

Appendix I

CAMBODIA COMPETITIVENESS REPORT 2005-2006

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Whether Cambodia can gain benefits from globalization remains a major concern among stakeholders who support the country's development. Since there is no unique process to achieve high sustainable economic growth, the question is how competitive Cambodia and its businesses are on the international market. Cambodia's competitiveness emerges as a central concern for its development.

The Cambodia Competitiveness Report intends to comprehensively assess the country's competitiveness through the observations of top business executives on various aspects of Cambodia's economic environment, in order to eventually aggregate and to analyse their perceptions on issues related to national competitiveness. The report contains three basic sets of findings. First, it details outcomes of an executive opinion survey conducted among leading business executives in Cambodia. Second, it deals with the Growth Competitiveness Index of the WEF in which Cambodia is compared to its competitors. Third, Cambodia's performance is assessed within the framework of the Business Competitiveness Index of Professor Michael E Porter.

The first index highlights Cambodia's competitiveness from the quality of its macroeconomic environment, public institutions and technology, while the second index focuses more on micro components, with a strong emphasis on the quality of a country's business environment to support the high productivity of its businesses. Findings from both indexes are drawn primarily from a combination of the survey data and hard data from each country. They are complementary, allowing us to comprehensively cover the notion of competitiveness from both a macro and micro point of view.

Both indexes presented Cambodia with a relatively low score compared to the rest of the world. The Growth Competitiveness Index puts Cambodia in 112th position among 117 countries assessed this year by the World Economic Forum. Prof. Michael Porter's Business Competitiveness Index ranks Cambodia as 109th out of 116 countries. Cambodia's poor performance relates to the country's comparative weaknesses in different areas assessed by the indexes.

Cambodia's macroeconomic environment is characterized by high government deficit, high lending-borrowing interest rate spread, difficulty in acquiring business credit and wastefulness of government spending. Besides the country's macroeconomic uncertainty, Cambodia is still considered one of the world's riskier countries to invest in. Government efforts to reduce poverty are seen as insufficient in order to achieve the Millennium Development Goals.

Cambodian public institutions are a disadvantage to the country, believed to negatively affect the process of development. The perceived serious level of corruption and the weak enforcement of contracts and laws incite a lack of confidence among business people, investors and the public. The judiciary is seen as hardly independent from external

influences, while the legal framework is reported inefficient for private businesses to settle disputes or challenge the legality of the government's actions. Government decision making is not considered neutral.

Consistently with the findings of the World Bank's report, corruption has been judged pervasive in Cambodia, the leading constraint for doing business in Cambodia. The use of unofficial payments is still widespread in order to receive satisfactory public services.

Being a technology follower, Cambodia is believed to obtain technology mainly from FDI's. With an unclear policy towards the promotion of ICT, Cambodia's weaknesses can be identified in various areas such as a low level of technological readiness; rare company spending on research and development; limited internet access in schools; insufficient competition among ISPs; and unavailability of laws relating to ICT.

Table A1.1 : Growth Competitiveness Index for 2005 (Selected Countries)

	GCI		Macroeconomic environment Index		Public Institutions Index		Technology Index	
Country	Rank	Score*	Rank	Score*	Rank	Score*	Rank	Score*
Finland	1	5.94	4	5.52	5	6.19	2	6.02
United States	2	5.81	23	5.07	18	5.77	1	6.19
Singapore	6	5.48	1	5.82	4	6.25	10	4.93
Japan	12	5.18	42	4.40	14	5.84	8	5.24
Thailand	36	4.50	26	4.94	41	4.88	43	3.69
China	49	4.07	33	4.61	56	4.41	64	3.18
Indonesia	74	3.53	64	3.89	89	3.58	66	3.13
Vietnam	81	3.37	60	3.96	97	3.43	92	2.72
Bangladesh	110	2.86	83	3.43	117	2.55	101	2.06
Cambodia	112	2.82	104	3.04	114	2.90	105	2.51
Paraguay	113	2.80	102	3.07	112	2.97	111	2.35
Benin	114	2.74	101	3.08	110	3.06	116	2.09
Guyana	115	2.73	113	2.77	109	3.01	112	2.34
Kyrgyz Republic	116	2.62	115	2.62	115	2.89	113	2.34
Chad	117	2.37	114	2.67	116	2.64	117	1.80

Source: World Economic Forum, *Global Competitiveness Report 2005-2006*, September 2005.

* 1: the least competitive, 7: the most competitive.

Cambodian human resources are perceived to be in general of low quality and low education. The public educational system was observed as very poor, hardly able to be the breeding ground for a competitive economy. Cambodian people were however perceived as

particularly willing to learn and very flexible, which was appreciated by the business community.

The majority of companies in Cambodia were recognized as deriving their competitiveness in international markets from local natural resources, which is a harmful situation as Cambodia's natural resources have dramatically declined during the past decade. In addition, the perceived lack of value added, foreign control of international distribution, unsophisticated production processes and the limited extent of marketing are notable weaknesses in the area of company operations and strategies.

As a relative concept, competitiveness only exists through comparison. Five countries were chosen as specific benchmarks in order to compare Cambodia's competitiveness: Thailand, China, Vietnam, Indonesia and Bangladesh. Overall, the benchmarking shows that Cambodia's competitiveness lags far behind its main neighbouring countries: Vietnam, Thailand, China and Indonesia, but is comparable to Bangladesh.

