



CAMBODIA

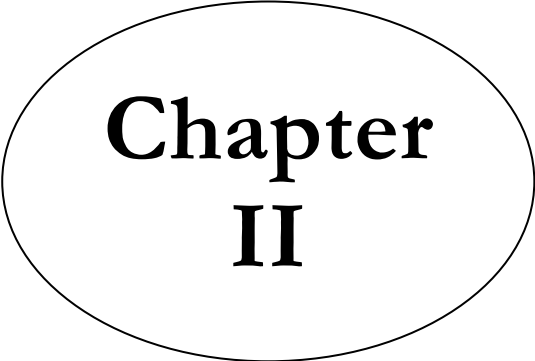
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Chapter II

INVESTMENT POLICIES & HUMAN DEVELOPMENT IN CAMBODIA

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General Investment Policies

All investments in Cambodia, either domestic or foreign sourced, are regulated by the Law on Investment of 4 August 1994, together with Sub-Decrees of 29 December 1997 and 11 June 1999. The law attempts to similarly treat all local and foreign investors in all areas, except in the ownership of land. In general, Cambodia neither prohibits nor restricts foreign investment, except for reasons of national security and social safety, or when deemed necessary for economic reasons. For instance, foreign investment in rice milling is subject to local equity participation, to be determined through negotiations between the investors. Foreign investment in livestock and forestry also requires a local partner. The criteria governing these restrictions are laid down in Sub-Decree No. 88 of 29 December 1997.

Cambodia's Constitution reserves the ownership of land for Cambodia citizens, or legal entities with a minimum Cambodian ownership of 51 percent. Foreign investors are allowed to lease or use land for up to 70 years in accordance with the 1994 Law on Investment. The 2001 Land Law defines two types of land – concession land and leasehold land. Concession land may be leased for a period of up to 99 years for agro-industrial projects. Leasehold land is defined as real estate, including buildings and land, available for short-term or long-term lease. The leasing period may either be indefinite, or have a specified duration. The lease with definite duration may be short with a renewal option or long term 15 years or longer.

Cambodia's legislation guarantees compensation in case of expropriation. Article 44 of the Constitution stipulates that legal private property is protected by law, and the right to confiscate property may only be exercised in the public interest with a fair and just compensation as provided for in the law. Article 9 of the Law on Investment provides a general guarantee against nationalisation.

To enhance investor confidence further, Cambodia has concluded bilateral investment guarantee agreements with twelve countries.³² It signed and ratified an agreement with the Overseas Private Investment Corporation (OPIC) of the United States, and ratified the Multilateral Investment Guarantee Agency (MIGA) of the World Bank. These bilateral agreements do not include trade preferential arrangements,

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³² China, Croatia, France, Germany, Indonesia, Malaysia, the Philippines, the Republic of Korea, Singapore, Switzerland, Thailand, and Viet Nam

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except for ASEAN countries under the ASEAN Framework; but they contain provisions granting MFN treatment on a general or specific basis. Cambodia joined ASEAN in 1999, which implies an automatic accession to the ASEAN Free Trade Area (AFTA). Therefore, Cambodia has agreed to eliminate tariffs on essentially all ASEAN products by 2015.

Cambodia provides incentives to stimulate investment with Article 14 of the 1994 Law on Investment. These incentives are granted to Cambodian and foreign firms without discrimination upon application to the Council for the Development of Cambodia (CDC). The incentives include:

- i. corporate tax rate of 9 percent, except for exploration of natural resources, timber, oil, mining, gold, and precious stones (30 percent);
- ii. tax relief on corporate tax for up to eight years with a loss that may be carried forward for five years, and exemption from all corporate tax for profits reinvested in Cambodia;
- iii. no withholding tax on dividends; and,
- iv. unrestricted repatriation of profits.

In addition, investment projects exporting 80 per cent or more of their production may benefit from a full import duty exemption on input construction materials, means of production, equipment, intermediate goods, raw materials, and spare parts. The import duty exemption is also available for projects located in designated special promotion zones (SPZ), in the tourism industry, in labour-intensive industries (e.g. garments, footwear, and toys), agro-industry, and food processing industries, as well as physical infrastructure and energy generation. In short, Cambodia's investment law contains a range of taxation concessions for approved investment activities.

