INTERNATIONAL MONETARY FUND

IMF Country Report No. 17/325

CAMBODIA

2017 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR CAMBODIA

October 2017

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2017 Article IV consultation with Cambodia, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its September 22, 2017 consideration of the staff report that concluded the Article IV consultation with Cambodia.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on September 22, 2017, following discussions that ended on July 25, 2017, with the officials of Cambodia on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on August 30, 2017.
- An **Informational Annex** prepared by the IMF staff.
- A **Debt Sustainability Analysis** prepared by the staff of the IMF and the International Development Association (IDA).
- A **Statement by the Executive Director** for Cambodia.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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Press Release No. 17/405
FOR IMMEDIATE RELEASE
October 20, 2017

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Washington, D. C. 20431 USA

IMF Executive Board Concludes Article IV Consultation with Cambodia

On September 22, 2017, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Cambodia.[1]

Cambodia's economy is expected to grow by 6.9 percent this year, with moderating private investment offset by higher public spending and robust construction and tourism activities. Headline inflation rose to 3 percent in 2016 and 3.5 in the first half of 2017, mainly driven by higher food and energy prices.

Overall credit growth has slowed, owing in part to policy measures. Real estate sector-related bank credit growth, however, remains strong, supported by demand for housing from Cambodia's young and growing middle-income population.
The current account deficit narrowed to 8.8 percent of GDP in 2016. Driven by strong FDI inflows, foreign reserves have continued to grow, reaching $7.9 billion in June 2017, about 5.5 months of next year's imports.

While the authorities again outperformed their revenue target in 2016, higher current spending resulted in an increase of the fiscal deficit to around 2.8 percent of GDP (compared with 1.6 percent in 2015). The fiscal deficit is expected to widen further this year due to higher public sector wages and other election-related current spending.

Looking ahead, the outlook is positive, although challenges remain. Real GDP growth is projected to remain robust over the next few years. Growth is then expected to slow over the medium-term to around 6 percent, due to moderation in the credit and real-estate cycles and ongoing challenges in improving economic diversification and competitiveness.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

Executive Board Assessment[2]

Executive Directors commended the authorities for Cambodia's impressive economic growth over the past few years, which has benefited from a stable macroeconomic environment and efficiency improvements. Directors were encouraged by the dramatic gains in poverty reduction over the past two decades. They considered that, with a robust external environment and strong domestic fundamentals supporting investment, Cambodia's economic outlook is positive. Directors noted, however, that the outlook is subject to downside risks stemming from elevated financial sector vulnerabilities, as well as the external outlook, including weaker-than-expected growth in Cambodia's main trading partners. Against this background, Directors encouraged the authorities to strengthen the fiscal position, safeguard financial sector stability, and implement reforms to boost competitiveness and the business climate.

Directors welcomed policy measures to bolster financial stability, which have helped moderate credit growth, and ongoing efforts to address vulnerabilities. They considered that further targeted prudential policies will be key to containing macro-financial risks. Priorities include strengthening regulations on loan classification to better manage credit risk; introduction of additional targeted macro-prudential policies, including gradually increasing reserve requirements on foreign exchange liabilities to build liquidity buffers; and expediting collection of data on the real-estate sector. Directors considered that the growing systemic relevance of large deposit-taking micro-finance institutions warrants strengthening prudential regulation, and saw merit in the development of a comprehensive crisis management framework. Implementation of the remaining FSAP recommendations was also encouraged.

Directors welcomed efforts to promote financial market development and steps that have been taken to improve financial inclusion. However, they noted that Cambodia's high level of dollarization contributes to vulnerabilities and limits the scope for monetary policy. Directors underlined the importance of expanding use of the local currency and developing the equity, interbank, government and corporate bond, and foreign exchange markets. Further efforts to promote inclusion should focus on improving financial literacy and consumer protection and introducing a comprehensive financial inclusion strategy, which would help address risks, while at the same time fostering innovation and competition.

Directors commended the improvements in tax administration, which have led to large revenue increases and the accumulation of government deposits, as well as the planned framework for social protection. To ensure that the recent gains are sustained, further improvements in revenue administration and tax policy modernization are needed. Directors emphasized that fiscal deficits should be contained to safeguard fiscal and external sustainability. Further public wage increases should be fiscally sustainable and be accompanied by continued progress in public

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[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

administration reforms, while spending on education and health should be safeguarded. Directors underscored that developing a medium-term budget framework would improve spending efficiency, while strengthening the framework for public-private partnership would better manage fiscal costs and risks.

Directors encouraged the authorities to accelerate the implementation of structural reforms to promote economic diversification, boost competitiveness, and improve the business climate and inclusiveness. They recommended that efforts should continue to focus on lowering energy costs, accelerating implementation of the Industrial Development Policy, upgrading infrastructure, strengthening the rule of law and transparency, and further investing in human capital. Including the impact of climate change and mitigating measures in policy design would improve resilience.

