 4 (17 December 2020-12 January 2021), Phnom Penh, Cambodia or the link of the full brief Monitoring the Impact of COVID-19 on Households in Cambodia.

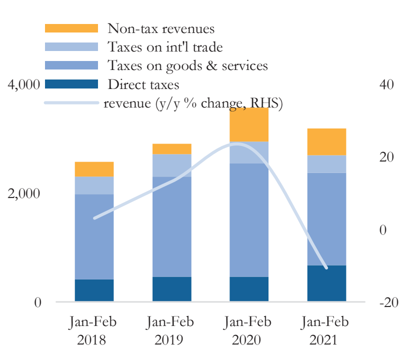
in household income has slowed since May 2020, about one in two households continued to report that their household income had declined relative to the last survey. Children's engagement in learning activities declined due to the school term holiday and the second nationwide closure of schools on November 30, 2020 following a local COVID-19 outbreak. The proportion of households with school-age children aged 6–17 engaged in learning activities declined from 92 percent in October—when it had reached pre-pandemic levels—to 57 percent in December 2020.

### Revenue collection slowed further as impacts of the pandemic were felt

**Revenue collection, which was relatively strong in 2020 when ballooned profit taxes for 2019 were filed, started to slow as negative impacts were felt.** During the first two months of 2021, central government revenue reached 3.18 trillion riels, or a 10.6 percent year-on-year contraction, due largely to a decline in taxes on goods and services as consumption faltered (figure 25).[27] Tax revenue, which includes taxes on goods and services; taxes on profits, income, and capital gains; and taxes on international trade, collected during the first two months of 2021 amounted to 2.68 trillion riels or an 8.7 percent decline. This was due to the decline in taxes on goods and services, and taxes on international trade, while direct taxes remained resilient. Similarly, non-tax revenue shrank, reaching 0.69 trillion riels, a 19.8 percent year-on-year contraction.

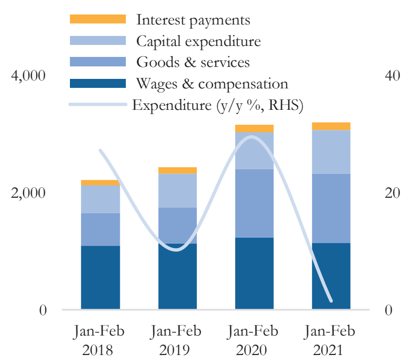
**Despite intervention, central government expenditure remained contained,** amounting 3.19 trillion riels or a 1.5 percent year-on-year increase during the first two months of 2021 (figure 26). Total expenditure was driven largely by capital expenditure which increased by 18.2 percent y/y in the first two months of 2021, while wages and compensation remained subdued, declining by 6.8 percent during the same period. In 2021, the share of externally funded capital spending shrank to 19.0 percent of total expenditure or 49.2 percent of total capital spending, due largely to the domestically financed capital spending boost. It is the first time that domestically financed capital exceeded externally financed capital. Public sector wages continued to be contained. The authorities' target of having a minimum civil servant's monthly wage of at least 1 million riels has been met or exceeded. In addition, responding to the pandemic has required a substantial increase in public outlays, reducing authorities' fiscal space for raising civil servants' wages much further. Due to the continued government intervention program, spending on social benefits and subsidies combined, increased to 913.8 trillion riels (figure 27), a rise of 17.4 percent y/y during the first two months of 2021.

**Figure 25: Central government domestic revenue eased**
(billions of riels)



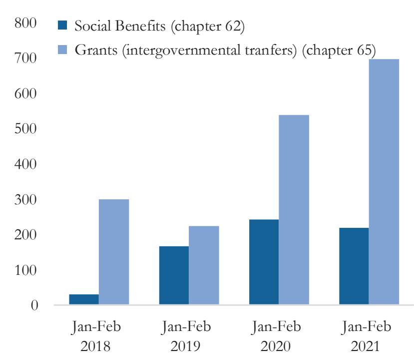

*Source:* Cambodian authorities.
*Note:* RHS = right-hand scale.

**Figure 26: Central government expenditure slowed**
(billions of riels)




*Source:* Cambodian authorities.
*Note:* RHS = right-hand scale.

**Figure 27: Social benefits and grants rose**
(billions of riels)




*Source:* Cambodian authorities.

27 Ministry of Economy and Finance, February 2021 Government Finance Statistics.

**The authorities extended the cash transfer program through March 2021,** after quickly introducing and scaling it up in June 2020.[28] As of January 2021, the cash transfer program benefited 710,929 poor and vulnerable households (2.8 million people), of which 6,421 households were in Phnom Penh, 32,693 were from other urban areas, and 671,815 were from rural areas. The cash transfer program amounted to an estimated US$300 million in 2020. In 2021, the cash transfer program is budgeted at US$200 million. Cambodia has been able to quickly scale up and deepen the nascent cash transfer program, which was barely in place in the pre-pandemic period. A decision by the authorities to provide emergency relief in the form of cash transfer to families with COVID-19-related deaths and infected as well as poor residents in lockdown areas was issued May 2021 and effective in June 2020.[29]

**Lessons have been learned from Cambodia's rapid deployment, expansion, and deepening of its social assistance program,** particularly the cash transfer system. (See the Special Focus section on government-to-person (G2P) payments for social benefits.**)** The Special Focus section presents the key findings of a study on social benefit payments under the government-to-person (G2P) initiative, which assesses the payment system set up for the COVID-19 relief transfer program and draw lessons learned from the G2P payments for the current and future social assistance programs and beyond.

### Government intervention is budgeted at US$719 million

**The 2021 budget for government intervention is US$719 million (compared to US$823 million in 2020),** of which the wage subsidy program of US$59 million is allocated to provide partial wage subsidies of US$40 per month, together with technical/soft skills training for furloughed workers in the tourism and garment industries. Cash for work of US$160 million provides jobs in rural areas through construction, upgrade, and maintenance of rural roads, drainage systems, and small-scale irrigation. The cash transfer program of US$200 million pays monthly cash grants to poor and vulnerable individuals who are registered in the government's Identification of Poor Households (IDPoor) database. There is a reserved COVID-19 outbreak prevention and treatment fund of US$30 million to upgrade prevention and detection facilities and to cover all costs for COVID-19-related treatment for Cambodian citizens. Necessary financing to the SME sector is provided through an SME financing facility of US$270 million, a reserved contingent fund.

### The overall deficit continued to be financed by current savings and external borrowing

**Continued spending pressures keep public expenditure elevated, while revenue collection has slowed, resulting in the widening of the overall fiscal deficit.** However, the deficit is expected to be fully financed by the government's current savings (without resorting to domestic bank financing) and external borrowing. The overall fiscal deficit in 2020 is estimated to have widened but remained at a moderate level of 2.7 percent of GDP in 2020 (figure 28). Despite an unprecedented increase in COVID-19-related spending, estimated at 4 percent of GDP, efforts were made to contain expenditure with a reduction in spending on goods and services and other nonpriority spending. Total expenditure increase is, therefore, estimated to have been moderate, rising to 26.8 percent of GDP in 2020, up from 25.5 percent of GDP in 2019. In addition, the impact of the pandemic on domestic revenue was lessened by ballooned profit taxes for 2019, which were collected in April 2020.

**In 2021, total revenues and grants are expected to ease further, declining to 22.7 percent of GDP,** down from an estimated 24.1 percent of GDP in 2020 (and 27.0 percent of GDP in 2019). Despite continued government intervention, budgeted at 2.6 percent of GDP, total expenditure is also projected to moderate, falling to 26.0 percent of GDP in 2021, compared to an estimated 26.8 percent of GDP in 2020, thanks to the budgeted decline in spending on goods and services. Under public expenditure rationalization measures, spending on goods and services has recently been cut and is projected to

28 Announcement on the outcome of the national social protection council dated March 3, 2021.
29 A decision by the Ministry of Economy and Finance and the National Social Protection Council dated May 13, 2021.

halve, falling to 3.1 percent of GDP in 2021, down from estimated 6.5 percent of GDP in 2020.[30] The overall fiscal deficit is therefore projected to marginally widen to 3.3 percent of GDP in 2021, compared to 2.7 percent of GDP in 2020.

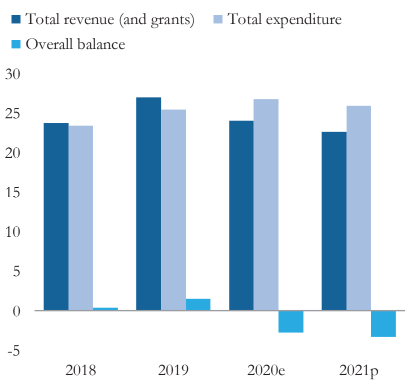
**In 2021, the deficit is expected to remain fully financed by external borrowing of 4.2 percent of GDP, and by domestic financing-drawdown of government deposits of 0.3 percent of GDP,** while debt amortization accounts for 1.2 percent of GDP (figure 29). To finance the gap between revenue collection and financing requirements, the authorities continue to tap into their current savings–-drawdown of government deposits in the banking system. While remaining solid, accounting for 24.1 percent of GDP (or 24.9 trillion riels) at the end of 2020, government deposits significantly eased. Deposits grew at 4.6 percent (y/y) in 2020, down from 47.2 percent in 2019 (figure 30), due to a slowdown in revenue collection and thus a deceleration of government savings accumulation. Cambodia experienced a prolonged decline in government deposits during 2009–11, when public expenditures shot up, rising to 23.0 percent of GDP in 2011, up from 16.1 percent of GDP in 2008 (see Annex) as the authorities introduced a fiscal stimulus to mitigate the negative impacts of the 2008–09 global financial crisis (as well as other spending boosts caused by the Cambodia-Thailand border dispute and other factors).

**Cambodia has managed to greatly boost revenue collection in recent decades thanks to its success in revenue mobilization under its public financial management reform program.** As a result, the authorities have accumulated a relatively large fiscal space in the form of government savings, while continuing to maintain prudent fiscal management and a stable macroeconomic performance.

### Rising domestically financed capital during the pandemic boosted total capital spending

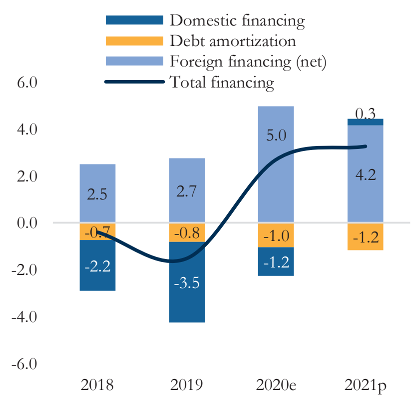
**Since 2019, efforts have been made to significantly boost public capital investment in physical infrastructure, while public investment management and debt management reforms have accelerated.** Until a few years ago, Cambodia heavily depended on external funds, which included both loans and grants financed by its development partners (official creditors) to fund its capital investment, especially its physical infrastructure. However, Cambodia's domestically financed capital has been boosted since 2019 (figure 31). In September 2020, the government approved an allocation of US$150 million to develop physical infrastructure, consisting of 38 roads in Siem Reap to be ready

**Figure 28: The general government overall fiscal deficit widened** (% of GDP)



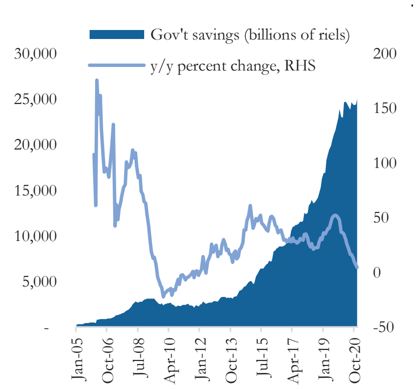

*Source:* Budget settlement laws and World Bank staff estimates and projections.
*Note:* e=estimate, p=projection.

**Figure 29: Foreign borrowing financed the fiscal deficit** (% of GDP)




*Source:* Budget settlement laws and World Bank staff estimates and projections.
*Note:* e=estimate, p=projection.

**Figure 30: Government savings remained solid** (billions of riels)




*Source:* Cambodian authorities.
*Note:* RHS = right-hand scale.