Reviewed by Foreign Investment Advisory Team (FIAS) in 1997, this investment law was regarded as being subject to too much discretion in its application, leaving investors with unnecessary uncertainty and potential corruption. Furthermore, tax-reducing provisions available under the law were considered to be too generous, potentially hampering revenue mobilisation and causing distortions to the overall tax policy framework. Therefore, as insisted by some donors, the Cambodian government initiated some changes to the

investment regulations. The changes introduced a greater transparency to the granting of investment incentives, limiting the ability of some government members to exercise their discretion, and expanding investment monitoring capacity and customs governance. However, a subsequent FIAS review in 2000 found that, despite these changes, Cambodia's investment regime remained heavily discretionary, selective, complex, and open to unnecessary State revenue sacrifice and abuse. The main reason for the failure was that the government did not possess the governance and administrative capability to implement the current investment incentive regime as intended.

Under the insistence of some donors, the 1994 Law on Investment was subject to another revision. Discussions were held among donors, government, and private sector. The objective of the revision proposed by FIAS was to create an investment regime with transparency, simplicity, and predictability in both the approval process of private investments and the provision of fiscal incentives to such private investment. In addition, FIAS proposed some changes in granting tax incentives to the private sector, such as eliminating a concessionary tax rate on profit, reducing tax relief, and in taxing reinvestment of profit.

The private sector welcomed the FIAS proposal on the improvement of the legal framework for investment in Cambodia, but did not agree with the new fiscal measures. They argued that the business environment in Cambodia was not yet conducive to making an acceptable return on invested capital, because of high operating costs, excessive layers of bureaucracy, and visible lack of good governance. They pointed out that if the investment environment were perfect, and operating costs related to corruption were at an acceptable level, those investment incentives would then be of marginal importance to them. However, they emphasised it was not the case in Cambodia. Finally, a compromise on tax incentive measures was reached, and the National Assembly duly adopted in February 2003 the revised Law on Investment.

Foreign Direct Investment and Its Impact

Propelled by the 1994 Law on Investment which had been designed to attract investments, foreign direct investment (FDI) in Cambodia significantly increased from 3.5 percent of GDP in 1994 to 8.3 percent of GDP in 1996. The investment covered almost all sectors of the economy. Economic growth was strong, reaching the

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government's annual target of 7 to 8 percent, and generating significant employment. Household income increased by almost 20 percent per year in U.S. dollar terms. However, persistent weak governance and the political crisis of 1997, combined with the simultaneous Asian financial crisis, led to a sharp economic slowdown. Some critical reforms, such as civil service reform, were shelved, and investor confidence was buffeted.

Since 1994, the amount of stocks of FDI in Cambodia is estimated to reach US\$1.3 billion. About 50 percent of that has been concentrated in the industrial sector (mainly in the garment industry), 40 percent in services (essentially tourism, transportation, and telecommunications), and the balance of 10 percent in agriculture (mainly logging). It is also estimated that FDI has generated a total value added of about US\$750 million, or 20 percent of GDP, and has directly created approximately 300,000 formal jobs, representing about 6 percent of the total labour force.

The FDI inflow into Cambodia began to slow down in 1998, and continued to decline to less than 2 percent of GDP in 2002. The country's real GDP growth, however, remained relatively high, averaging about 6 percent during 1999-2002. The main reasons for the growth were the large investments that have gone into the garment industry since 1997, and the tourism industry since 1999. The strong development in these two industries was sufficient to make up for the overall decline in FDI and the negative economic impact of floods that adversely affected some parts of the country.

The FDI has also brought about a significant improvement in external trade in Cambodia's economic development. From 1995 to 2002, Cambodia's external trade grew at an annual rate of 12 percent in real terms, while domestic demand expanded only about 5 percent per year. Despite the slowdown in the garment industry and substantial decline in timber exports, the volume of Cambodia's external trade continued to grow steadily, exceeding the nominal GDP in 2000 for the first time in Cambodia's history.