Table 1. Cambodia: Selected Economic Indicators, 2012–18

	2012	2013	2014	2015	2016	2017	2018
						Est.	Proj.
Output and prices (annual percent change)							
GDP in constant prices	7.3	7.4	7.1	7.2	7.0	6.9	6.8
(Excluding agriculture)	8.3	9.5	9.2	9.2	8.5	8.3	8.0
Inflation (end-year)	2.5	4.7	1.0	2.8	3.9	3.1	3.4
(Annual average)	2.9	3.0	3.9	1.2	3.0	3.7	3.5
Saving and investment balance (in percent of GDP)							
Gross national saving	15.3	10.5	13.4	13.1	14.1	13.6	13.4
Government saving	1.9	2.2	3.4	3.8	2.8	1.5	0.4
Private saving	13.4	8.4	10.0	9.3	11.3	12.2	13.0
Gross fixed investment	23.5	23.5	23.2	22.4	22.9	22.2	22.0
Government investment	9.0	8.9	8.0	6.9	7.8	8.2	8.6
Private investment 1/	14.5	14.6	15.2	15.5	15.1	14.0	13.4
Money and credit (annual percent change, unless otherwise indicated)							
Broad money	20.9	14.6	29.9	14.7	18.0	14.4	12.9
Private sector credit	38.3	17.3	31.3	27.1	22.5	12.5	10.0
Velocity of money 2/	2.2	2.0	1.8	1.6	1.6	1.4	1.3
Public finance (in percent of GDP)							
Revenue	16.9	18.5	19.8	18.8	19.8	19.5	19.6
Domestic revenue	14.2	14.6	16.9	16.5	17.9	18.0	18.1
Of which: Tax revenue	11.3	11.8	13.8	14.5	15.3	15.3	15.3
Grants	2.8	3.9	3.0	2.3	2.0	1.5	1.5
Expenditure	20.7	20.7	21.0	20.4	22.7	23.2	24.1
Expense	12.0	12.0	13.1	13.2	14.9	15.0	15.6
Net acquisition of nonfinancial assets	8.7	8.7	7.9	7.1	7.8	8.2	8.5
Net lending (+)/borrowing (-)	-3.8	-2.1	-1.1	-1.6	-2.8	-3.7	-4.6
Net lending (+)/borrowing (-) excluding grants 3/	-6.3	-6.4	-4.2	-3.2	-4.7	-5.2	-6.0
Net acquisition of financial assets	0.6	0.5	2.3	2.8	2.1	0.6	-0.5
Net incurrence of liabilities 4/	4.4	2.6	3.5	4.4	4.9	4.2	4.1
Of which: Domestic financing	0.7	-0.5	-1.5	-0.7	0.2	0.0	1.0
Government deposits	4.9	5.0	6.9	9.1	10.1	9.7	8.3
Balance of payments (in millions of dollars, unless otherwise indicated)							
Exports, f.o.b.	5,633	6,530	7,407	8,453	9,233	10,112	11,041
(Annual percent change)	11.9	15.9	13.4	14.1	9.2	9.5	9.2
			-	-	-		-
Imports, f.o.b.	-8,139	-9,749	10,613	11,920	12,649	-13,717	15,053
(Annual percent change)	13.4	19.8	8.9	12.3	6.1	8.4	9.7
Current account (including official transfers)	-1,150	-1,979	-1,641	-1,694	-1,776	-1,904	-2,098
(In percent of GDP)	-8.2	-13.0	-9.8	-9.3	-8.8	-8.6	-8.6
Gross official reserves	3,463	3,642	4,391	5,093	6,731	8,097	8,955
(In months of prospective imports)	3.6	3.5	3.8	4.2	5.0	5.5	5.6
External debt (in millions of dollars, unless otherwise indicated)							
Public external debt	4,852	5,269	5,610	6,457	7,267	8,216	9,100
(In percent of GDP)	31.6	31.6	31.8	30.8	31.9	32.8	34.0
Public debt service	112	143	172	239	244	192	313
(In percent of exports of goods and services)	1.3	1.4	1.5	1.9	1.8	1.3	1.9
Memorandum items:							
Nominal GDP (in billions of riels)	56,650	61,414	67,485	73,694	81,703	90,325	99,753
(In millions of U.S. dollars)	14,049	15,249	16,714	18,150	20,157	22,252	24,307
Exchange rate (riels per dollar; period average)	4,032	4,027	4,038	4,060	4,053	…	…

Sources: Cambodian authorities; and IMF staff estimates and projections.

1/ Ratio of nominal GDP to the average stock of broad money.

2/ According to GFS 86 used by Cambodian authorities.

3/ Includes statistical discrepancy.

4/ Excludes unrestricted foreign currency deposits held as reserves at the National Bank of Cambodia; starting in 2009, includes the new SDR allocations made by the IMF of SDR 68.4 million.

INTERNATIONAL MONETARY FUND

CAMBODIA

STAFF REPORT FOR THE 2017 ARTICLE IV CONSULTATION

August 30, 2017

KEY ISSUES

Context. Cambodia continues to grow at an impressive pace. Looking ahead, the outlook is positive, although there are near-term downside risks. Financial sector vulnerabilities stemming from rapid financial deepening remain elevated despite a recent slowdown in credit growth. Revenue performance has been strong, but spending pressures are contributing to larger fiscal deficits. Medium-term prospects are favorable, though important challenges remain.

Policy priorities.

- **Managing macro-financial risks.** Further prudential measures are needed to improve resilience and address elevated financial sector vulnerabilities. This includes effective implementation of past measures to build liquidity and capital buffers, gradual increases in reserve requirements, introduction of a crisis management framework, and continued upgrading in regulation and supervision, including for non-bank financial institutions.
- **Safeguarding fiscal sustainability.** Spending pressures should be contained, including to ensure that wage increases are consistent with fiscal sustainability and priority is given to development spending. Further efforts are needed to modernize tax administration and policies to achieve sustained improvements in revenue. Developing a medium term fiscal framework would facilitate policy planning and effective resource allocation. Improving the public-private partnership framework would help manage fiscal costs and risks while addressing infrastructure bottlenecks.
- **Reforms to support growth, resilience and inclusion.** Structural reforms are needed to increase competitiveness and encourage diversification through lower energy costs, continued upgrading of human capital and infrastructure, and stronger rule of law and transparency. Promoting further financial market development and reforms to encourage local currency use would help increase resilience. Use of financial technology, further developing financial infrastructure and improving financial literacy can help expand financial inclusion.

Approved By
Markus Rodlauer and Yan Sun

Discussions took place during July 12–25, 2017. The mission team comprised Jarkko Turunen (Head), Tadaaki Ikoma, Sohrab Rafiq, Katsiaryna Svirydzenka (all APD), and Yong Sarah Zhou (Resident Representative). Markus Rodlauer (APD) joined the concluding meetings. Ms. Edna Villa and Mr. Kaweevudh Sumawong (both OED) participated in some meetings. Vipichbolreach Long, Simon Paroutzoglou and Ross Rattanasena assisted in this report's preparation.