30 Instruction circular dated May 4, 2021, on expenditure rationalization and efficiency strengthening for 2021 budget, Ministry of Economy and Finance.

by the end of 2021.[31] A similar public investment project, amounting to US$ 300 million to build 34 roads with a combined length of 82.5 kilometers was approved in 2019 to develop physical infrastructure in the seaside province of Sihanoukville. The project is complete.[32] In 2021, domestically financed capital is expected to exceed (or be equal to) externally financed capital for the first time. As a result, Cambodia's public investment is the largest in the region (figure 32). Efforts to reform public investment management (PIM) have intensified. The 2019–25 Public Investment Management System Reform Strategy (PIMSRS) was introduced in October 2019. Implementation of a detailed action plan for the PIMSRS began in March 2020. A technical working group for preparation of detailed guidelines on the project cycle and the project development facility for public investment management has been operational since June 2020. Preparations have been made to develop government securities (see the section on the domestic debt market for a more detailed discussion).

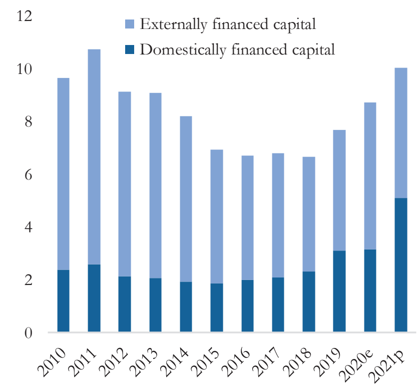
**Cambodia's gross fixed investment rose quickly after the economy recovered from the global financial crisis in 2009** (figure 33). Gross fixed investment reached 24.6 percent of GDP in 2020, up from 16.2 percent of GDP in 2010 as economic growth accelerated. The share of private investment in total investment rose to 64.6 percent, up from 32.8 percent in 2011, reflecting continued investor confidence. While countercyclical public investment is important to economic recovery, private investment is also key for the revival of the private sector. Rising gross fixed investment helps underpin economic recovery and sustain economic growth.

### Cambodia's public debt rose, but risk of debt distress remains low

**In 2020, the authorities signed US$2.02 billion in concessional loan agreements (74 percent of the debt ceiling) with their development partners,**[33] compared to US$1,288.27 million signed in 2019. As impacts of the pandemic continue, the gap between revenue collection and financing requirements is widening. To partly finance the widening gap, Cambodia's public debt is increasing. The country's public debt, which consists solely of external debt, is rising. Cambodia's debt-to-GDP ratio reached 34.2 percent of GDP (US$8.8 billion in outstanding debt) in 2020 and is projected to increase to 35.2 percent of GDP (US$9.6 billion) in 2021 (figure 34).

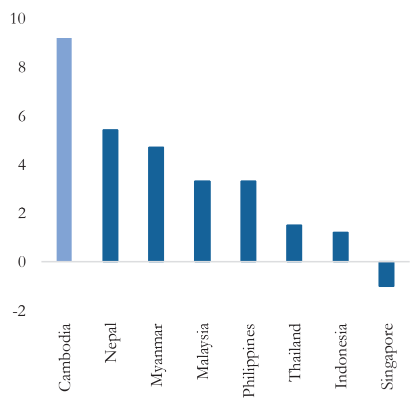
**Risk of debt distress, however, remains low, due largely to the authorities' borrowing**

**Figure 31: Public investment is rising**
(% of GDP)



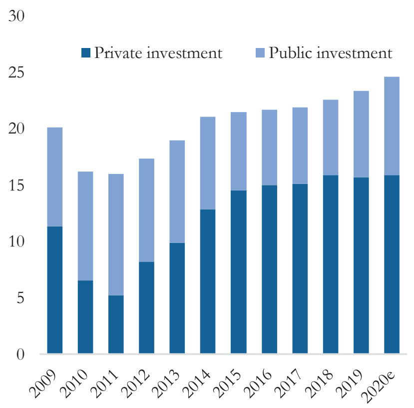

*Source:* Cambodian authoriites.
*Note:* e=estimate, p=projection.

**Figure 32: Cambodia's net investment in nonfinancial assets is large**[1]
(% of GDP, 2019)




*Source:* World Development Indicators and Camobodian authoriites.
*Note:* 1 Cambodia 2020, the rest is 2016.

**Figure 33: Gross fixed investment rose**
(% of GDP)




*Source:* Cambodian authorities.
*Note:* e=estimate.

31 See a letter dated September 4, 2020 from Siem Reap provincial governor to the prime minister.
32 See news release dated July 17, 2020 by National Committee for Managing and Developing Cambodian beaches.
33 Cambodia *Public Debt Statistical Bulletin*, Volume 11, March 2021.

**principle of only contracting external debt on concessional terms.** The debt sustainability analysis (DSA) conducted by the authorities in 2020 concluded that Cambodia's risk of debt distress remains low. There is as yet no joint World Bank/International Monetary Fund DSA for 2020. The weighted average grant element remained relatively high: 43.2 percent (2018), 51.6 percent (2019), and 46.5 percent (2020). In 2020, external borrowing was mainly for the public infrastructure sector, which accounted for 62.6 percent, while the remaining 37.4 percent was for other priority sectors.

**China is Cambodia's largest official creditor, with a total outstanding debt of US$3.9 billion, or 44.2 percent of total debt stock.** In recent years, Cambodia has grown increasingly dependent on China for both public sector loans and FDI inflows. Unlike Cambodia, Vietnam has diversified sources of finance. Vietnam's largest creditor is the World Bank, accounting for 31.9 percent of total central government public external debt or US$15.2 billion (figure 35). Its second-largest creditor is bilateral, Japan, accounting for 30.4 percent of total central government external debt or US$14.5 billion, followed by the Asian Development Bank which accounted for 17.4 percent.

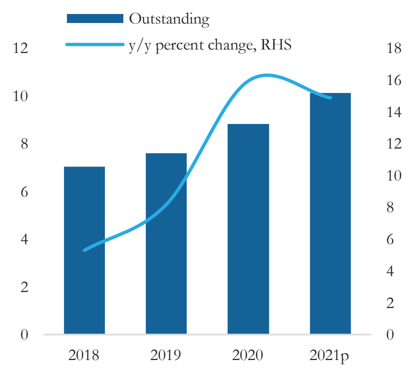
**In 2020, U.S. dollar-denominated debt was the largest, accounting for 43.5 percent of total debt stock,** followed by Special Drawing Right (SDR)-denominated debt, at 24.6 percent. Although China is Cambodia's top creditor, the country's public external debt denominated in Chinese yuan covered only 15.7 percent of total debt stock.

## Last year, loan disbursement from ADB was the largest

**Loan disbursements from a few main creditors, which include the ADB, Japan, China, and the World Bank, boosted public sector loan disbursements to Cambodia in 2020.** Total debt disbursement peaked in 2020, reaching more than US$1.2 billion, or a 40.3 percent y/y increase (table 1). Unlike during the past several years, when the largest contributions to loan disbursement growth came mostly from bilateral creditors such as China and France, in 2020, the contribution of loan disbursement by the ADB was the largest, accounting for 30.4 percentage points of the 40.3 percent increase in total loan disbursement. Disbursement from the ADB peaked at US$421.9 million in 2020, up from US$159.11 million in 2019. The contribution of debt disbursement from Japan was next, accounting for 7.6 percentage points (US$149.8 million) of the increase, followed by those from China and the World Bank, accounting 4.0 percentage points and 3.5 percentage points, respectively.

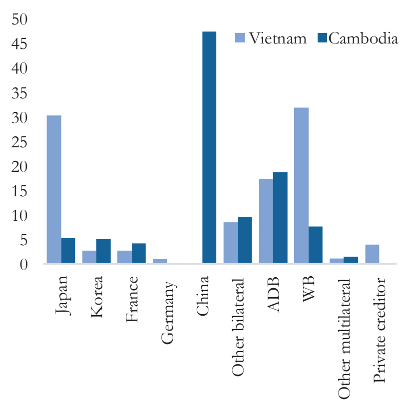
## Unlike its peers, Cambodia's public debt is entirely external

**Figure 34:** **Public debt is rising** (US$ billion)



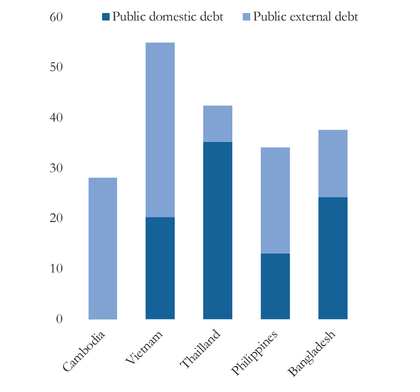

*Source:* Cambodia Public Debt Statistical Bulletins.
*Note:* p=projection, RHS = right-hand scale.

**Figure 35:** **Cambodia is heavily dependent on China as official creditor** (% share, 2019)




*Source:* Cambodia Public Debt Statistical Bulletins and Haver Analystics.

**Figure 36:** **Unlike its peers, Cambodia had no domestic public debt** (% of GDP, 2019)




*Source:* MFMod, World Bank Group.

**Cambodia's public debt comprises only external debt,** as the remaining outstanding domestic public debt of US$1.57 million was fully repaid in February 2020.[34] As discussed, the entire public debt stock is denominated in foreign currencies. Cambodia is, therefore, exposed to risks from exchange rate adjustments, while the economy is highly dollarized. Cambodia's ASEAN neighbors such as Vietnam and Thailand have already shifted to borrowing domestically. Domestic public debt accounted for 82.9 percent and 36.8 percent of total outstanding public debt in Thailand and Vietnam, respectively (figure 36).

**Cambodia is in the process of establishing its domestic debt market.** A new Law on Government Securities was adopted in December 2020, paving the way for issuance of the first government securities in the near future, establishing a domestic debt market. The 2020 Law on Government Securities provides an overall legal and regulatory framework for issuing, trading, and managing government securities with transparency, accountability, efficiency, and effectiveness, supporting public debt management and debt sustainability. It aims at strengthening cash management of the government, responding to financing requirements for socioeconomic developments. The law mandates that issuance of government securities be stipulated in the budget law and under the sole authority of the Minister of Economy and Finance to meet specified financing requirements. Cambodia has become a lower-middle-income economy. Concessional borrowing is, therefore, shrinking. The domestic debt market, when established, will help gradually diversify financing sources with a shift toward public domestic debt, while promoting domestic savings. It also helps dedollarize the economy if domestic debt issued is denominated in local currency.

## Outlook

**Cambodia's growth outlook remains highly uncertain** as the actual shape and pace of recovery is largely dependent on the course of the virus and the pace at which the vaccine can be rolled out. Therefore, we explore two scenarios: a baseline scenario, which is based on more optimistic assumptions on infection and vaccination; and a downside scenario, which assumes the realization of most of the downside risks.