However, the total trade deficit significantly increased, reaching 14 percent of the nominal GDP in 2002, against 8 percent in 1995. Moreover, despite an expansion in tourism, the balance in the services sector did not improve much during those seven years, due to a large

deficit in the Cambodian air transportation sector. Subsequently, Cambodia's current account deficit rose to 9.6 percent of GDP in 2002, from 8 percent in 1995. This weakness will worsen if the garment and tourism industries lose their competitiveness as a result of implementation of WTO agreements, and/or the international environment becomes unstable.

The influx of FDI has impacted the population movement to a large extent, especially among young workers. The concentration of FDI in growing cities like Phnom Penh and Siem Reap has led to huge migration of young people, particularly female, from rural to urban areas. The movement has also brought about a positive cultural change in the Cambodia society. As in other less developed Asian countries, Cambodian women used to stay at home with their immediate family, attending to household chores. Now due to the rural dire poverty, the parents have no option but to reluctantly let their daughters leave their rural family to work and live independently in the city. Their movement certainly opens up one of the main sources for family income in rural areas. They make up the largest part of workers in FDI-related industries, accounting for about 85 percent in the garment industry, and 60 percent in tourism sector.

About the Garment Industry

The garment industry has now become one of the fastest growing private investment areas in Cambodia; it is a leading export sector for the country. The robust growth has mainly resulted from the Normalised-Trade Relationship agreement with the United States in 1996 and with the European Union in 1997. The industry has benefited greatly through the Most Favoured Nation (MFN) and the Generalised System Preference (GSP) trading status that was granted by the United States, European Community, and other developed nations.

The textile and garment industry is highly labour intensive, with low production costs due to its large and relatively cheap labour force. Most garment workers are young, unskilled women who have migrated from rural areas, while most of the supervisory staff are foreign. Rapid development of the garment industry, combined with the country's democratisation process, has led to a rapid expansion of unionisation. Misunderstandings between local workers and foreign managers, and

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disregard for labour law by some factory managers, have often caused labour unrest. To encourage the Cambodian government to improve working conditions in the garment industry, the US linked in 1999 its quota allocation to workers' rights improvement.

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Relative to other countries in the region, Cambodia's garment industry remains in its infancy, in both competitive experience and in marketing strategies. Although the government has heretofore shown vigorous commitment in boosting the textile and garment industry in Cambodia, many onlookers questioned the sustainability of this commitment. Meanwhile, the garment industry has benefited from many tax exemptions; it has thus contributed only moderately to the state budget. Another concern is that the garment industry in Cambodia has no real local roots. Inputs, markets, and management come from foreign sources, and could easily be moved out of the country on short notice. This is potentially worrisome for the long-term development and industrialisation of Cambodia.

About the Tourism Industry

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Cambodia is now becoming an attractive tourist destination after more than two decades of war and internal strife. The number of foreign tourists visiting Cambodia has grown remarkably, from 140,000 visitors in 1993 to 800,000 visitors in 2002. Up to 2002, the amount of total investment in this industry should have reached the same amount as that in the garment industry of about US\$ 400 million.

The real challenge for Cambodia is how to take advantage of this rapid growth in tourism. Net incomes and job creation directly generated from tourism industry seem to be relatively limited, although the number of foreign tourists has sharply increased during the last two years. In 2002, gross incomes generated from foreign tourists visiting Cambodia amounted to about US\$220 million, which is very low compared to other countries in the region; for instance, Thailand raked in US\$10 billion. Furthermore, according to a study in December 2002 by a group of local NGOs, CCC-ADI, only 30 percent of foreign tourist spending in Siem Reap has, in fact, benefited Cambodia.

It would be interesting, therefore, to examine in some detail the impact of the FDI on four major aspects of human development

employment and productivity, equity, empowerment, and sustainability with references to Cambodia's two fastest growing industries.

Impact of FDI on Employment

The garment industry has played a significant role in providing employment to the low-skilled labour force in Cambodia; it accounts for about 70 percent of total employment in the manufacturing sector. But it represents only about 4 percent of the total labour force, as Cambodia remains largely an agriculture-based economy.