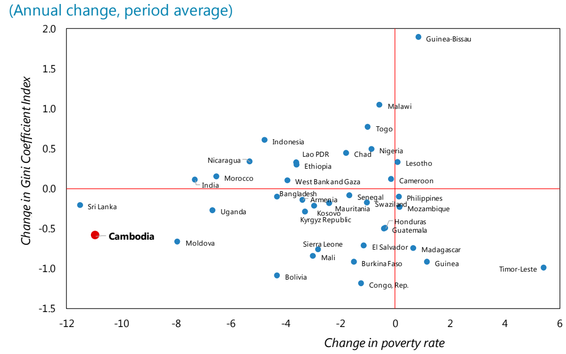
CONTENTS

APPENDICES

RECENT DEVELOPMENTS, OUTLOOK AND RISKS

1. **Context.** Cambodia is a fast-growing, small, open economy. Robust growth over the past few years has benefited from a stable macroeconomic environment, efficiency improvements supported by an open and market-oriented economy, as well as the country's geographical location in the world's fastest-growing region and its relatively young population. Poverty has fallen, although a significant share of the population still lives just above the poverty line.

Cambodia: Poverty Reduction and Income Inequality, 2002–2013 1/
(Annual change, period average)

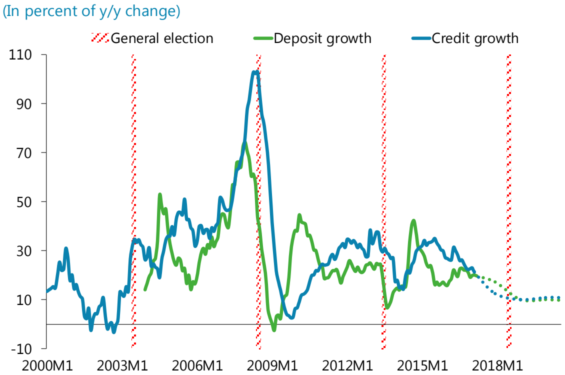


Sources: World Bank; and IMF staff calculations.
1/ Selected countries: low income countries and lower middle income countries; selected period: closest period to 2002–2013. National Poverty line is used to measure poverty rate.

2. **Robust economic activity.** Domestic investors are in wait-and-see mode ahead of next year's national elections. Real GDP growth is nevertheless expected to remain robust at around 7 percent this year, with moderating private investment offset by higher public spending and robust construction and tourism activity. Headline inflation rose to 3 percent (average) in 2016 and around 3.5 percent (average) in the first half of 2017, mainly driven by higher food and energy prices (Box 1).

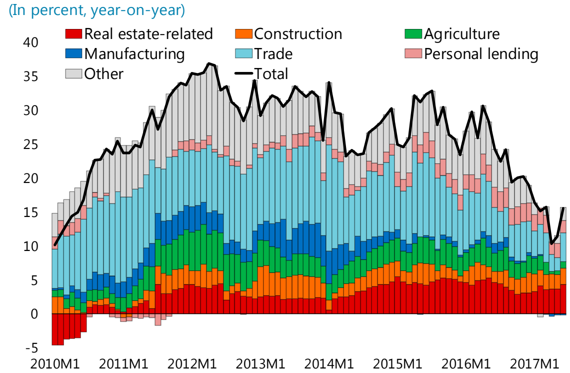
3. **Slower credit growth.** Bank credit growth has slowed to about 15 percent (year-on-year) in May 2017, from an average of 30 percent over the past few years. This moderation is due in part to policy measures, as well as lower demand for credit for private investment owing to election related uncertainties. While the number of microfinance institutions (MFIs) continues to grow, MFI credit growth also slowed down (to 24 percent at end-2016 compared with over 50 percent the past few years).[1] Real estate sector-related bank credit growth remains strong, supported by demand for housing from Cambodia's young and growing middle-income

Cambodia: Credit and Deposit Growth
(In percent of y/y change)



Sources: Cambodian authorities; and Fund staff calculation.

Cambodia: Contribution to Credit Growth
(In percent, year-on-year)



Sources: NBC; and IMF staff calculations.

[1] Official MFI credit growth is 4.8 percent at end-2016. However, this partly reflects a merger between a second-largest MFI (Sathapana Microfinance) and a bank (Maruhan Bank) in 2016.

population. Anecdotal evidence, however, suggests that some segments of the property market are cooling.

4. **Moderating current account deficit.** The current account deficit narrowed to 8.8 percent of GDP in 2016. While the first half of 2017 saw a slowdown in garment exports growth, tourist arrivals grew by a robust 12.8 percent (compared to 2.6 percent last year), primarily driven by arrivals from China. Significant FDI and other capital inflows have helped fuel construction and real estate sector growth. As a result, foreign reserves continued to grow, reaching $7.9 billion in June 2017, about 5.5 months of next year's imports.

5. **Widening fiscal deficits.** Continued Revenue Mobilization Strategy (RMS) implementation coupled with robust growth and administrative efforts, such as more stringent audits, have boosted tax revenues from around 11 percent of GDP in 2012 to 15.3 percent in 2016. While the authorities again outperformed their revenue target in 2016, higher current spending resulted in an increase of the fiscal deficit to around 2.8 percent of GDP (compared with 1.6 percent in 2015). The fiscal deficit is expected to widen further this year owing to higher public sector wages and other current spending.