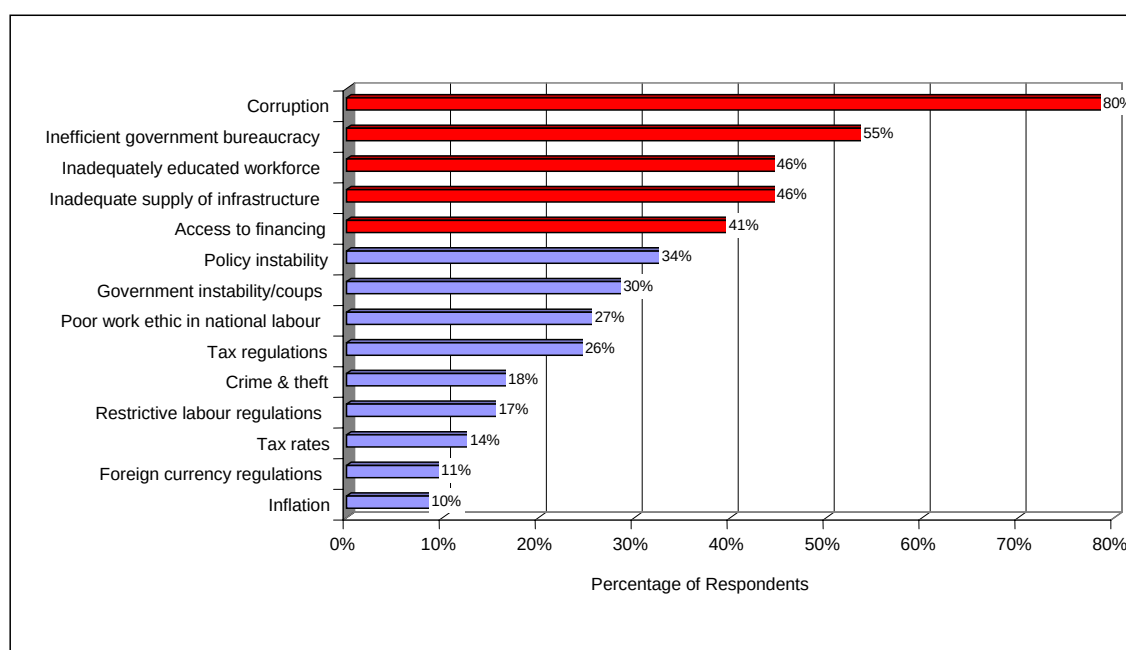
Out of the six countries, Cambodia's macroeconomic environment was viewed as the least favourable, although the business community was somewhat optimistic about the country's economy in the short-term. The country's relative weaknesses in this area are seen as high trade deficit, high public debt, high lending-borrowing interest rate spread and difficulty in receiving credit for business. The uncertain ability of the country to meet its debt obligation is another concern, reflecting the lowest country credit rating out of the benchmarking countries. Despite its small amount, the business community views government spending in Cambodia as less wasteful than in Bangladesh and Vietnam.

The perceived quality of Cambodian public institutions is among the worst in the world, and comparable with Bangladesh, while the other benchmark countries ranked higher. Noticeably, corruption is the most problematic factor for doing business in Cambodia, according to the business community. It has become more sensitive as compared to the parallel findings from the World Bank's investment climate in 2004. According to the opinion survey results, the second most problematic factor is an inefficient government bureaucracy, followed by an inadequate educated workforce, inadequate infrastructure and poor access to financing.

As a non-core economy, innovation is not an important source of technology in Cambodia, with technology being transferred through FDI. Usually, companies in Cambodia do not spend heavily on research and development. Neither do they have good business collaborations in R&D with local universities, causing Cambodia's level of technological readiness to lag far behind many other countries.

“Corruption is the most problematic issue that we face, because it really diminishes one’s willingness to invest. It also adds a lot of hidden cost. It is one of the biggest, if not the biggest challenge that we face.”

Figure 1: The Most Problematic Factors for Doing Business in Cambodia



Note: From a list of 14 factors, respondents were asked to select the five most problematic factors for doing business in Cambodia.

Source: EIC, Executive Opinion Survey 2005 in Cambodia, February-April 2005.

The quality of Cambodia's business environment ranks below Thailand, Indonesia, China, Vietnam and Bangladesh, which is the result of poor performances in the areas related to the four components of Porter's national competitive advantage: input conditions, demand conditions, related and supporting industry and context for firm strategy and rivalry. Particular notes should be observed in connection with the poor infrastructures (physical and administrative) input conditions and lack of supporting industry for business.

In order to remove Cambodia's business environment constraints and restore national competitiveness, critical reforms are necessary. Public administrative reforms were viewed as the most critical to achieve business development, followed by legal and judicial reforms, and financing and banking reforms.

"Certain reforms have to be done. But, really, it is a question of implementation. It depends on how the government is committed to execute the reforms. I believe that there is an effort. But the question is of following it through."

Governance and the rule of law must be ensured for public as well as investor confidence. Only then can Cambodia attract more investment, both domestic and foreign, that would bring in new, innovative and productive technology. Only when public institutions can deliver necessary services and corruption is curbed can the country's