It is estimated that the garment sector employed about 200,000 people in 2002. From 1997 to 1999, the garment industry created almost 40,000 new jobs per year on average. However, the trend slowed down significantly in 2000-2002 to less than 15,000 new jobs per year, because of a sharp decline in investment.

Like other countries, Cambodian women make up the largest portion of garment and footwear factory workers, accounting for about 85 percent, according to the Garment Manufacturers Association in Cambodia (GMAC). About 90 percent of them come from rural and provincial areas. The proportion of job seekers from rural areas is growing; they are understandably seeking greater economic opportunities in towns and cities, particularly in Phnom Penh.

According to a CDRI survey in 2000, 50 percent of survey respondents reveal that they have spent an average of about a month's wage to obtain their job in garment industry. The money may be paid to a number of people, such as factory security guards, interpreters, or the person who introduced the worker to the factory. In addition, 57 percent of them say they took out a loan to pay for this "bribe". According to GMAC, factory owners condemn this practice, and invite workers to lodge their complaints, but none of them would agree to testify against the practice.

Skill is another concern for the Cambodian labour force. Competency of workers in the garment and textile industry plays a significant role in attaining competitiveness, and also in attracting foreign investors to further develop it into a high-tech industry. Investors need more than just cheap labour; they need labour literacy,

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availability, and competency. According to the CDRI survey, the average educational level of young female garment workers is limited: 61 percent have attended primary school, 31 percent have attended secondary school, and 8 percent have attended high school. In 1999, a vocational training programme was undertaken by the garment industry, with the support of major Japanese sewing machine manufacturers JETRO, MARUBENI, and JUKI. A training centre was established to form and upgrade the skills of Cambodian sewing and stitching operators to become supervisors. According to GMAC, more than 500 Cambodian supervisors have been trained in the last three years.

The tourism industry as a whole includes hotels, restaurants, bars, travel agencies, and guides; it is estimated to have employed about 70,000 people in 2002. However, only about 7,000 workers in the hotel industry and 3,000 in guide and travel agencies are well trained and well paid. The other 60,000 workers take in meagre earnings from jobs at restaurants and related tourism-focused businesses. Based on a socio-economic survey in 1999, about 60 percent of tourism sector employees are female.

Cambodian investment policies seem to be confusing, producing opposite outcomes to their intent. The very generous Law on Investment is supposed to encourage job creation in less-developed regions of the country, in lieu of encouraging mass migration of workers toward urban areas, particularly Phnom Penh. The tax relief is granted on socio-economic and geographic criteria laid down in Annex III of Sub-Decree No 88 of December 1997. However, this relief has not been taken advantage of, due to the absence of infrastructure in those regions. Investors prefer to stay in and around Phnom Penh, or the new special promotion zones, where they benefit from tax incentives and have ready access to better public infrastructure. As a result, the new investment law may serve only to reinforce the development gap between regions, provoking further migration and failing to create more employment. Furthermore, additional tax incentives may reduce the already weak national budget revenue without providing any offsetting benefit.

Impact of FDI on Productivity

Investment does play a crucial role on improving worker productivity. Table 1 shows that for some major sectors of the economy there appears to be a significant positive correlation between the productivity of workers and the level of capital stock per worker,

which essentially measures investment level. It means, though the causal effect is uncertain, that a high level of one factor would go hand-in-hand with a high level of another.

It appears that while the entire economy has suffered from low stocks of capital and productivity, the garment sector was the best performer in 2002 in term of efficiency. It registered the highest productivity-capital ratio of 1.89; i.e. for every US dollar invested in stocks of capital, the garment sector produced \$1.89. It seems interesting that the ratio for the agriculture sector was the second highest at 1.15, a point higher than that of tourism, which means both sectors could almost be equally productive. However, the ratio for agriculture is somewhat distorted as the sector includes logging activities which are far more efficient and productive with modern equipment than traditional farming which makes up the bulk of the agriculture sector.