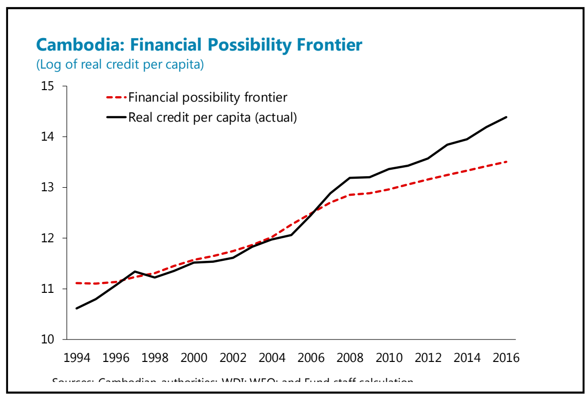
6. **Positive outlook.** Real GDP growth is projected to remain robust at around 7 percent over the next few years. Growth is then expected to slow down over the medium-term to around 6 percent, owing to moderation in the credit and real-estate cycles, coupled with ongoing challenges in improving economic diversification and competitiveness. The garment sector is expected to grow at a slower pace owing to increasing competition from neighboring countries and a higher minimum wage. Manufacturing exports will benefit from an extension of preferential US trade access for specific travel-related items and some product diversification. Continued regional economic integration is expected to support Foreign Direct Investment (FDI) and other capital inflows. These factors should support economic activity and narrow the current account deficit over the medium-term. Inflation is projected to rise in the short-term, reflecting higher food and energy prices as well as demand pressures from higher public spending and wages. A moderation in the pace of government revenue growth and rising spending pressures, including public wage increases and spending to support social programs and infrastructure, are expected to result in higher fiscal deficits and lower government deposits over the medium term.

7. **Significant downside risks.** While overall credit growth has moderated, concerns about credit quality, concentration in the real estate sector, reliance on external funding, and growing importance of MFIs continue to pose risks to financial and macroeconomic stability. With a closely managed exchange rate, large increases in the minimum wage could further erode competitiveness, particularly in the key garment sector. Potential social unrest in the run-up to next year's general elections could dampen confidence. External risks include weaker growth in China, which would have significant negative spillovers through FDI, banking, and tourism channels. A growth slowdown in advanced economies, stronger-than-expected U.S. dollar, or rise in protectionism could dent garments exports and tourism growth. Sharper than expected global financial tightening could raise funding costs and heighten liquidity risks (Appendix I)

8. Authorities' views. There was a broad agreement on the macroeconomic outlook and risks. The authorities continue to aim for sustained growth at 7 percent and agreed on the need to implement structural reforms to achieve that goal over the medium-term. The authorities emphasized their efforts to mitigate potential macro-financial risks. On external risks, the authorities considered that positive investor sentiment and strong domestic fundamentals would mitigate the impact of a potential tightening of global financial conditions on capital inflows.

MANAGING MACRO-FINANCIAL RISKS

9. Sustained financial deepening. Rapid credit growth, sustained for the past several years, has led to significant increase in the bank credit-to-GDP ratio (to close to 70 percent). The real per capita credit gap, a measure of excessive credit growth, peaked in early 2016 and, while having declined, remains high at around 10 percent.[2] While distinguishing between healthy financial development and excess credit is fraught with challenges, the level of financial development is closely related to a country's economic development. Benchmarking against other emerging and frontier market economies also suggests that credit growth has been faster than implied by structural fundamentals ("the financial possibility frontier").[3] Credit has continued to grow in 2017, albeit at a less rapid pace, and the banking sector continues to attract sizeable FDI inflows. Credit growth is expected to moderate somewhat this year and next, in part owing to lower private investment and policy measures, but—barring additional measures to contain it—is projected to remain elevated over the medium term. Projections assume that the real per capita credit gap declines to about 5 percent over the medium-term, reflecting tightening global financial conditions and maturation of the credit and real-estate cycles.

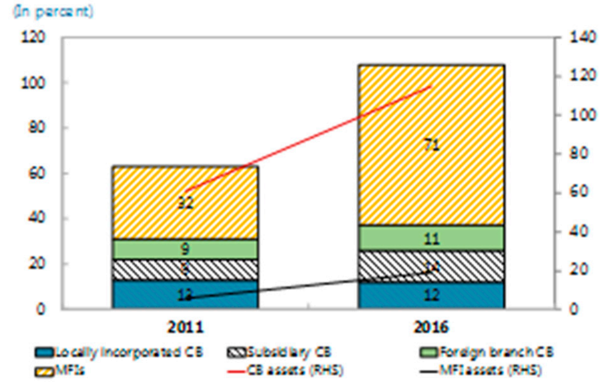


10. Elevated macro-financial risks. Despite slower credit growth, elevated financial sector vulnerabilities related to (i) credit quality, (ii) real-estate sector concentration, (iii) significant reliance on external funding and (iv) growing importance of MFIs continue to pose significant risks. First, deficiencies in the current regulatory framework complicate early identification of emerging risks. Existing loan classification definitions are drawn too broadly and fail to capture adequately potential evergreening. While the system-wide non-performing loan (NPL) ratio remains low at 2.5 percent in June 2017, weaknesses in loan classification may result in

[2] The gap is defined as the deviation of real credit (deflated by CPI inflation) per capita from its trend. Other gap measures point to similar conclusions. A threshold of 10 percent is considered a strong signal of an impending crisis (see e.g., Drehman et al., 2010).
[3] For the methodology, see Barajas et al. (2013) "Too Cold, Too Hot, Or Just Right? Assessing Financial Sector Development Across the Globe," IMF Working Paper No. 13/81.

underreporting and, coupled with difficulties in asset classification, lead to an overstatement of the system-wide capital adequacy ratio. Second, credit to the real estate-related and construction sectors continues to grow rapidly, with growth of about 33 percent (year-on-year) in June 2017, contributing to growing sectoral concentration and heightened credit risks associated with a potential fall in real estate prices. Third, the banking sector continues to rely on external borrowing, with the system wide loan-to-deposit (LTD) ratio reaching 105 percent in May 2017. Finally, while less stringent regulation has allowed the MFI sector to contribute to improving financial inclusion, recent growth of large deposit taking MFIs (MDIs) has further increased their systemic role. They rely mainly on external borrowing and receive some funding from domestic banks, with MDIs' LTD ratio at more than 200 percent on average.