**Under the baseline scenario, the economy is projected to grow by 4 percent in 2021** (table 2), supported by a gradual recovery in domestic demand following the vaccine deployment and improvement in external demand and capital inflows (see also table 3 which is an assumption matrix, under the baseline and downside scenarios, below). The projections assume that market confidence is restored, while the current community outbreaks, which began in February 2021, remain under control, resulting in a staged

**Table 1: Debt disbursements (US$ million) and contribution to debt disbursement growth** (percentage points)

| | 2014 | | 2015 | | 2016 | | 2017 | | 2018 | | 2019 | | 2020 | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | % | | % | | % | | % | | % | | % | | % |
| **Total** | 648.4 | 6.3 | 595.3 | -8.2 | 543.0 | -8.8 | 722.2 | 33.0 | 598.3 | -17.2 | 864.7 | 44.5 | 1,213.3 | 40.3 |
| **China** | 432.2 | 5.4 | 367.3 | -10.0 | 328.2 | -6.6 | 392.9 | 11.9 | 231.9 | -22.3 | 322.1 | 15.1 | 356.5 | 4.0 |
| **ADB** | 71.6 | -9.2 | 97.5 | 4.0 | 143.3 | 7.7 | 137.0 | -1.2 | 100.7 | -5.0 | 159.1 | 9.8 | 421.9 | 30.4 |
| **WB** | 34.2 | 3.6 | 2.1 | -4.9 | 7.0 | 0.8 | 15.7 | 1.6 | 23.6 | 1.1 | 61.7 | 6.4 | 92.0 | 3.5 |
| **S. Korea** | 36.9 | 0.9 | 32.1 | -0.7 | 19.7 | -2.1 | 38.5 | 3.5 | 33.9 | -0.6 | 44.7 | 1.8 | 67.0 | 2.6 |
| **Japan** | 21.9 | -0.3 | 27.5 | 0.9 | 23.6 | -0.7 | 48.9 | 4.7 | 72.8 | 3.3 | 83.8 | 1.8 | 149.8 | 7.6 |
| **France** | 27.3 | 4.5 | 38.3 | 1.7 | 0.0 | -6.4 | 72.5 | 13.4 | 47.0 | -3.5 | 147.3 | 16.8 | 47.1 | -11.6 |
| **ROW** | 24.1 | 1.3 | 30.2 | 0.9 | 21.0 | -1.5 | 16.4 | -0.8 | 88.1 | 9.9 | 45.8 | -7.1 | 78.8 | 3.8 |

*Source:* Cambodia Public Debt Statistical Bulletins, Ministry of Economy and Finance.
*Note:* ADB = Asian Development Bank; ROW = rest of the world; WB = World Bank.

34 Cambodia Public Debt Statistical Bulletin (March 2021), Ministry of Economy and Finance.

easing of the lockdown restrictions without significant mid- to long-term adverse impacts on the corporate or banking sector. FDI inflows are steadily returning. Under the baseline, it is expected that the authorities are taking steps to attract further investment and promote trade by introducing a new investment law in the second half of 2021, boosted by the recently signed free trade agreements. Under Cambodia's economic recovery plan, efforts are underway to boost competitiveness through investment climate and business environment reforms and leveraging of digital technologies. The authorities are pursuing a countercyclical fiscal policy with a continued social protection program, while boosting public investment. Public debt and budget pressures have risen sharply and are likely to persist, and the authorities will need to consider options for restoring fiscal discipline once the recovery takes hold.

**Under the downside scenario, the economy is projected to grow at 1.0 percent in 2021.** The downside scenario assumes a deterioration in domestic economic conditions caused by repeated lockdowns and travel restrictions as

**Table 2: Macro outlook** (baseline)

| | 2020e | 2021p | 2022p | 2023p |
|---|---|---|---|---|
| National Accounts and Prices | | | | |
| GDP at constant market prices (% change) | -3.1 | 4.0 | 5.2 | 6.0 |
| Agriculture | 0.4 | 1.1 | 1.0 | 1.3 |
| Industry | -1.4 | 6.7 | 7.4 | 8.5 |
| Services | -6.2 | 2.6 | 4.8 | 5.4 |
| Inflation, consumer prices (annual %, period average) | 2.9 | 3.0 | 3.0 | 3.0 |
| General Government (% of GDP) | | | | |
| Revenue and grants | 24.1 | 22.7 | 23.1 | 23.8 |
| Expenditure and net lending | 26.8 | 26.0 | 27.1 | 27.0 |
| Overall balance (including grants) | -2.7 | -3.3 | -4.0 | -3.2 |
| Foreign financing | 4.8 | 4.2 | 4.1 | 4.1 |
| Net domestic financing (from current savings) | -1.0 | 0.3 | 1.1 | 0.3 |
| Amortization | -1.0 | -1.2 | -1.2 | -1.2 |
| Money and credit | | | | |
| Broad money (% change) | 15.3 | 20.0 | 21.4 | 21.0 |
| Credit to the private sector (% change) | 17.7 | 23.2 | 25.8 | 28.1 |
| External Sector (US$ million unless otherwise specified) | | | | |
| Exports (goods and services) | 15,853 | 18,844 | 20,361 | 22,857 |
| Imports (goods and services) | 16,221 | 19,981 | 21,616 | 23,963 |
| Foreign direct investment, net inflows | 3,485 | 3,750 | 4,160 | 4,249 |
| Gross official reserves | 21,228 | 23,140 | 25,026 | 27,272 |
| (months of imports) | 10.4 | 9.5 | 9.3 | 9.0 |
| Current account (percent of GDP) | -9.9 | -9.8 | -10.2 | -9.7 |
| Exchange rate (Khmer riel per US$ average) | 4,077 | 4,070 | 4,050 | 4,050 |
| Total public debt (% of GDP) | 34.6 | 35.2 | 36.9 | 36.4 |
| *Memorandum items:* | | | | |
| Nominal GDP, US$ million | 25,484 | 27,215 | 29,749 | 32,524 |

*Source:* Cambodian authorities and World Bank staff estimates and projections.

*Note:* e = estimates; p = projections

efforts to contain the outbreaks are not successful, preventing economic recovery from taking hold, regardless of improvements in external conditions. Containment efforts drain public resources while deployment of the vaccination program is assumed to have progressed slowly. Consequently, market confidence is subdued, leading to a marked slowdown in FDI inflows, while the main export-oriented manufacturing sector such as GFT goods is disrupted by repeated lockdowns and impacted by the partial withdrawal of the "Everything But Arms" arrangement and temporary expiration of the Generalized System of Preferences. The fiscal deficit widens, as spending pressures rise, while domestic revenue declines sharply, caused by prolonged and sluggish domestic economic activity. As public debt and budget pressures persist, external borrowing and drawdown of the

**Table 3: Assumption matrix under the baseline and downside scenarios**

| Assumptions | Baseline | | Downside | |
|---|---|---|---|---|
| **Length, duration, and intensity of the lockdowns** | Lockdowns are few, brief, localized and only confined to Q2 of 2021 for pockets of urban areas. | | Lockdowns are frequent, prolonged, nationwide and may extend to Q3 of 2021. | |
| **Pace of vaccination** | Already going well, with 13.6% vaccinated – second highest in ASEAN after Singapore (as of end-April 2021). | | Vaccination drive is met with public health human resource constraints. Consequently, the country will not reach herd immunity until late 2022. | |
| **Government's response** | Strong counter-cyclical policies | | Same as baseline | |
| **Speed of global recovery and return of international tourism** | Speedy recovery in the United States, Europe, and China—Cambodia's three major trading partners. | | Same as baseline | |
| **Economic conditions** | Vaccines are successfully administered as targeted, leading to a restoration of market confidence, while FDI inflows continue, attracted by the new investment law and CCFTA (and RCEP) and a relocation of factories as political tensions in Myanmar persist. There are moderate adverse effects affecting corporates as goods exports (including agricultural exports) recover, thanks to improvements in external demand conditions. Efforts under the economic recovery plan are currently underway to boost competitiveness through investment climate reforms and leveraging of digital technologies. Although public debt and budget pressures have risen, the authorities will be able to restore fiscal discipline once the recovery takes hold in the short term. | | Market confidence is subdued, leading to a marked slowdown in FDI inflows, while the main manufacturing sectors such as garment, footwear and travel goods for exports are disrupted by lockdowns and impacted by the partial withdrawal of the "Everything But Arms" arrangement and temporary expiration of the Generalized System of Preferences, regardless of improvements in external demand conditions. Consequently, significant adverse effects resulting in liquidity problems become solvency problems affecting corporates. The fiscal deficit is expected to double as spending pressures rise and domestic revenue declines caused by prolonged sluggish economic activity. Rising public debt and budget pressures persist, requiring more external borrowing and drawdown of the government's current savings. | |
| **Macro projections** | **2021** | **2022** | **2021** | **2022** |
| **Real growth** (percent) | 4.0 | 5.2 | 1.0 | 4.5 |
| **Fiscal deficit** (percent of GDP) | -2.7 | -3.3 | -5.0 | -6.5 |
| **Debt stock** (percent of GDP) | 35.2 | 36.9 | 36.5 | 38.0 |

government's current savings increase, requiring more time before fiscal discipline can be restored.

**In the post-pandemic world, Cambodia's economy will likely follow a new trajectory** (a new normal), expanding rather moderately in the short term. Cambodia's economy is tourist-dependent. Regardless of a recovery in domestic tourism after the easing of lockdowns, global tourism is expected to remain below pre-pandemic levels until 2023. Global economic recovery, supported in part by the significant U.S. stimulus, will revive trade in goods and could provide an external boost to growth of as much as 1 percentage point on average, but global tourism is expected to remain below pre-pandemic levels until 2023, which will delay economic recovery in tourism-dependent economies. A structural change, driven by a diversification of FDI projects which were earlier concentrated largely in the construction and real estate sector to non-garment manufacturing and agricultural commodity exports appears to be emerging, adapting to changes in domestic economic and external demand conditions.

## Challenges and risks

**Risks to Cambodia's growth outlook have intensified as the current wave of coronavirus outbreaks lingers.** Domestic economic activity has recently been disrupted by the reintroduction of a lockdown during the second half of April 2021. The lockdown, which was imposed on the two largest urban centers–-Phnom Penh and Takhmao, the second-most populated city in Kandal province–-was necessary and saved lives, though it may also have been economically damaging. The current high infection rate is also threatening the public health system. Factories and businesses were affected, while domestic demand, especially for services products such as domestic travel, tourism, and hospitality services, were once again hit by travel restrictions, travel avoidance, and declining incomes. This will likely be a drag on growth until wider vaccine deployment.

**Cambodia's growth model—characterized by a narrow export base with a high degree of concentration of products and markets—exhibited weaknesses years before the pandemic hit.** While the country has a well-established, labor-intensive, and export-oriented garment industry, the manufacturing sector has for decades remained largely engaged in the "cut-make-trim" process, the lowest value-added section of the entire value chain. The country's external competitiveness eroded, partly caused by rapidly rising wages—made worse by a dollarized economy—and exacerbated by challenges in doing business and investment climate reforms. The vulnerabilities, however, were masked by a surge in capital inflows in the pre-coronavirus crisis period to largely finance the construction and real estate sector. With the collapse of the tourism sector and the stalled construction boom, the pandemic has exposed Cambodia's structural weaknesses.

**Along with domestic weaknesses, an uncertain global outlook remains a key risk to Cambodia's recovery.** Delays in global vaccine distribution could lead to the persistence of the pandemic, while outbreaks trigger more lockdowns. Cambodia's merchandise exports will likely be further impacted by partial withdrawal of the "Everything But Arms" arrangement and temporary expiration of the Generalized System of Preferences. In addition, Cambodia is increasingly dependent on China in trade, investment, and official development assistance. High credit growth in the banking sector, particularly to the construction and real estate sector, remains a key risk to Cambodia's financial stability.

**Following a local outbreak that started on February 20, 2021, Cambodia has experienced rapidly rising reported coronavirus cases and deaths.** As of May 31, 2021, there were 30,094 cases and 214 deaths. The pandemic threatens to reverse years of extraordinary development gains in the country. In the absence of significant mitigation measures, the COVID-19 pandemic could result in sharply rising unemployment and increased poverty. Poverty simulations based on macroeconomic projections show that a sharp economic slowdown would produce a substantial increase in poverty of between 5.4 and 6.0 percentage points. This translates into between 859,000 to 950,000 additional poor and a reversal of six years of progress against poverty. Of these, households relying on non-agricultural wages, particularly construction workers, will be hit hardest by the outbreak.

## Policy options

**It is urgent to accelerate implementation of the vaccination program, while continuing to effectively contain the rise in infection cases and deaths.** Given potentially lingering outbreaks across the country, the benefits of rapid vaccination in reducing growing numbers of hospitalization and deaths, while relieving pressures on the struggling health system will outweigh its costs. Non-pharmaceutical interventions can also play a complementary role in the containment of the disease. Of a population of more than 15 million, over 10.1 million Cambodians are aged 18 and older and may need to be vaccinated. Thus, Cambodia needs over 20 million doses of coronavirus vaccine for this age group alone. According to the national COVID-19 vaccination strategic plan, the country expects to obtain 13.5 million doses, or about 66 percent of the needed vaccines for the age group by September 2021. The plan targets to fully vaccinating about 5 million people under the first priority group during May to November 2021, a period of seven months, with about 10 million doses of coronavirus vaccines. As of end-April 2021, about 2.4 million doses of the vaccines have deployed. So, the plan should achieve an average of 1.1 million doses per month during May to November 2021 to completely deploy the remaining 7.6 million doses. A masterplan for COVID-19 vaccination published in March 2021 by the Ministry of Health targets vaccinating 10 million people by mid-2022.