Table 2. Growth of Productivity and Income during 1995-2002
(%, yearly average, constant prices)

	Productivity	Salary/Income
Garment	11.2%	13.4%
Tourism	5.2%	8.6%
Whole Economy	3.2%	5.0%

Source: EIC, compiled from government primary data

The growth of worker productivity in the garment industry was by far the strongest, averaging 11.2 percent per year during 1995-2002, compared to 5.2 percent for the tourism sector and only 3.2 percent for the whole economy (Table 2). Table 2 also shows that salaries grew faster than productivity. This may be explained by the fact that garment industry salaries were initially set at a very low base, about US\$35 per month in 1995, and have been raised by increasingly effective bargaining power by worker unions.

Industry Costs and Equity in Capital Assets

It can be argued that, unfortunately, the FDI inflow has concentrated on industries that seem to be capable of retaining only a minimum real benefit for the local economy. The garment and tourism industries – which have grown remarkably in recent years due to the heavy FDI inflow – have left rather little for local workers and businesses.

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For the fledgling Cambodian garment industry, Table 3 shows a high import input of 67 percent of sales revenue, reflecting the fact that the industry has relied heavily on imported raw materials; there is little local industrial base to provide input supplies. Labour cost represents about 13 percent, and other cost components, including gross profit before capital amortization, make up the remaining 20 percent. However, industry professionals interviewed by the EIC for this segment maintain that within the “other cost components” are “bureaucracy costs” that amount to about 7 percent. Hence, the gross profit after this bureaucracy cost is estimated to be 13 percent. Overall, the FDI in the garment industry provides to the local economy only about 13 percent of the industry’s total revenue to the workers, plus the 7 percent bureaucracy cost, plus a difficult-to-quantify multiplier effect on the local economy.

**Table 3. Structure of Costs in FDI-related Industry
(% of Total Sale)**

	Garment	Tourism
Import Inputs	67%	62%
Labour Cost	13%	3%
Others	20%	35%
Total	100%	100%
Total Sale (US\$ m)	\$1,300	\$570

Sources: Compiled by EIC from primary data of GMAC,
Ministry of Commerce and Ministry of Tourism

Although sales revenues in the garment and tourism industries make up more than half of the country’s total GDP, it is estimated that less than 15 percent of these revenues have remained in Cambodia. Most has been repatriated.

Table 3 also paints a similar picture for the fast-growing tourism industry. Its import input – which is mainly the air transportation cost that foreign visitors have to pay to reach Cambodia – accounts for 62 percent of the total cost of visiting Cambodia. The labour cost component in the industry is extremely low, amounting to a mere 3 percent of total sales revenue, while the combined cost of capital and gross profit components are as high as 35 percent. Most of the physical facilities for tourists - including airlines, hotels, resorts, and airports - are foreign-owned. Cambodia has no national air carrier since Royal Air Cambodge went into bankruptcy in 2001.

Therefore, the benefits to Cambodian workers and the economy from the FDI-induced growth in Cambodia’s two major industries have been relatively insignificant. Although sales revenues in the garment and tourism industries are very high, making up more than half of the country’s total GDP, it is estimated that less than 15

percent of these revenues have remained in Cambodia. Most has been repatriated. The two main industries also are still heavily dependent on foreign supplies. The garment industry needs a local industry support base to supply raw materials, while the tourism industry requires at least a viable national air carrier to keep a larger portion of revenues within the country.

Ironically, one so-called benefit to the local economy is the bureaucracy cost, which is among the highest in this region. Business people complain that it continues to increase. The Cambodian government provides many tax exemptions to industry, such as no tariff on importing garment-related raw materials into Cambodia, and neither a profit tax nor a value-added tax. This only seems to be in compensation, though, for myriad bureaucratic difficulties which garment investors complain of in dealing with government officials. Red tape, tardiness, and under-the-table solutions are among problems they claim cause them headaches.

Contrary to some fears, Cambodia still has a competitive advantage with respect to labour costs, which are basically the same as in Vietnam, and three times lower than that of Thailand and the Philippines.

Empowerment

The rapid growth of industries, particularly the garment sector, in recent years has had a dramatic impact on the country's socio-economic conditions. It has opened up Cambodia to world issues, including labour rights, pollution, and various social problems.