Cambodia: Number of Institutions and Assets to GDP
(In percent)



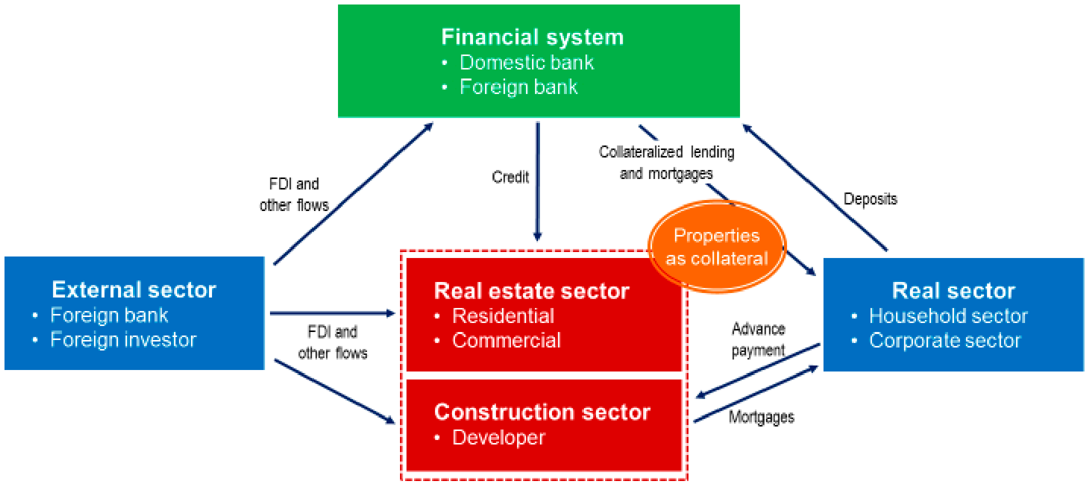
Sources: National Bank of Cambodia, Annual Supervision Report 2011-2016; and IMF staff calculations.

Text Table 1. Cambodia: Selected Financial Soundness Indicators (FSIs), 2011–17
(In percent)

	2011	2012	2013	2014	2015	2016	2017 Mar.
Capital Adequacy							
Regulatory capital to risk-weighted assets	26.2	25.0	24.2	20.4	20.3	20.9	22.6
Asset Quality							
Nonperforming loans to total gross loans	2.1	2.0	2.3	1.6	1.6	2.1	2.2
Earnings and Profitability							
Return on equity 1/	9.7	10.3	12.1	15.5	16.3	14.5	15.2
Return on assets 1/	1.8	1.7	2.4	2.9	2.9	2.5	2.6
Interest margin to gross income	64.3	66.7	68.6	72.9	63.1	65.3	63.5
Liquidity							
Liquid assets to total assets	16.2	15.4	17.9	16.2	16.6	15.8	16.2
Liquid assets to short-term liabilities	23.0	21.2	24.2	23.1	25.4	24.3	24.9
Sensitivity to Market Risk							
Net open position in foreign exchange to capital	3.9	2.0	9.4	4.1	3.6	2.6	2.1

Source: National Bank of Cambodia.
1/ Annualized.

Text Figure 1. Cambodia: Funding for the Real Estate Sector



Source: IMF Staff.

11. Policies to address stability risks. The authorities have introduced several policy measures, including (i) continued phased implementation of a Liquidity Coverage Ratio and higher minimum capital requirements[4]; (ii) bank-specific prudential measures (including higher minimum capital requirements and strengthened governance) for institutions deemed to be taking excessive risks; and (iii) liquidity-providing collateralized operations, established in October 2016 to provide lower-cost local currency (Riel) liquidity. The authorities are also preparing regulation to improve loan classification, introduce a liquidity management framework and capital conservation buffers, and strengthen regulation of microfinance institutions. The MFI interest rate cap (at 18 percent) introduced in April this year is expected to result in challenges for some institutions, likely leading to consolidation and reduction in financial access, and could potentially encourage informal lending practices, particularly in rural areas. International evidence suggests that interest rate caps are not an effective tool to increase access to low-cost credit, and that fundamental reforms to reduce funding and operational costs, and to improve financial literacy and consumer protection are needed instead.

[4] The NBC raised minimum capital requirement for banks from $37.5 million to $75 million, for branches of foreign banks with an investment grade rating from $12.5 million to $50 million, and for deposit-taking microfinance institutions from $2.5 million to $30 million. Banks are mandated to increase their capital by at least half of the additional required capital by March 2017 and to meet the requirement in full by March 2018.

Text Table 2. Cambodia: Policy Recommendations for Safeguarding Financial Stability

Priority	Policy Objective	Short-term	Medium-term
High	*Contain real estate sector growth*	Improve sectoral loan classification Collect real estate data	Impose sectoral limits Consider imposing LTV/DTI limits
	Mitigate liquidity risks	Implement LCR and introduce liquidity risk management framework	Gradually raise RR for foreign currency liabilities Consider funding requirements (e.g. LTD limits)
	Develop crisis management	Strengthen prompt corrective action to take early action	Develop deposit protection scheme and resolution framework
	Ensure adequate capital buffers	Implement new minimum capital requirements Strengthen existing prudential policies (e.g. asset classification and provisioning rules)	Introduce capital conservation buffers and counter-cyclical capital requirements
Medium	*Upgrade non-bank regulations*		Identify systemically important MFIs and monitor interlinkages Upgrade regulations on MDIs broadly in line with commercial banks

* Measures: Macro-prudential measures

12. Policy recommendations. Near-full financial dollarization and commitment to a closely managed exchange rate leave little room for independent monetary policy. The authorities are encouraged to continue building foreign reserves given elevated vulnerabilities and high dollarization, and to maintain sufficient government deposits. While recent steps to strengthen prudential policies are to be commended, further efforts are required, including to expedite the implementation of outstanding FSAP recommendations. The authorities should continue to seek measures that address risks without aiming to limit capital flows.