**Given the country's relatively large fiscal space, further boosting pro-poor and growth-enhancing public investment, including cash-for-work projects, is critical for economic recovery.** In this regard, the 2021 budget has boosted domestically financed public investment which, for the first time, exceeds externally financed public investment. More efforts are needed, however, to improve the business and investment climate, especially to facilitate the structural change, as the construction boom has stalled and more investment is now going into production to serve mostly exports, while shoring up confidence with introduction of the new investment law, taking advantage of the CCFTA and RCEP. As the economy is highly dollarized, fiscal policy will continue to be the sole macroeconomic instrument to support relief, recovery, and growth. Relief continues to be needed, especially for poor and vulnerable households. Recovery requires improvements in the investment climate and incentives to spur investment and to boost exports because the COVID-19 shock threatens to lock the economy into an underemployment equilibrium. Growth requires further public investment to improve the quality of both hard (physical) and soft (regulatory) infrastructure to reduce transport and logistics costs in order to boost external competitiveness.

**It is imperative to continue to closely monitor vulnerabilities arising from a prolonged property boom and the increase of credit provided to the construction sector during the pre-pandemic period.** The loan-to-deposit ratio had already reached 120 percent in 2020, up from 78.7 percent a decade ago. This is particularly crucial as current community outbreaks linger and the number of factories and firms being severely affected are rising. Such events are likely to further diminish the ability of businesses and households to repay loans, putting the entire financial sector under increased stress. The authorities recently called on housing developers to accept delays in mortgage payments. The total value of loans and affected borrowers' accounts that need to be restructured will likely increase further this year, from last year's reported 285,000 accounts with a total of US$4.2 billion or 11.2 percent of total outstanding credit of the banking and microfinance sectors. Of this US$4.2 billion, US$1.73 billion, or 41.5 percent, was provided to affected borrowers engaged in the construction, tourism, and transport (and logistics) sectors combined. As these sectors continue to be hit hard by lingering local outbreaks, demand for loan restructuring from the sectors will certainly increase further. Non-performing loans are expected to rise from their current low levels of 2.7 percent and 1.8 percent for the banking sector and microfinance sector, respectively, in 2020. The central bank needs to continue to closely monitor financial risks, focusing on liquidity conditions, capital, and quality of credit together with the current macroprudential measures in place as discussed in the monetary section above.

# Special Focus:

# Government-to-Person (G2P) Payments for Social Benefits

# SPECIAL FOCUS: GOVERNMENT-TO-PERSON (G2P) PAYMENTS FOR SOCIAL BENEFITS[35]

## INTRODUCTION

As discussed in the macroeconomic section above, Cambodia has been able to quickly scale up and deepen its cash transfer program, which was barely in place pre-COVID-19. Thanks to the current social assistance program, Cambodia has so far been able to prevent millions of people from falling back into extreme poverty, which could potentially reverse decades of hard-won gains in reducing poverty.

To gather lessons learned from Cambodia's relatively swift introduction, rapid expansion, and deepening of its social assistance program, particularly the cash transfer program, the World Bank is undertaking a study on government-to-person (G2P) payments for Cambodia's social benefit system. Key findings of the study discussed below provide insights on the (G2P) payments for the current and future social assistance programs and beyond.

## RGC RESPONSE TO THE COVID-19 PANDEMIC

**Cambodia's national social assistance programs were at a nascent stage when the COVID-19 pandemic hit.** Until 2018, Cambodia spent around 0.05 percent of its GDP on social assistance—one of the lowest in the world. Cambodia launched its first national social assistance program, the Official Cash Transfer Program for Pregnant Women & Children, using identified poor (IDPoor) families. The program, announced in June 2019, was formally established through a sub-decree and became effective in January 2020. By February 2020, when the pandemic hit, the program had reached approximately 80,000 beneficiaries, or about 0.5 percent of the population.

**In response to the challenges created by COVID-19, the Royal Government of Cambodia (RGC) established a comprehensive response and fiscal stimulus package.** The response was aimed at addressing the health, social, and economic impacts of the crisis. The government introduced, among other things, social protection of poor and vulnerable groups and economic measures that include wage subsidies and tax relief for businesses in hard-hit sectors, a Cash for Work program to create job opportunities in rural areas, a support facility to small and medium-sized enterprises (SMEs), and low-interest loans to struggling businesses through the newly established SME Bank and the Agricultural and Rural Development Bank.

**Social assistance has been massively scaled up to the poor and vulnerable households, leveraging the existing IDPoor database to deliver relief cash transfers to registered IDPoor households.** Based on the CTP-PWYC as a model for delivering immediate relief assistance (see box S.1), the cash transfer program has been the largest component of the government's support package. Launched in June 2020, the program has disbursed US$230.5 million in cash transfers as of February 2021.[36] The program is currently expected to continue at least until June 2021 and to disburse around US$30 million in cash transfers per month. The program has reached over 688,000 households (2.7 million individuals) or about 17 percent of the population, which is a dramatic increase compared to the pre-COVID-19 level of social assistance in terms of both reach and coverage.

35 This Special Focus was prepared by Marco Nicolì. The author wishes to thank Maheshwor Shrestha, Robert J. Palacios, and Biagio Bssone for their inputs and suggestions.

36 Though initially introduced as a two-month program in June 2020, the program has been extended multiple times. Currently, the relief transfers are expected to continue until June 2021, which could potentially be extended depending on the circumstances.

Box S.1.

## CAMBODIA'S SOCIAL PROTECTION RESPONSE TO COVID-19

Bracing for the economic impact of COVID-19, the Royal Government of Cambodia moved quickly to fund and scale up a cash transfer program for poor households. Before COVID-19, as of early 2020, 506,000 households (approximately 15 percent of the population) were identified as poor through the country's poverty identification system known as the IDPoor program, thereby qualifying for a number of social services. Developed within the Ministry of Planning (MOP) since 2005, the IDPoor system uses a participatory community approach combined with a poverty scorecard to identify households living in poverty. Until 2019, a third of provinces conducted the extensive community-led process each year, ensuring all urban and rural areas were covered during a three-year period. Since 2011, all services for poor people have been legally required to use IDPoor to target beneficiaries. Currently, households with an IDPoor "equity" card can access several national programs, such as free access to health care under the Health Equity Fund, financial assistance via the Cash Transfer Program for Poor Pregnant Women and Children (zero to 2 years old) (CTP-PWYC), and the Scholarship Program for Children in Primary and Secondary Schools.

The social protection response to the COVID-19 crisis built on the existing infrastructure of the CTP-PWYC. Any IDPoor equity cardholder can register with an administrator at the commune level and receive an account from an e-payment provider (see box S.3). The cash transfer program is implemented primarily by the Ministry of Planning (MOP) and the Ministry of Social Affairs, Veterans and Youth Rehabilitation (MoSVY) with support from the Ministry of Interior. The MOP is responsible for beneficiary identification through IDPoor, including making data on eligible households available to the MOSVY, which manages registration, benefit calculations, and payment processes.

Due to a high level of commitment from local stakeholders, the IDPoor program has switched to an on-demand system (OD-IDPoor) to identify the poor, led by the communes. This process led to the registration of over 560,000 households by June 2020, and the number continues to increase. As of March 2021, over 710,000 households (2.8 million individuals) were eligible to receive the cash transfer benefit.

*Source: Policy in Focus, The International Policy Centre for Inclusive Growth, Volume 19, Issue No. 1, March 2021.*

**The relief cash transfer program provides benefit amounts based on locality, poverty status, household demographics, and vulnerability.** The benefit levels depend on locality (rural or urban), level of poverty (IDPoor 1, the extreme poor; or IDPoor 2, poor), and household size. An additional amount is provided for vulnerable groups that include people with disabilities, the elderly above age 60, children under age five, and people living with HIV/AIDS. The information relevant to the determination of the benefit amount is collected as part of the IDPoor program and is present in the database. On average, each household received about US$45 per month.

**The rapid rollout has been challenging, yet successful.** The government (through relevant ministries) has been working closely with development partners to ensure affordability and to develop a comprehensive implementation plan including identification, registration, linking to mobile payment systems, and building the capacity of at least 30,000 program implementers and commune officials to ensure prompt delivery of this social assistance program.[37] This was the first time a social protection program has covered such a large proportion of the population (as defined by IDPoor), and was achieved in a remarkably short time through an effective, ad-hoc payment mechanism (see next section). Indeed, survey data show that relief transfers reached over 95 percent of eligible households (that is, IDPoor households).[38]

37 Development Policy Letter from Dr. Aun Pornmoniroth, Deputy Prime Minister and Minister of Economy and Finance of the Kingdom of Cambodia, to the President of the Asian Development Bank, June 16, 2020.

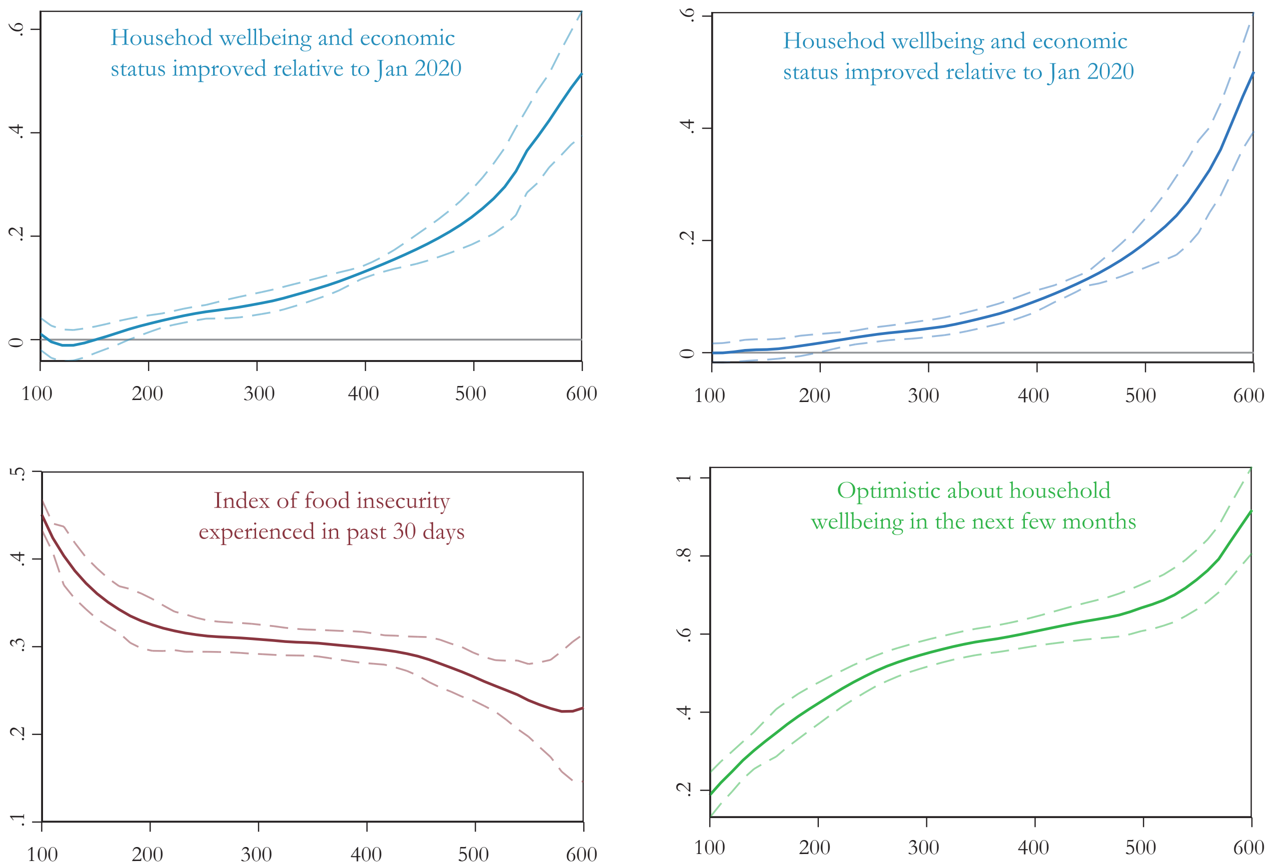
38 Independently conducted phone-based surveys by the World Bank also find similar levels of reach among the eligible population (World Bank 2021, forthcoming).