Labour Rights – Industrial Relations

The FDI has also encouraged Cambodia to address industrial relations issues. The rapid growth in the work force in response to new industrial development, and a national commitment in the Paris Peace Accord in 1991 to open Cambodia to the ideals of freedom, human rights, and democracy, have naturally led to a working environment in which interests of employers and workers need to be represented. A Labour Law was promulgated to regulate working conditions. The Garment Manufacturers Association and various unions all have played notable roles in Cambodian industrial relations, even though these industries emerged only a few years ago.

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Founded in March 1996, the Garment Manufacturers Association in Cambodia (GMAC) has so far been the most important player in the development of the garment industry. This powerful association – representing about 200 garment factories operating in Cambodia – actively pushed the government to seek special trading status (GSP and MFN) from developed countries, mainly the US and European Union. This effort reached success in 1997. GMAC has also advised the government on how to promote the garment industry in Cambodia and acted as a mediator in conflicts between garment factory owners and workers.

The workers consists mainly of young Cambodian women who are generally low skilled, poorly educated, and who traditionally stayed at home with their parents until they got married. Most are peasants who were unaccustomed to working according to schedules and time clocks. Now, they live in an urban setting and work with hundreds of other colleagues in factories with stringent timeframes and disciplines. This new-to-Cambodia working structure has led to the formation of many worker unions, which have taken on the advocacy of workers who are otherwise unsophisticated in matters of worker rights.

Through the efforts of worker unions, complaints have been raised and heard, and demonstrations and strikes organised. The unionisation of the work force, however, has been formidable only in Cambodia's manufacturing sector. As of September 2003, there were a total of 482 registered labour unions in Cambodia, most of which represented garment workers. All garment unions are affiliated with one of the six national labour federations.

According to some industry professionals, there is not yet a real collective bargaining going on in Cambodia, although some of the unions believe otherwise. Most of what people call collective bargaining in Cambodia amounts instead to dispute settlement negotiations aimed at getting employers to comply with existing law. Real collective bargaining, meaning the process by which a union negotiates with an employer for agreements on wages, leaves, and other benefits, has been in limited evidence. The goal of collective bargaining is usually for workers to obtain benefits that exceed what is imposed by law.

Although the unions are relatively inexperienced and immature, they have nevertheless achieved some remarkable successes in

bargaining within the structure of the Labour Advisory Committee that groups together the government, unions, and factory owners. Those successes include raising minimum monthly wage in 1997 for garment workers from US\$ 27 to US\$ 40, and from US\$ 40 to US\$ 45 in 2000. They are now wrestling with employers for further improvement in working conditions by demanding a reduction in the work week from 48 to 44 hours. There were 76 strikes in 1999 and about the same in 2000, but the number has steadily declined since.

Only in the garment and footwear industry is there a minimum monthly wage. This minimum wage is still insufficient, according to some garment union leaders. They argue that at least US\$ 85 is needed for a decent livelihood for Cambodian garment workers. Currently, on average, garment workers earn about US\$60 per month. About half of this amount goes to minimum subsistence costs of food, lodging, and transportation between home and work. Most garment workers send the other half of their earnings home, to support their poor families in rural areas. Thus they live on a very tight budget, and work hard; they minimise their own spending and extend their overtime work. Subsequently, many have health problems brought on by long hours of overtime and/or inadequate attention to proper nutrition.

Despite some problems, Cambodian labour rights have generally been improving. Cambodian labour conditions have not strictly complied with internationally recognised standards; but relative to other developing countries, it has made notable progress in the area of workers rights. These rights include non-discrimination in employment, prohibition of forced or bonded labour, and prohibition of exploitative child labour.

The application of labour law in Cambodia is relatively good, but room for improvement exists in the law's guarantee of "freedom of association." The Cambodian Constitution and labour code stipulate clearly about a guarantee of freedom of association, and of workers' rights to exercise that freedom. In practice, however, the guarantee seems to have had a limited effect. In the garment industry, a climate of impunity for factory managers who violate the freedom of association provision is prevalent. The issues surrounding freedom of association remain controversial, and have been sources of labour unrest, in spite of a gradual decline in the level of harassment, in the dismissal of union leaders and intimidation of workers, in the

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interference in union formation, and in other anti-union activities in the past few years.