- **Better managing credit risk.** The authorities should focus on (i) implementing the revised regulation on loan classification to improve bank reporting of NPLs; (ii) revising existing regulations on related-party lending and large exposures to align them with international best practice; and (iii) conducting regular validation exercises to ensure accurate reporting.

- **Targeted prudential policies**. A further gradual increase in reserve requirements on foreign exchange liabilities is needed to ensure sufficient liquidity buffers and promote use of the Riel. Other measures targeted at specific vulnerabilities include: (i) improving sectoral asset classification would enable the introduction of sectoral concentration limits and/or higher risk weights for real-estate loans; (ii) expedited collection of data on the real-estate sector and household balance sheets to enable the introduction of limits on debt-to-income and loan-to-value ratios; (iii) introduction of a liquidity risk management framework; (iv) potential funding requirements such as limits on LTD ratios would ensure that banks hold more internal and stable liabilities; (iv) introduction of capital conservation buffers and counter-cyclical capital requirements as tools to further build buffers.

- **Strengthening non-bank regulation.** The systemic relevance of MFIs calls for strengthening regulation to prevent regulatory arbitrage. Policies should standardize asset classification, unify accounting and provisioning standards between MFIs and banks, adjust reserve requirements for deposit-taking MFIs to be in line with banks and improve monitoring of systemic linkages. The need to strengthen regulatory capacity and move to risk-based supervision also applies to the emerging insurance sector.

- **Introducing a comprehensive crisis management framework.** Further work towards a comprehensive framework is needed. The National Bank of Cambodia (NBC) is working to introduce a framework for prompt corrective action and progress has been made in establishing a multi-agency financial stability committee and introducing a deposit protection scheme.

13. Authorities' views. The authorities agreed with the need for further measures, broadly in line with staff's recommendations. However, they argued that before introducing further measures that could slow credit growth down further more time was needed to assess the impact from past measures. The authorities agreed on the need to better monitor risks related to the real estate sector and have established an inter-agency working group to collect data. They noted strong demand for affordable housing from the emerging middle-class and continued monitoring banks' internal rules governing LTV ratios for mortgages, which appear conservative. The authorities argued that external funding consisted of mostly longer-term funding from parent banks (to banks) and from financial institutions with development purposes (to MFIs), thus mitigating liquidity risks. They agreed that the interest rate cap on MFI lending could lead to challenges, but expect that over time, it could also lead to efficiency improvements by encouraging consolidation and reductions in operational costs.

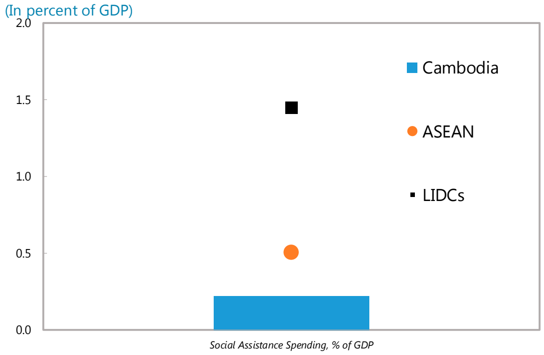
SAFEGUARDING FISCAL SUSTAINABILITY

14. Fiscal outlook. The authorities continue to rely largely on administrative measures, such as more stringent audits, to mobilize revenues. While the budget revenue target is likely to be exceeded slightly this year, the fiscal deficit is expected to widen (to about 3.7 percent of GDP) owing to higher capital spending, increases in public sector wages and other election-related spending. Government deposits are projected to be around 9.7 percent of GDP in 2017, a level that is considered adequate. Priorities for the 2018 budget include a further increase in public wages, support for education (including for vocational training) and agriculture, as well as higher infrastructure investment. Preliminary budget figures suggest a further increase in the fiscal deficit to about 4.6 percent of GDP in 2018. Public sector salaries are projected to rise further while capital spending is projected to increase to 8.5 percent of GDP.[5]

[5] The government has previously pledged to increase minimum wages for civil servants, military and armed police to US$250 dollars by 2018.

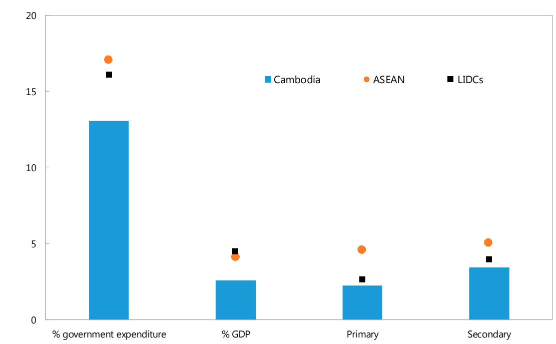
15. Rising medium-term fiscal pressures. A moderation in the pace of revenue growth and rising spending pressures would—absent corrective measures— result in elevated fiscal deficits over the medium term which in turn would erode government deposits below comfortable levels. On the revenue side growth in international trade taxes is expected to decline as tariffs are cut in line with regional free trade arrangements, while growth in domestic taxes is expected to moderate as gains from RMS implementation mature. Moreover, development-related grants are expected to decline due to the achievement of lower middle-income status. On the expenditure side, the government is facing mounting pressure to increase social spending, which remains the lowest in the region. Public wage pressures are likely to remain strong (even though staff projections keep them at pace with nominal GDP growth) and investment spending needs will remain large given significant infrastructure gaps.

Cambodia: Social Assistance Spending
(In percent of GDP)



Sources: : IMF FAD Expenditure Assessment Tool (EAT), World Economic Outlook, ASPIRE, and IMF Pension Indicators.