**Consequently, the relief transfer program has had a large positive impact among the recipients.** Forthcoming analysis by the World Bank finds that the relief transfers were highly valued by the recipients. Seventy-eight percent considered the transfers to be either extremely important or very important to their well-being. A similar share reported that the transfers mattered a lot for their well-being. Furthermore, households that received larger transfers are more likely to have better living conditions (figure S.1) and are more likely to report an increase in household well-being compared to the pre-pandemic (January 2020) or pre-relief (June 2020) period. They are also less likely to report food scarcity and to have a more optimistic outlook about their well-being in the coming months.

## SOCIAL ASSISTANCE DELIVERY PROGRAM: PAYMENT MECHANISM

**The payment mechanism of the program relies on the services of Wing, a leading mobile payments provider in Cambodia, and its network of more than 9,000 payment agents across the country.** Eligible beneficiaries (heads of household) register for the program with their IDPoor cards in the presence of commune council members (who verify household identity) and activate an account. The account is not a full-fledged mobile money account; it does not require a phone number and is dedicated exclusively to the transfer program. Beneficiaries then visit a Wing agent and set up a personal identification number (PIN), which allows them—along with their IDPoor card—to collect cash at a Wing agent every month. Wing is given automated access to relevant fields of the IDPoor database via an Application Programming Interface (API), so that each account can be associated with every owner's IDPoor number and receives government money to fund cash collection by beneficiaries (figure S.2).

**Figure S1: Household well-being increases with higher amounts of received relief transfers**




Cumulative amount of relief transfers received (US$)
*Source: World Bank (2021, forthcoming).*

**The program has been largely successful in effectively delivering funds to the beneficiaries.** The payment mechanism was designed with the sole purpose of delivering cash rapidly to beneficiaries, as cash was the quickest option available in the country. Technology has helped the pre-delivery phase, in a context that was constrained by mobility restrictions and social distancing.

**The distribution of funds was remarkably smooth given the circumstances.,** Some challenges were encountered during implementation, especially in the initial stages, but these seem to have affected a minority of transfers. The most frequently reported challenges included implementation aspects (unstable internet connection, issues with timely handling of complaints, limited monitoring capacity); issues at the level of the Commune office (limited capacity of some commune officials or untimely replacement of trained officials, not enough awareness raising, and occasional unlawful practices); and, issues at the level of the household (lack of awareness of the program, lost stolen or damaged cards, forgotten PIN, unpermitted sharing of benefit card, difficulty in withdrawing funds by non-head of households).

**A sizable share of beneficiaries needed to travel a considerable distance to receive the transfer, particularly in the mountains.** The need to physically distribute cash implies that beneficiaries need to reach the Commune first when registering and the closest Wing agent after that for each withdrawal.

**Figure S2: Benefit registration and disbursement process**

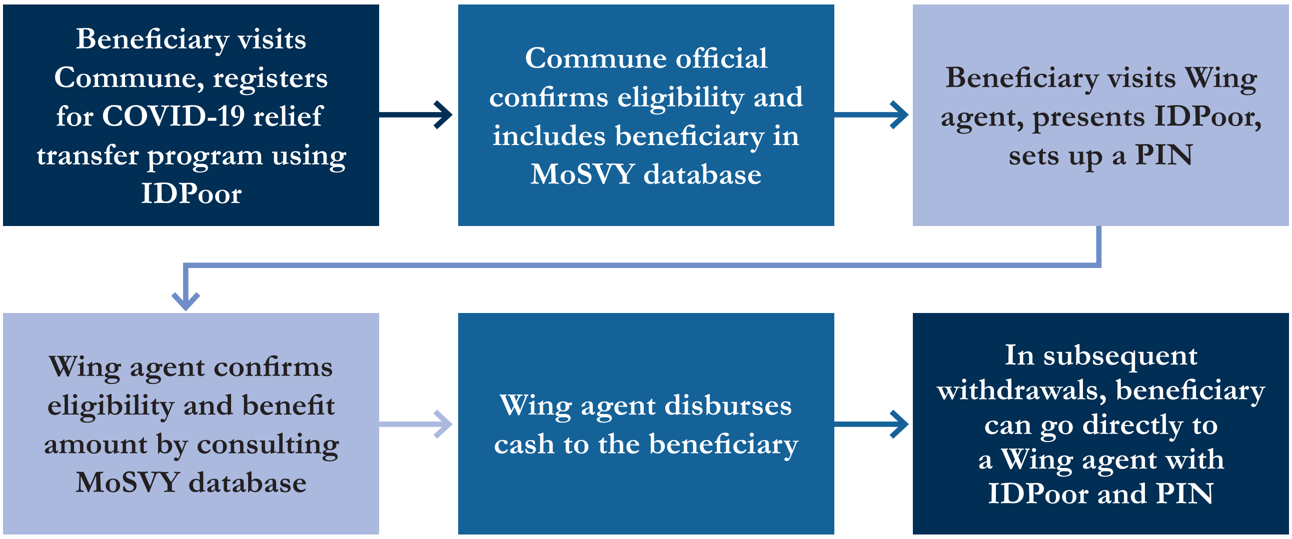



**Figure S3: Average travel time**

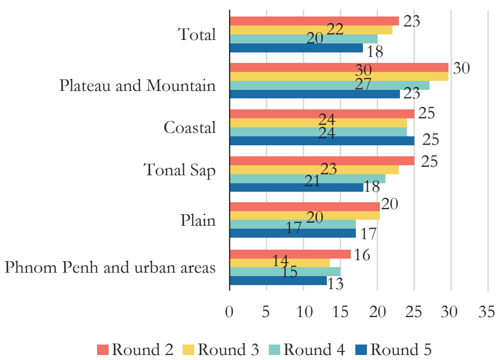
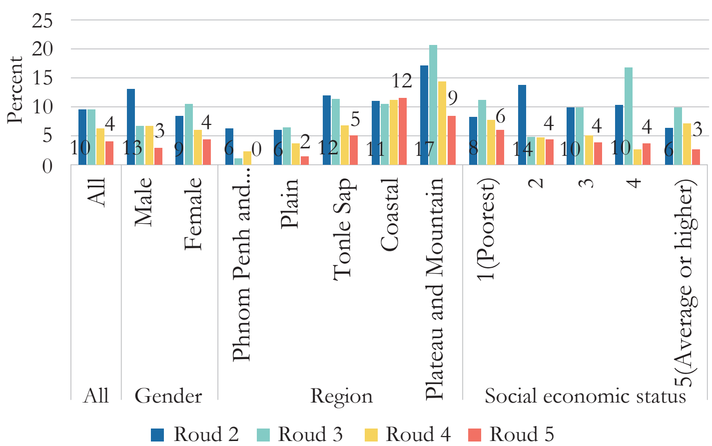



**Figure S4: Percentage of households traveling 45+ minutes Average travel time**




*Source:* Cambodia COVID-19 High-Frequency Phone Survey, World Bank, European Union, and Australian Aid, 2020–2021.

This can be a significant cost for a household when accounting for the cost of travel, the time spent, and the possible loss of opportunity / income. On average, beneficiaries had to travel 18 minutes to receive the transfer; however, in some areas they had to travel up to 25 minutes (see figure S.3). Four percent of beneficiaries had to travel more than 45 minutes, but this figure went up to 12 percent in some areas (see figure S.4). Preliminary analysis being undertaken by the World Bank indicates that over 15 percent of beneficiary households may live more than 10 kilometers from the nearest agent, and over 3 percent may live more than 30 kilometers from the nearest agent.

**Figure S5: Percentage of adults with a formal account**

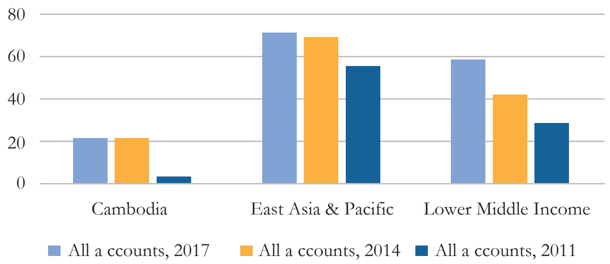



**Figure S6: Percentage of the population with an account at a financial institution or mobile money provider**

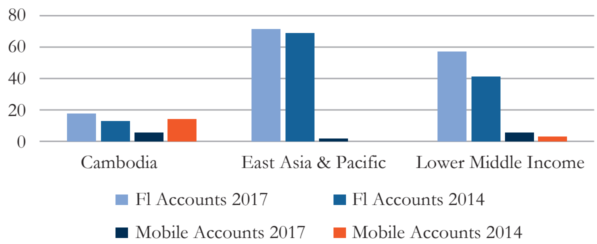
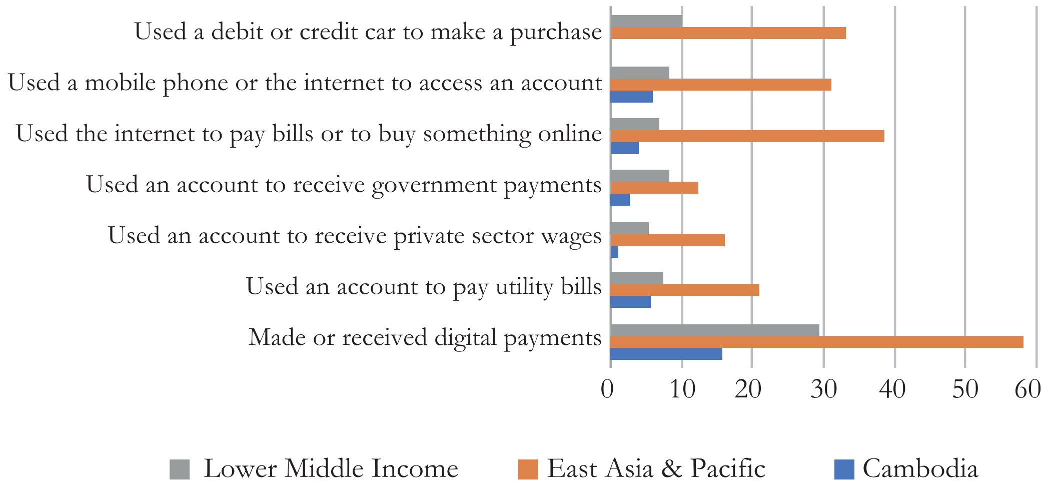



**Figure S7: Percentage of adults who have made a digital payment**




*Source:* World Bank's 2017 Global Findex Database.

**Figure S8: Do you have a payment account? (%)**

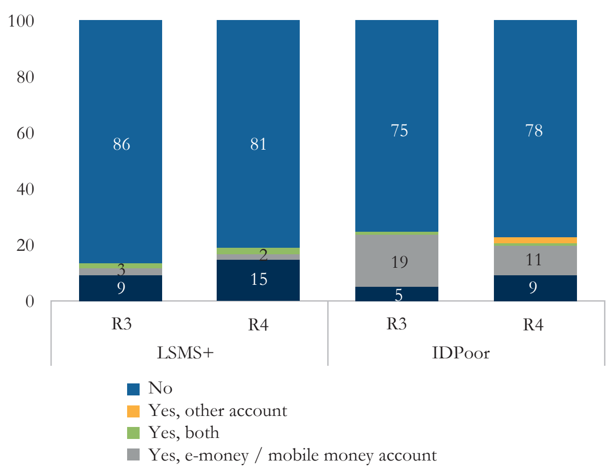
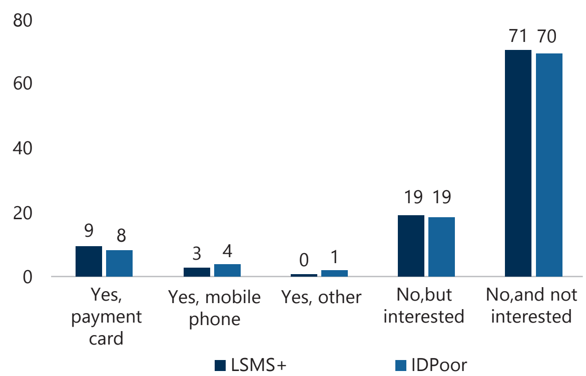



**Figure S9: Do you use anything other than cash to make payments?**




Data from round 4.