Pollution

The robust growth of tourism industry has also led to a great change of the level of environmental pollution in Cambodia.

The robust growth of tourism industry has also led to a great change of the level of environmental pollution in Cambodia. Many hotels in Phnom Penh are polluting the air and water every day. Due to high cost of State electricity, most hotels run their own generators, which produces unpleasant smog and noise to neighbouring homes/businesses and to the environment. The majority of hotels do not have a waste treatment system. The extent of the pollution may never be clearly known because there is no legal requirement for environmental impact assessments in Cambodia.

Outside Phnom Penh, there also is a general lack of attention given to environmental degradation. Many tourist sites do not have facilities for tourists – such as rubbish bins, public toilets, or other basic provisions. Specifically, a small river that runs through the City of Siem Reap is classified as highly polluted, fouled by plastic bags, bottles, rubbish, and wastewater from surrounding hotels and restaurants. Disorderly waste disposal and littering by local inhabitants are also concerns in the environment protection of Cambodia.

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In fact, the government has paid little consideration, if any, to ecological protection at tourist sites. Perhaps it believes the situation is not yet serious enough to warrant its close attention. The legislative framework and the information base are insufficient, weak, and incomplete. There are some legislative instruments to deal with polluters, but there have been problems with enforcement. Moreover, there is a general lack of awareness on environmental issues among Cambodia citizens.

What are needed are tough environment protection laws and policies that obligate polluters to contribute funds for environmental safeguarding and clean-up (commonly known as the Polluter Pays Principle). Hotels, restaurants, investors in tourism sites, and investors in commercial and business activities could fall under these obligations. The government itself also must take an active role to prevent and combat environmental degradation and environmental pollution. To receive government approval, a development project

needs to be preceded by an environmental impact study to assess costs and benefits. Appropriate waste treatment systems must be part of any development plan.

The Darker Side of Tourism

While the tourism industry is on the rise in Cambodia, generating economic benefits, there also has been a rise in sex tourism and, most disturbingly, child sex exploitation. Despite some arrests of foreign tourists for engaging in child sexual abuse and child pornography, Cambodia remains a hotspot for such unscrupulous tourists. While Thailand and the Philippines used to be known destinations for sex tourists, both countries have made notable progress in reducing and controlling sex tourism. This means that sex-seeking tourists simply travel to poorer neighbouring countries for their satisfaction. Cambodia has now become an easy target for those opportunistic men. One-third of all sex workers here are estimated to be children, mostly ages 12 to 17, but some even younger.³³

In January 2000, research initiated jointly by the Ministry of Tourism, Cambodian National Council for Children, and World Vision Cambodia, explored the problem of tourism involving sexual exploitation of children. The research outcome, published in "Children's Work, Adult's Play", show that 22 percent of foreign tourists have come to Cambodia for sexual pleasure. Almost all of 22 tour operators interviewed (91 percent) maintain that child prostitution in Cambodia is on the rise, and 45 percent say they have seen even some tour guides bringing girls for tourists.

Given the dire poverty of many Cambodian families, young girls of these families are vulnerable to being exploited, abused, and thrown into the world's oldest profession. As victims of a failed economy and society, they are at great risk of contracting and spreading HIV/AIDS, in addition to psychological damage they may have to bear for life. An alarming sign regarding the commercialised sex industry and child prostitution in Cambodia is that, in a survey carried out by the Ministry of Women and Veterans Affairs among prostitutes in one area of Phnom Penh, 60 percent of them were former garment workers.³⁴ What will happen to garment workers is

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³³ Los Angeles Times: Tuesday, December 12, 2000

³⁴ UNDP, The macroeconomics of Poverty Reduction in Cambodia, 2004, p. 157.

the current garment industry fails to compete in the world market from 2005, leading to the downsizing or closure of factories?

Eradication of commercial sex is difficult, but possible. Strong action and authority is needed to contain and regulate the whole industry. Child sex exploitation must be absolutely prohibited. There should be active, on-going campaigns to protect child rights and to promulgate tough laws against abusers. This can be successfully done through participation from policy makers, legislators, and non-government advocates, both to protect children and to prosecute culprits.