Cambodia: Government Education Expenditure, Latest Value Available



Source: IMF FAD Expenditure ASsessment Tool (EAT), World Bank.

Reflecting these trends, and absent additional measures, fiscal deficits are projected to trend upward, the expenditure mix to deteriorate and become less growth-friendly and government deposits to fall below comfortable levels. In the absence of alternative financing sources due to under-developed capital markets, adequate government deposits (an important fiscal anchor) will be essential to maintain sufficient buffers in the event of shocks.[6] The Debt Sustainability Analysis suggests that the risk of debt distress remains low, but increasing risks to the debt outlook call for continuous monitoring of debt dynamics.

16. Policy recommendations. Against this background, further efforts starting next year are needed to moderate spending growth and sustain revenue performance (see Text Table 3).

- **Containing near-term fiscal deficits.** To safeguard fiscal and external sustainability, and in view of medium term spending pressures, any revenue overperformance should be saved and non-development current expenditure curtailed, by continuing to enhance spending efficiency, particularly regarding public sector wages. Together with other policy measures,

[6] Staff analysis presented in the 2015 Article IV report suggests a floor on the level of government deposits at about 5.5 percent of GDP.

lower near-term deficits would help stabilize government deposits at around 6.5 percent of GDP over the medium-term.

- **Ensuring sustained revenue improvement**. The authorities should re-invigorate the RMS to ensure sustained revenue improvement. Strengthening the institutional development of the tax administration agency, especially the Large Taxpayer Department, is needed to facilitate future tax policy reforms. In preparation for the next RMS, the authorities should consider undertaking a tax administration diagnostic assessment. A new diagnostic would provide an up-to-date assessment of tax administration benchmarked against good practices, and thereby provide targeted policy advice on priority areas. Tax policy reforms are needed to sustain improvements in tax revenue over time and should initially focus on tax incentives (to improve their effectiveness and efficiency) and excise taxes, and over the medium term aim at reforming VAT and personal income taxes, and increasing property taxes.

- **Prioritizing development spending.** Plans to boost social protection spending, as reflected also in the government's Social Protection Policy Framework, are welcome. However, public education and health expenditure is expected to remain below peers and further prioritization is needed as revenue gains are secured.

Text Table 3. Cambodia: Active Fiscal Policy Scenario (GFSM 2001)

(In percent of GDP)

	2017	2018	2019	2020	2021	2022
Revenue	19.5	19.7	20.0	20.5	20.5	20.9
of which : Tax Revenues	15.3	15.5	15.6	15.8	16.0	16.3
Expenditure	23.2	24.1	24.1	24.1	24.2	24.2
Wage	7.9	8.4	8.4	8.4	8.4	8.4
Non-wage	7.1	7.2	7.3	7.3	7.3	7.3
Net Acquisition of Non-Financial Assets	8.2	8.5	8.5	8.5	8.5	8.5
Overall Balance	-3.7	-4.4	-4.1	-3.7	-3.6	-3.3
Government Deposits	9.7	8.5	7.5	7.0	6.6	6.6
Memorandum items:						
Baseline Overall Balance	-3.7	-4.6	-4.4	-4.0	-4.0	-3.8
Baseline Government Deposits	9.7	8.3	7.1	6.2	5.6	5.1

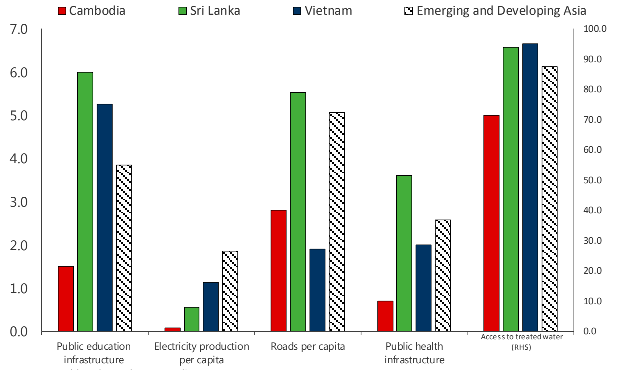
Sources: Data provided by the Cambodian authorities; and IMF staff estimates and projections.

- **Sustainable wage increases.** Keeping wage increases on a sustainable path will help moderate growth in current spending and support a more growth and development friendly composition of spending over the medium term. Further wage increases should be contingent on meeting revenue targets and maintaining adequate fiscal buffers, and accompanied by further progress in public administration reforms. This includes strong efforts to strengthen human resource management, including to increase skills and labor productivity, improve spending efficiency, and enhance transparency. Balancing fiscal sustainability and competitive civil service salaries will require careful targeting of incentives.

- **Medium Term Fiscal Framework (MTFF).** The authorities should push ahead with developing a multi-year budget framework to allocate expenditure more systematically.

17. Financing infrastructure investment. Infrastructure gaps remain large, especially in electricity, health, education and road infrastructure, where Cambodia scores below regional peers.[7] This calls for increasing domestically financed public investment to maintain public investment at about 8.5 percent of GDP (see Text Table 3). With lower access to concessional finance in the coming years (owing to the attainment of lower middle income status), and slow progress in developing domestic debt markets, the authorities plan to increase the share of PPPs in public investment. They have established a roadmap to have a full set of PPP mechanisms in place by 2020. The aim is to limit fiscal costs and keep government debt low, while closing the large infrastructure gap. Although PPPs can increase efficiency and increase value for money relative to public financing, their fiscal implications are hard to monitor and control. Managing fiscal costs and risks will therefore require strengthening the PPP framework (Box 2).

Cambodia: Measures of Infrastructure Access
(Most Recent Year)



Source: World Bank Development Indicators.