*Source:* Cambodia COVID-19 High Frequency Phone Survey, World Bank, European Union, and Australian Aid, 2020–2021.

**While the payment mechanism adopted has indeed proven effective as an immediate remedy to an emergency, some limitations should be noted that prevent it from being a springboard for future developments.** These limitations can be summarized under the following three interlinked aspects: (i) use of cash instead of digital payments, (ii) reliance on a single service provider, and (iii) missed opportunity to advance financial inclusion.

**The level of financial inclusion in Cambodia is still very low.** As shown in figure S.5, account ownership in Cambodia is one of the lowest in the East Asia and Pacific region; only 21.7 percent of Cambodians currently have access to an account compared to a regional average of 70.6 percent. When compared to other lower middle-income countries, Cambodia falls far behind the group average of 57.8 percent. While account use is low, there has been good growth over the last six years, with account ownership increasing from 3.7 percent in 2011 to the current level of 21.7 percent.[39] Figures S.6 and S.7 confirm this finding and show a very low level of adoption of digital payments in Cambodia.

**The most recent survey covering IDPoor households confirms that most of them are still unbanked and prefer to make payments in cash rather than using other payment devices** (see figures S.8 and S.9). With limited or no access to e-money facilities especially by the poor, physical cash had to be relied upon to make government funds available to people who had no alternative means to receive it.

**Demand-side elements contribute to the low levels of financial inclusion and interest in digital payments in Cambodia.** Financial literacy levels are low, especially among the low-income population. In a recent survey,[40] the share of respondents who answered five out of seven financial knowledge questions correctly, which is considered the minimum target level, was 17 percent (compared to 26.6 percent in Vietnam, another low-scoring country). The basic financial needs are satisfied by cash and cash-based services such as over-the-counter person-to-person payments. Even in urban areas where

**Box S.2.**

### Retail Payment Systems in Cambodia

**The retail payment infrastructure of Cambodia is developing rapidly, but the overall landscape has not yet taken a clear configuration, as various initiatives are in place and some of them overlap to some extent.** The introduction of the National Clearing System operated by the National Bank of Cambodia (NBC) has been one of the main drivers for the growing use of interbank credit transfers in Cambodia. In 2016, the NBC—in cooperation with commercial banks and deposit-taking microfinance institutions—established Fast and Secure Transfer (FAST), a payment system for low-value credit transfers, which offers 24/7 processing of funds (denominated in Cambodian riel) and ensures availability to the receiver in close to real time. The system is open to the participation of banks, Payment Service Institutions (PSI), and Micro Deposit-taking Institutions (MDI). The system is still characterized by very low volumes and values of transactions, and not all banks are actively using its services, largely due to investment cost issues.

**The NBC is soft launching the Retail Payment System (RPS), in cooperation with a select group of banks and one MDI.** The RPS consists of three retail payment mechanisms (Real-Time Fund Transfer, Mobile Payment System, and QR-Code Payment System) and an Electronic Clearing System for the electronic transfer of funds. The main purpose of the RPS is to promote innovation in the retail payments space, improve interbank transactions, accelerate operational efficiency, enhance fund transfer security, and promote financial inclusion.

**The NBC is promoting interoperability of domestic debit card payments by establishing the Cambodian Shared Switch (CSS).** The CSS aims to enable central clearing for all banks and other financial institutions, thereby increasing the convenience and reducing costs for customers and members of the switch. The CSS is also intended to support e-commerce transactions and innovative payment instruments and to increase the number of people with access to financial services.

**Finally, the NBC is piloting the Bakong system,** a wallet-based platform employing a permissioned distributed-ledger technology (DLT) network. Bakong is currently designed for the execution of very small, low-value transactions.

39 World Bank Findex; https://globalfindex.worldbank.org/sites/globalfindex/files/countrybook/Cambodia.pdf.
40 Morgan and Trinh 2017.

e-commerce is growing and digital financial services are becoming increasingly available, cash-on-delivery is often preferred to digital payment options.

**At the same time, several supply-side factors seem to be hindering rather than stimulating demand.** For instance, acceptance of digital payments is still limited, and merchants have little incentive to accept cashless payments. Quick response (QR) codes, which are becoming prevalent in the region as a lower-cost way to quickly increase acceptance, are also being adopted in Cambodia; however, fragmentation and lack of interoperability are a concern. Pricing for some services may also be too high, especially for low-value transactions,[41] although additional data and analysis are needed to confirm this. Innovation in some segments of the market, such as payments aggregation, gateway, and other back-end services, is limited.

**The payment system infrastructure in Cambodia has been developed significantly by the National Bank of Cambodia (NBC) over the last few years, but it remains fragmented and cannot support the effective delivery of social benefits.** As described in box S.2, the NBC has launched and operates several retail payment systems. However, the fragmentation in the infrastructure still leaves Cambodia without a system that is well-established and that has broad enough participation to be considered a viable solution for the distribution of government benefits or other government payments in the country.

**In this context, the only available option to disburse funds quickly and effectively to those in need was indeed to leverage an existing network of agents to disburse physical cash.** Wing has the most extensive territorial reach across the country, to which they were also able to add a commitment to set up new agents in any location that would not be well serviced in the first place. However, despite Wing being a provider of digital payment services, its innovative potential could not be fully put to use beyond the mere cash-out transaction.[42] Moreover, moving forward, exclusive reliance on a single provider for the distribution of social benefits and other government payments clearly risks reinforcing the dominance of that one provider in the market.

**Box S.3.**

### The market for retail payment services in Cambodia

**In recent years, Cambodia has been experiencing rapid growth in the payments and financial technology ("Fintech") industry.** Enabled by NBC's new regulations, both banking and non-banking institutions have introduced a wide array of payment and money transfer options for individuals and businesses. By the end of 2018, 16 PSIs were granted licenses by the NBC to operate payment services, including money transfers in and out, bill payments, retail payments, online payments, and cross-border money transfers. Some of the more notable market players include Wing, True Money, Asia Wei Luy, PayGo, and PiPay.

**Competition among PSPs appears to be strong with no significant barriers to entry for new providers.** With 41 banks, 16 PSIs, and 4 specialized bank there is a healthy number of providers in the market, offering a range of digital payment products. Many of the banks have launched or are in the process of launching mobile and online banking services for both personal and corporate customers.[43]

41 The cost of making very low-value transactions, across multiple use cases can be as expensive as 38 percent of the value of the transaction. This is exorbitant and could discourage lower-income individuals who are likely to send smaller amounts from using digital channels to do so (World Bank 2019).

42 It is worth noting here that a large part of transactions through the Wing network – also beyond social transfer – still consist of cash-based overt-the-counter payments. The COVID19 pandemic seems to have somewhat accelerated growth of fully digital transactions, but several challenges remain (consumer literacy and trust, smartphone penetration, adequate use cases etc.).

43 The National Bank of Cambodia – Financial stability Review https://www.nbc.org.kh/download_files/publication/annual_rep_eng/FSR-for-publication-final-22Apr2019.pdf

In conclusion, the solution that was adopted, though practical given the circumstances, is anything but ideal for modernization, since it does not contribute to financial inclusion, does not provide beneficiaries with choices, and risks distorting competition in the payments market.

**Lessons can be distilled from the experience of the COVID-19 relief transfer with a view to undertaking future reforms of GPPs, as the National Social Protection Council is already in the process of doing.** These include:

- A program whose delivery mechanisms are essentially centered on the role of the heads of households, who may be the least prepared members of society to accept and use digital instruments, cannot be conducive to digitalization. More will need to be done to communicate with the youngest segments of the population about future program developments.
- Greater efforts will have to be coordinated at the national level to promote the use of digital payment services and discouraging the use of cash, including through education and awareness initiatives on how to access and use digital payment services, how to use mobile wallets through mobile phones, and how digital channels enable users to make transactions, from transferring money to receiving salaries and financial assistance electronically from the government.
- At the same time, it will be necessary to improve existing payment infrastructure and to use it more efficiently (the cases of Thailand[44] and Jordan, see box S.4, could be helpful references from this perspective). These and other measures discussed in the next section should be considered strategically as ways not only to further strengthen the resilience of the economy and society to crises, but also to modernize GPP delivery services as part of a fast-developing economy, like Cambodia, and more broadly to facilitate access for all its population to digital financial services.

**Box S.4.**

### The Case of Jordan: Lockdown but not shutdown

In Jordan, the government and some of its key institutions seized the opportunity to shift financially excluded individuals to the realm of digital finance, increasing financial inclusion and the acceptance and spread of digitalized services. In the early days of the pandemic, the government announced its adoption of digital payment channels to replace cash, encouraging citizens and employers to use mobile wallets to conduct financial transactions. The Ministry of Labor called on employers to digitize the payment of salaries that were paid in cash before the pandemic.

What made this transition to digital finance relatively smooth is the solid digital payments infrastructure in the country. Two key national institutions (the National Aid Fund and the Social Security Corporation) announced that aid and other types of payments would be made through bank or mobile wallet transfers only. Digital financial services, more specifically mobile wallets, took prominence in mid-March 2020, especially given the growing fear of contagion through contaminated cash.

Jordan resorted to mobile payments. Many governmental and nongovernmental entities introduced mobile payments to beneficiaries to replace previously cash-based payments. As a result, the number of active mobile wallets in the Kingdom doubled over four months to over 1 million users.

*Source:* JOPACC 2020.

44 The example of Thailand's "Leave No One Behind" Income Compensation Program for Informal Workers could be useful in this respect. In Thailand, people could apply online and verify themselves using their national ID, subject to cross-checks from the Ministry of Finance to ascertain whether the national ID numbers submitted were active in other registries, indicating that the applicants should be excluded because they were formal workers or received other benefits. Government payments were made in the PromptPay national e-payment system to the accounts linked to the national ID numbers. (This information is preliminary and based on a World Bank internal study still in progress.)

## POLICY RECOMMENDATIONS

### Improving the social assistance landscape in Cambodia

**The COVID-19 relief transfer program has shown how effective social assistance can be in combating the adverse effects of the pandemic.** Even after the pandemic ends, the impacts will linger. As the relief program ends, Cambodia will need to develop stronger social assistance programs to support the poor and vulnerable population, who are adversely affected by the current pandemic as well as other economic shocks and vulnerabilities in the future. The following steps could help move Cambodia in that direction.

**Increase the coverage of the IDPoor program.** The current relief cash transfer program was limited by the scope of the IDPoor database, which covered fewer than one in five households. The adverse impacts of the pandemic extend beyond the 17 percent of the households currently identified by the IDPoor program. Among those excluded there may be near-poor or vulnerable households, micro-entrepreneur households, those working in the tourism sector, those relying on migrant incomes sent by their family members, and so on. The lack of a database with broad coverage, beyond the IDPoor database, limited the ability of the government to target social assistance more efficiently and effectively.

**Develop an IDPoor database as a registry of potential beneficiaries for all social programs.** An expansion in coverage of the IDPoor program will need to be accompanied by additional reforms to transform this into a social registry for all social programs. The necessary reforms include (i) modernizing the scoring system (such as using a proxy means test to generate welfare scores) to achieve a finer classification of households into various levels of poverty and vulnerability; (ii) linking the program to the national identification system and other administrative databases; and (iii) introducing shock response and vulnerability elements into the IDPoor instruments so that social programs can further target specific groups.

**Ensure the adequacy of existing program benefits.** While receiving social assistance is important, the adequacy of the benefits is also important for effective social assistance. As seen above, the impact of social assistance increases with the amount of the transfer, and low transfer amounts may not be effective. For instance, the CTP-PWYC provides US$190 to women for seeking pre- and postnatal care over the course of three years. While the benefits may elicit health-seeking behavior, they are inadequate to improve maternal and child nutrition. Larger program benefits would be much more effective at supporting the poor and vulnerable to get out of poverty.