The Cambodian law on anti-child prostitution is currently good enough on paper for prosecution, but actual application is notoriously weak and/or slow.

In addition, the home governments of foreign sex tourists should be approached to legislate against their own nationals who commit child sex exploitation in other countries. The Cambodian law on anti-child prostitution is currently good enough on paper for prosecution, but actual application is notoriously weak and/or slow. Due to the government's lack of will to enforce the law and to allocate adequate resources for the tasks, there has been reportedly an increase, rather than a reduction, in the numbers of clandestine child sex exploitation in Cambodia.

Sustainability

Cambodia's management of its World Trade Organisation membership will be a litmus test for sustainable industrialization... It will find there are many challenges awaiting it from 2005 onward.

Cambodia may have a monopoly over Angkor Wat – it is a world-renowned tourist attraction – to keep its tourism industry continually prosperous. But the garment industry does not have Angkor's unique advantage to enjoy such an assurance for the future. The current development of the garment industry in Cambodia is heavily dependent on the concession of trading status obtained from the developed nations while some countries in the region have been deprived of it. For now, Cambodia is relatively better off, even though its bureaucracy cost is one of the highest in the world. But from 2005, such protective assurance will be removed, leaving the industry to stand on its own feet.

What will Cambodia face from 2005 onward when the quota system trade of garment products is lifted? Cambodia's management of its World Trade Organisation membership will be a litmus test for sustainable industrialisation, particularly the garment industry. It will find there are many challenges awaiting it from 2005 onward – such as a recent accession of China to the WTO and bilateral agreement on the Normal Trade Relationship between Vietnam and the US.

According to a World Bank study, 40 percent of Cambodian products will compete head-to-head with China, which has comparative advantages through a better skilled labour force and cheaper raw materials. It can export better quality products to the world's large markets, including the United States and Europe. Vietnam is also a garment producer with an abundance of skilled and cheap labour; it will be another main rival, potentially hindering further growth of the Cambodian garment industry.

Cambodia's relative progress in labour rights, in comparison to other competitors like China, may be a positive factor in helping sustain its market share. However, if continued progress is not made in the areas of transparency and managerial systems, particularly in terms of respecting the freedom of association, Cambodia will relinquish its competitive advantage in this area.

Unpredictable external factors, such as war in the Middle East and the outbreak of the SARS disease in Asia have constituted the main sources of uncertainty affecting the development of the Cambodian tourism industry. In 2002, these events cost Cambodia tens of millions of dollars and eliminated hundreds of jobs. In addition, Cambodia's tourism development has no strong local roots, as foreigners are the ones who control and own most of the management systems and the country's fixed assets, including the main airport. The tourism industry is at the mercy of foreign-based investors.

Conclusion

The generous incentives in the Law on Investment indeed succeeded in mobilising tremendous FDI inflow into the Cambodian economy, especially in the first few years of its implementation. The garment and tourism industries were the main beneficiaries and creators of jobs that kept the GDP growth at a reasonable level for a number of years. The workers are improving their skills and extending their work experiences, accompanied by improvements in productivity and by progress in labour rights.

It seems, however, that the rush to the economic growth has left a number of adverse by-products that now require special adjustments to socio-economic policies for a better and balanced growth. Some of the major issues are:

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- The development has been so concentrated in two industries – garment and tourism – that the economy is left open to a greater degree of fluctuation. The garment industry is facing a great deal of uncertainty at the advent of the WTO membership when it will face worldwide competition. A diversified investment would help ensure a sustainable growth in the long run.
- The design and implementation of the policies to induce and manage FDI did not ensure that local workers and the economy benefited better from the rapid growth. The garment industry needs raw materials that Cambodia is not ready to supply; furthermore, those production inputs are even imported duty-free, depriving the State of significant revenue. Major capital assets in the fast-growing tourism industry are foreign-owned, meaning that the bulk of tourist dollars spent in Cambodia are repatriated.
- The heavy concentration of FDI in large cities encourages massive migration toward them, putting pressure on urban congestion and leaving rural areas undeveloped.
- The growth in the tourism industry has caused environmental pollution and has inadvertently caused a flourishing of the commercial sex industry. Both problems urgently need corrective measures.