**Institute evidence-based social assistance to support the poor and the vulnerable.** The relief program provided a good opportunity for Cambodia to learn about the importance and effectiveness of social assistance. The demand for sustained social assistance is evident. The RGC is currently planning to institute post-COVID-19 social assistance measures. The design of such programs and the parameters of support should be based on global as well as contextual evidence on their benefits and efficacy in supporting the poor and the vulnerable.

### Improving G2P payments in the current scenario

**As mentioned, the COVID-19 relief transfer program was effective in reaching a large number of beneficiaries within the short time available, dictated by the emergency.** Some improvements could be considered for similar endeavors in the near future, assuming the current scenario is largely unchanged from a regulatory, infrastructure, and financial inclusion, and education perspective.

**The National Bank of Cambodia (NBC) should be considered an important stakeholder when discussing G2P payment mechanisms.** The NBC is the overseer of the National Payments System (NPS). As such, the NBC should ensure the smooth, safe, and efficient functioning of the NPS, of which G2P payments are also a part. The NBC's voice is particularly relevant in guiding other RGC agencies through the available options for disbursing G2P payments to identify the most efficient alternatives. This should also include how to leverage the NPS infrastructure (that is, the systems operated by the NBC). Also, given the magnitude of G2P programs, the NBC should assess the potential impact of the payment mechanism on competition in the payments market. Finally, the NBC should bring the financial inclusion perspective, as G2Ps payments are considered among the effective use cases that could help expand financial inclusion.[45]

**Greater effort should be made to consider more than one provider for the distribution of G2P payments.** When distributing G2P payments, an effective go-to option is often to leverage the agent network of the largest payment service provider in the country. While achieving the objective in the short term, especially when quick scale up is of essence, this can end up having a negative impact on the market for payment services in the country. G2P payments allow the leading provider to further strengthen its position in the market, further expand its network of agents or branches, and increase trust and brand recognition among the population. This in turn can make it even more challenging for other players to emerge, thereby distorting competition in the market. Eventually, this may even end up making future G2P programs more costly, as the dominant player may then be able to negotiate higher processing fees.

**Beneficiaries could be given the option of receiving the funds digitally onto an account or wallet.** Cash is by far the preferred option of G2P beneficiaries in Cambodia, as seen above. However, distribution of social benefits should be seen as an important opportunity to advance adoption and use of transaction accounts and other financial services. G2P programs could be a unique opportunity for the RGC to promote financial inclusion in Cambodia, increasing the familiarity and trust of beneficiaries of social payments in digital instruments. While times may not be ripe for digital payment instruments to be the only (or even the default) option in Cambodia, given the low levels of financial literacy, giving beneficiaries at least the option to receive money into accounts or wallets could be a good first step.

### Improving G2P delivery: a potential future scenario

**G2P delivery could be further improved in Cambodia if a more substantial reform agenda were developed by the RGC.** By embracing a more ambitious reform agenda and increasing coordination among different authorities, the RGC may be able to significantly improve the efficiency and effectiveness of G2P delivery in Cambodia in the near future. This could be developed following a similar approach as in Indonesia, where the government, with support from the World Bank, is developing a comprehensive set of reforms (known as G2P 4.0) to improve G2P delivery mechanisms in the country.

**The NPS infrastructure operated by the NBC could be leveraged for the distribution of G2P payments in Cambodia.** The NBC operates several payment systems (see box S.2), some of which may have the capability to disburse funds into multiple bank accounts or e-money wallets at once (that is, batch payments). This feature would allow the government to disburse social benefits quickly and efficiently into the beneficiary accounts. The broad participation of banks and non-bank payment service providers in the relevant payment system would allow maximizinz the benefits of this approach. The current fragmentation of the NPS infrastructure may hinder such broad participation; hence, the NBC should review the overall architecture of the NPS holistically and strategically.

**Beneficiaries of social payments could be given a full choice of provider and payment methods.** This would stimulate competition in the market and could motivate payment service providers to develop specific products aimed at expanding their customer base among the low-income population. For instance, at some points during the distribution of COVID-19 relief transfers, the demand for savings was over 10 percent,[46] but this demand was not met by any product offering since beneficiaries could only withdraw

45 BIS and World Bank. 2016.

46 In rounds 2 and 4 of the survey, 10 and 11 percent of households, respectively, indicated they were interested in saving some of the funds received through the program. In round 5, the percentage dropped to only 3 percent, perhaps due to a worsening of the pandemic in the country. However, this makes the case for adequate product offerings even stronger, as some households could have saved in e-wallets some of the benefits received during better times. (*Source: Cambodia COVID-19 High-Frequency Phone Survey, World Bank, European Union, and Australian Aid, 2020–*2021.)

cash. At first, to ensure a smooth transition and avoid the possibility that anyone in need of funds is unable to receive them, the option to receive cash could be maintained. However, the option to receive the funds into an account should be considered the default method.

**Financial education and consumer protection should be an imperative part of this reform effort.** As new customers are reached by financial services with which they were not previously familiar, it will be critical to accompany them in the process, taking the opportunity to provide basic financial education for the beneficiaries. Consumer protection, including adequate redress mechanisms, should also be in place to ensure beneficiaries can easily resolve any issue with the service provided.

### Government payment programs in Cambodia: a strategic approach to reforms

**The experience with emergency assistance during COVID-19 is an opportunity for the RGC to reform its payment programs in the context of the review of the country's system of social benefits.** The share of individuals receiving payments from the government digitally in Cambodia is dramatically low—only 2.9 percent compared to 12.2 percent in East Asia and Pacific and 8.8 percent in lower middle-income countries.[47] **As a first step, the RGC could undertake a landscaping exercise, mapping all government payment flows (including, for instance, civil service wages, social security benefits, tax-related payments, payments to and from businesses), and identify for each flow, and for the system as a whole, the steps needed to achieve digitization.**

**Government Payment Programs (GPPs) should support the sound, efficient, and transparent management of public financial resources.** In addition, efforts to modernize GPPs should be leveraged to accelerate the development of the NPS more broadly and to promote financial inclusion. They should therefore be safe, reliable, and cost-effective. More broadly, digitizing GPPs should be a priority, requiring a concerted whole-of-government approach to implement them in the medium term.

**Governments can do a lot to support both the supply and delivery side of GPP services and to encourage the demand for such services from the public.** However, this requires using a holistic approach to GPP reform and the coordination of a large set of actions to be taken on several fronts, given the relevance of the challenges that may hamper the transition to digital GPPs.[48] An increasing number of countries have initiated the transition to digital GPPs, yet in some cases the process has been stifled by bottlenecks, including ineffective systems or inadequate policies that have limited the incentives or capacities necessary to achieve the desired objectives. Failure to resolve these issues may risk not only slowing the transition process, but also damaging the credibility of the government plans in the eyes of the citizens and weakening public confidence in payment innovations.[49]

**In the medium term, the RGC should commit to achieving the highest quality of GPP delivery.** This will include ensuring that (i) all components of GPP delivery are digitalized end to end, and (ii) all government payments from and to all individuals and businesses in the country reach the right party,[50] for the right purpose, at the right time, in the right place, and in the right form, in a safe and efficient manner, and in the correct amount; and (iii) GPPs evolve over time so as to promptly satisfy the changing needs of the economy and society. **The following recommendations describe how this ambitious, yet realistic, vision could be achieved in the medium term in Cambodia.**

**An integrated approach should link the transition to digital GPPs with NPS modernization and financial inclusion, in the context of Cambodia's economic development and financial stability.** This implies that as Cambodia develops its NPS infrastructure (especially the retail segment) and pursues financial inclusion, the transition to digital GPPs should be considered as a key pillar supporting both

47 World Bank Global Findex 2017.

48 For a comprehensive discussion of these challenges and how they have been addressed in selected country cases, see Karandaaz Pakistan (2016).

49 Structural weaknesses such as poor connectivity (causing numerous instances of dropped or failed transactions), the lack of account-to-account interoperability (reducing the space of payments across the economy), or an insufficient network of cash-out points across the country may severely diminish the value proposition of digital GPPs.

50 In the case of G2P payments, a party is an individual or legal person; in the case of P2G, a party would be a government agency.

objectives.[51] Similarly, the government should act strategically and involve all relevant NPS and financial inclusion stakeholders both to ensure full consistency among GPP plans, NPS development, and financial inclusion, and to exploit maximum synergies from their integration.

**In principle, the full business process of digital GPP delivery can be digitalized, not just its payment component.** Digitalizing payments, only, would not be enough to generate the full efficiency gains that are expected from the transition to digital GPPs, since people receiving or making payments from or to the government might still need to spend unnecessary time submitting paper documents (such as certificates, forms, records) and having such documents validated by government officials. In situations like that, electronic payment solutions would not eliminate the need for consumers to go to government offices and stand in long lines, which diminishes the value of electronic payments.[52] Nor do electronic payment solutions by themselves fully address governance and control issues (for example, protection from misuse of funds, fraud, or corruption), as they merely shift the point at which unauthorized third parties or criminal actors may skim off part of the funds exchanged. Instrumental to achieving the strategic objective as operationalized above is that GPPs be made "end-to-end digital," that is, the exchange of value underpinning them should be digital from initiation to fund transfer to settlement and disbursement.[53] This requires that the transition to digital GPPs be coordinated with the e-government agenda, so that all components of GPP service delivery are treated integrally within the transition plan to digital GPPs.

**The RGC should adopt a neutral approach to technology and take on a developmental orientation to digital GPPs.** Ultimately (and ideally), every individual or business agent should be able to make or receive government payments using any means, through any provider of choice, and to and from any place in the country. Multiple options (in terms of instruments, channels, and providers) should be available to all users, and the rise of alternative options as well as of preferences leading to choices should be left to the interplay of market demand and supply. The government should facilitate such market interplay and create the conditions for promoting the greatest range of choices possible. In the context of a realistic and gradual approach, however, government should at a minimum ensure that all citizens and businesses, everywhere in the country, should be able to conveniently access at least one basic type of electronic payment channel (including also through the help of PSP agents) for the purpose of making or receiving government payments.

**Implementing the comprehensive set of reforms proposed here would have several practical and measurable outcomes.** These include (i) lower transaction costs, (ii) improved management of public funds, (iii) less leakage and loss of interest on private and public funds lying idle in intermediary accounts, (iv) less time spent on the processing of administrative practices and payment execution, (v) elimination of the need for one-on-one relationships between GPPs and financial institutions, (vi) detection and elimination of ghost beneficiaries and duplications, (vii) higher volumes of electronic payments, and (viii) higher numbers of people reached by formal finance.

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51 As noted, this is the approach currently recommended or adopted by the World Bank Group in the context of its advisory and technical assistance activities. Specifically, Guideline 10 of the World Bank's General Guidelines for the Development of Government Payment Programs recommends that governments "**Leverage on government payment programs to promote financial inclusion:** *the large volume of payments issued by governments, as well as the nature of some specific programs like social spending programs, represents an opportunity to promote or facilitate financial inclusion on a large scale."*

52 The actual transfer of funds is only part of a GPP transaction. If the full process is not fully digitalized, the digital GPP payment is unlikely to be transformational. For example, annual business registration and tax payments may require long lines. Also, there may be separate lines for handing over documents for a tax assessment, for obtaining forms that must be filled out to make payments, for receiving an official signature or stamp on the form, and another for making the actual payment. A digital GPP service can solve only the very last part of the process, causing consumers to still have to stand in multiple lines. In this scenario, the ability to make a digital payment does not save the consumer that much time. A process that allowed users both to execute payments electronically and to receive validated documents online would offer considerable time and cost savings.

53 A fully digital experience brings greater value to the system than GPP delivery mechanisms that, while partly automated, still feature similar characteristics of a cash-based system (for example, involvement of agents and physical presence).

# ANNEX. SELECTED INDICATORS

| SELECTED INDICATORS | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 E | 2021 F |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **INCOME AND ECONOMIC GROWTH** | | | | | | | | | | | | | | |
| GDP growth (annual %) | 6.7 | 0.1 | 6.1 | 7.1 | 7.3 | 7.4 | 7.1 | 7.0 | 6.9 | 7.0 | 7.5 | 7.1 | -3.1 | 4.0 |
| GDP per capita growth (annual %, real) | 5.1 | -1.4 | 4.5 | 5.4 | 5.6 | 5.6 | 5.4 | 5.3 | 5.3 | 5.4 | 5.9 | 5.5 | -4.4 | 2.6 |
| GDP per capita (US$, nominal) | 744.5 | 737.9 | 812.9 | 892 | 950 | 1,028 | 1,100 | 1,175 | 1,270 | 1,381 | 1,506 | 1,640 | 1,519 | 1,609 |
| Private Consumption growth (annual %) | 12.7 | -0.2 | 8.8 | 10.4 | 4.7 | 5.6 | 4.6 | 9.4 | 5.8 | 3.7 | 3.0 | 7.0 | -0.8 | 2.6 |
| Gross Investment ( % of nominal GDP) | 17.3 | 20.1 | 16.2 | 16.0 | 17.4 | 18.7 | 20.9 | 21.4 | 21.7 | 21.9 | 22.6 | 23.4 | 24.6 | 27.6 |
| Gross Investment - Public ( % of nominal GDP)[1] | 6.3 | 8.8 | 9.6 | 10.7 | 9.1 | 9.1 | 8.2 | 6.9 | 6.7 | 6.8 | 6.7 | 7.7 | 11.4 | 10.8 |
| **MONEY AND PRICES** | | | | | | | | | | | | | | |
| Inflation, consumer prices (annual %, period average)[2] | 12.3 | 3.1 | 2.6 | 3.4 | 1.4 | 2.2 | 1.2 | 1.8 | 3.5 | 3.3 | 3.1 | 3.2 | 2.9 | 3.0 |
| Broad Money (% of GDP)1 | 28.3 | 37.7 | 41.6 | 39.1 | 50.1 | 55.5 | 67.1 | 72.4 | 79.2 | 88.2 | 100.7 | 107.7 | 137.5 | 142.0 |
| Domestic Credit to the Private Sector ( % of GDP)[1] | 23.5 | 24.6 | 27.6 | 28.3 | 38.7 | 52.0 | 62.7 | 74.3 | 81.7 | 86.7 | 99.6 | 114.2 | .. | .. |
| Nominal Exchange Rate (local currency per USD) | 4,060.0 | 4,140.0 | 4,044.0 | 4,016.0 | 4,033.0 | 4,027.0 | 4,030.0 | 4,025.0 | 4,058.0 | 4,062.0 | 4,067.0 | 4,070.0 | 4,077.4 | 4,070.0 |
| Real Exchange Rate Index (2015=100) | 91.4 | 90.8 | 98.1 | 94.3 | 93.3 | 92.6 | 94.7 | 100.0 | 101.9 | 103.2 | 99.7 | 101.0 | 96.8 | 98.9 |
| **FISCAL** | | | | | | | | | | | | | | |
| Revenue (% of GDP) | 16.4 | 15.9 | 17.7 | 17.6 | 17.7 | 18.2 | 20.0 | 19.7 | 20.9 | 21.9 | 23.8 | 27.0 | 24.1 | 22.7 |
| Expenditure (% of GDP) | 16.1 | 20.5 | 21.0 | 23.0 | 21.9 | 21.4 | 21.9 | 20.2 | 21.1 | 22.7 | 23.4 | 25.5 | 26.8 | 26.0 |
| Interest Payments (% of GDP) | 0.2 | 0.2 | 0.3 | 0.3 | 0.5 | 0.7 | 0.7 | 0.3 | 0.4 | 0.4 | 0.4 | 0.4 | 0.6 | 0.5 |
| Non-Interest Expenditure (% of GDP) | 15.9 | 20.3 | 20.7 | 22.7 | 21.4 | 20.7 | 21.2 | 19.9 | 20.7 | 22.3 | 23.0 | 25.1 | 29.4 | 29.3 |
| Overall Fiscal Balance (% of GDP) | 0.3 | -4.6 | -3.3 | -5.4 | -4.2 | -3.2 | -1.9 | -0.5 | -0.2 | -0.8 | 0.4 | 1.5 | -2.7 | -3.3 |
| Primary Fiscal Balance (% of GDP) | 0.5 | -4.4 | -3.0 | -5.1 | -3.7 | -2.5 | -1.2 | -0.2 | 0.2 | -0.4 | 0.8 | 1.9 | -2.1 | -2.8 |
| General Government Debt (% of GDP) | 27.0 | 28.5 | 28.7 | 29.7 | 31.5 | 31.7 | 31.9 | 31.2 | 29.1 | 30.0 | 28.4 | 28.1 | 34.6 | 35.2 |
| External Public Debt (% of GDP)[1] | 24.5 | 26.3 | 27.1 | 26.9 | 30.4 | 31.5 | 31.4 | 31.2 | 29.1 | 30.2 | 28.7 | 28.1 | 34.6 | 35.2 |
| **EXTERNAL ACCOUNTS** | | | | | | | | | | | | | | |
| Export growth, G&S (nominal US$, annual %) | 20.2 | -24.4 | 22.9 | 11.4 | 16.0 | 16.8 | 10.3 | 7.5 | 9.0 | 9.4 | 12.3 | 9.5 | -4.0 | 18.9 |
| Import growth, G&S (nominal US$, annual %) | 11.3 | -17.0 | 19.1 | 11.4 | 14.2 | 16.9 | 8.8 | 7.6 | 9.0 | 7.8 | 9.3 | 9.0 | -3.9 | 23.2 |
| Merchandise exports (% of GDP) | 49.4 | 33.9 | 38.3 | 38.8 | 41.6 | 44.6 | 45.4 | 45.4 | 45.5 | 45.2 | 46.0 | 46.0 | 48.2 | 48.8 |
| Merchandise imports (% of GDP) | 58.2 | 46.8 | 50.4 | 50.5 | 53.7 | 57.5 | 57.5 | 57.3 | 56.9 | 55.6 | 55.1 | 54.6 | 56.5 | 57.3 |
| Services, net (% of GDP) | 6.5 | 6.2 | 6.8 | 6.3 | 7.3 | 7.8 | 7.7 | 7.5 | 7.0 | 7.0 | 7.4 | 7.2 | 6.8 | 4.2 |
| Current account balance (current US$ millions) | -622.3 | -1,120.4 | -1,165.3 | -1,309.3 | -1,390.7 | -1,489.3 | -1,899.7 | -1,680.6 | -1,756.6 | -2,140.5 | -2,180.1 | -2,632.5 | -2,525.5 | -2,663.3 |
| Current account balance (% of GDP) | -6.0 | -10.8 | -10.0 | -10.1 | -9.9 | -9.6 | -11.3 | -9.2 | -8.8 | -9.7 | -8.9 | -9.7 | -9.9 | -9.8 |
| Foreign Direct Investment, net inflows (% of GDP) | 7.6 | 8.8 | 11.9 | 11.6 | 13.9 | 13.0 | 10.5 | 9.5 | 12.0 | 12.1 | 12.6 | 13.2 | 13.7 | 13.8 |
| External debt, total (% of GDP)[1] | 25.5 | 31.7 | 35.6 | 36.2 | 47.9 | 49.9 | 49.7 | 52.2 | 50.2 | 51.5 | 55.0 | 56.6 | .. | .. |
| Multilateral debt (% of total external debt)[1] | .. | .. | .. | .. | .. | .. | .. | .. | .. | .. | .. | .. | .. | .. |
| Debt service ratio (% of exports goods and non-factor services)[1] | 0.8 | 1.0 | 1.1 | 4.0 | 6.0 | 5.7 | 5.4 | 5.1 | 5.1 | 6.2 | 6.7 | 6.9 | .. | .. |
| **POPULATION, EMPLOYMENT AND POVERTY** | | | | | | | | | | | | | | |
| Population, total (millions) | 13.9 | 14.1 | 14.3 | 14.5 | 14.8 | 15.0 | 15.3 | 15.5 | 15.8 | 16.0 | 16.2 | 16.5 | 16.7 | 16.9 |
| Population Growth (annual %) | 1.5 | 1.5 | 1.6 | 1.6 | 1.6 | 1.7 | 1.7 | 1.6 | 1.6 | 1.5 | 1.5 | 1.5 | 1.4 | 1.4 |
| Unemployment Rate1 | 0.8 | 0.6 | 0.8 | 0.6 | 0.5 | 0.4 | 0.7 | 0.4 | 0.7 | 0.7 | 0.7 | 0.7 | 0.7 | .. |
| Inequality - Gini Coefficient[1] | .. | .. | .. | .. | .. | .. | .. | .. | .. | .. | .. | .. | .. | .. |
| Life Expectancy[1] | 65.4 | 66.0 | 66.6 | 67.0 | 67.5 | 67.9 | 68.3 | 68.6 | 69.0 | 69.3 | 69.6 | .. | .. | .. |
| **OTHER** | | | | | | | | | | | | | | |
| GDP (current LCU, millions) | 41,968,385.0 | 43,056,732.0 | 47,047,985.0 | 52,068,693 | 56,616,800 | 62,219,524 | 67,740,436 | 73,422,702 | 81,241,866 | 89,830,525 | 99,544,275 | 110,014,048 | 103,511,609 | 110,763,826 |
| GDP (current US$, millions) | 10,337.0 | 10,400.2 | 11,634.0 | 12,965 | 14,038 | 15,451 | 16,809 | 18,242 | 20,020 | 22,115 | 24,476 | 27,030 | 25,484 | 27,215 |
| GDP per capita LCU (real) | 2,062,211.6 | 2,033,232.3 | 2,124,292.2 | 2,238,619 | 2,363,486 | 2,495,841 | 2,630,660 | 2,769,140 | 2,915,146 | 3,071,748 | 3,252,348 | 3,431,774 | 3,279,153 | 3,365,284 |
| Doing Business Rank[3] | .. | .. | .. | .. | .. | .. | .. | .. | .. | .. | .. | 144 | .. | .. |
| Human Development Index Ranking[4] | 142.0 | 142.0 | 143.0 | 143 | 145 | 144 | 144 | 146 | 146 | 145 | 144 | 144 | .. | .. |
| CPIA (overall rating)[1] | 3.3 | 3.3 | 3.4 | 3.4 | 3.5 | 3.4 | 3.4 | 3.4 | 3.4 | 3.4 | 3.4 | 3.4 | .. | .. |
| Economic Management[1] | 3.8 | 3.8 | 4.0 | 3.8 | 3.8 | 3.8 | 3.8 | 4.0 | 4.0 | 4.0 | 4.2 | 4.2 | .. | .. |
| Structural Policies1 | 3.3 | 3.3 | 3.3 | 3.5 | 3.7 | 3.7 | 3.7 | 3.5 | 3.5 | 3.3 | 3.3 | 3.3 | .. | .. |
| Policies for Social Inclusion and Equity[1] | 3.3 | 3.3 | 3.4 | 3.5 | 3.5 | 3.4 | 3.4 | 3.4 | 3.4 | 3.4 | 3.4 | 3.5 | .. | .. |
| Public Sector Management and Institutions[1] | 2.7 | 2.7 | 2.7 | 2.8 | 2.8 | 2.8 | 2.8 | 2.7 | 2.7 | 2.7 | 2.6 | 2.6 | .. | .. |

*Notes:* ".." indicates not available. E = estimate, F = forecast. Data from MFMOD unless otherwise noted

1/ World Development Indicators Database and World Bank Staff Estimates

2/ World Bank GEM database; MRV = Most recent value

3/ This indicator is ranked out of 190 countries (Doing Business 2019). Data are presented for survey year instead of publication year. Doing Business rankings change over time, due to both methodology and policy changes.

4/ The HDI ranking in 2001 is in relation to 175 countries and in 2010 in relation to 169 countries. Methodological enhancements in HDI calculations have resulted in notable improvements in the countries' rankings.

Sources: MFMOD Database, World Bank WDI and GEM databases, IMF.

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