18. Authorities' views. The authorities broadly agreed with staff's assessment and key policy recommendations. On the revenue side, they agreed with the need for higher revenues to meet rising spending pressures, especially in wage and infrastructure. While arguing that significant progress had been made in RMS implementation, the authorities concurred that achieving further gains through administrative measures would become increasingly challenging. They expected the next RMS phase (from 2019–2023) to focus on reforms in tax policies to boost revenues and improve efficiency. On expenditures, Public Financial Management (PFM) reforms, which include an expansion of program budgeting to almost all line ministries, had improved spending control. The authorities agreed on the importance of developing a MTFF, which they hoped to introduce in the medium term. They would continue to monitor the public wage bill closely to ensure sustainability and link medium term wage increases with progress in public administration reforms. They also acknowledged the need to

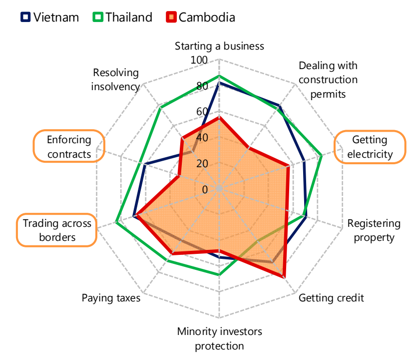
[7] The 2016 Article IV identified large infrastructure gaps. Higher public investment, financed by improved revenue collection and productivity improvements, is estimated to have a strong positive growth impact.

develop a well-designed PPP framework and expected to remain conservative in their approach to external borrowing.

REFORMS TO SUPPORT GROWTH, RESILIENCE AND INCLUSION

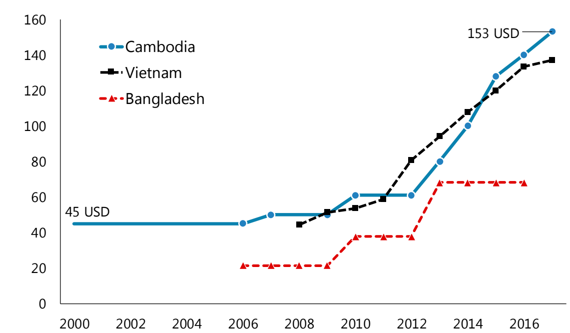
19. Structural policies to address constraints to growth and enhance resilience. Structural constraints include: (i) a narrow economic base, with exports relying largely on low-value added garments and footwear; (ii) weak business climate reflected in high cost of doing business, poor infrastructure, weak governance and low competitiveness (also owing to rising minimum wages); and (iii) underdeveloped financial markets. Accelerated implementation of the Industrial Development Policy (IDP) would spur growth of small-and-medium-sized enterprises and help Cambodia find a place in regional value chains. The planned National Logistics Council would help coordinate infrastructure plans. Recent education reforms include reforming the examination system, and increasing the quality of teaching by offering more training and increasing teachers' salaries on a merit basis. The authorities should continue focusing on reforms to provide low-cost, reliable and adequate electricity, enhancing transportation links, addressing skill gaps, strengthening governance, the rule of law and increasing transparency of business regulation.[8] The authorities are urged to address the issues identified in the recently-conducted AML/CFT mutual evaluation. Climate change is expected to have negative impact on climate-sensitive sectors, especially agriculture and tourism, with spillover effects on other sectors as well as on poverty reduction efforts. Internalizing climate change impact in the design of macroeconomic policies as well as structural reforms to improve productivity, especially in agriculture, and to diversify the economy would increase resilience (Box 3).

Cambodia: Ease of Doing Business
(Distance from the frontier; 0=farthest, 100=closest)



Source: World Bank, *Ease of Doing Business 2017*.

Cambodia: Minimum Monthly Wages - Garment Industry
(US dollars)



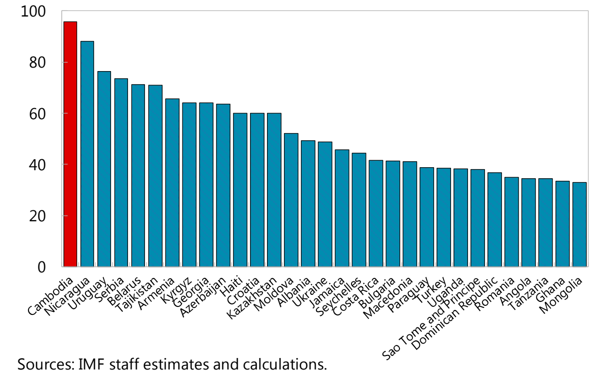
Sources: Cambodian, Bangladeshi and Vietnamese authorities; and IMF staff estimates and calculations.

[8] For example, according to the World Bank's Doing Business indicator, contract enforcement takes too long and is too costly, and as a result, Cambodia stands towards the bottom (at 178 out of 190 economies) on the ease of enforcing contracts.

20. Encouraging Riel use. High dollarization increases banks' vulnerability to liquidity risks in the context of rapid financial deepening and limits the scope for exchange rate and monetary policies. The authorities have taken welcome measures to promote Riel use, including by requiring a minimum of 10 percent of the loan portfolio to be in Riel by 2019 and obliging businesses registered with government to post prices in Riel. Further recommended measures include: (i) reallocating the renumeration currently paid on USD reserve requirement to Riel denominated reserve requirement, Negotiable Certificates of Deposits (NCDs), and excess reserves; (ii) gradually increasing the reserve requirement on foreign exchange liabilities, a key prudential tool in dollarized economies; (iii) monitoring unhedged exchange rate risk exposures and ensuring that they remain within prudent limits; and (iv) systematically factoring in dollarization risk in prudential regulation. Beyond these measures, encouraging Riel use requires a multi-pronged approach and close inter-agency collaboration. This includes effectively enforcing the requirement for prices to be labeled in Riel, requiring all government transactions to be based on Riel, and other market-based policies to improve Riel's attractiveness, such as ensuring convenient banknotes and payment methods.

Cambodia: Dollarization

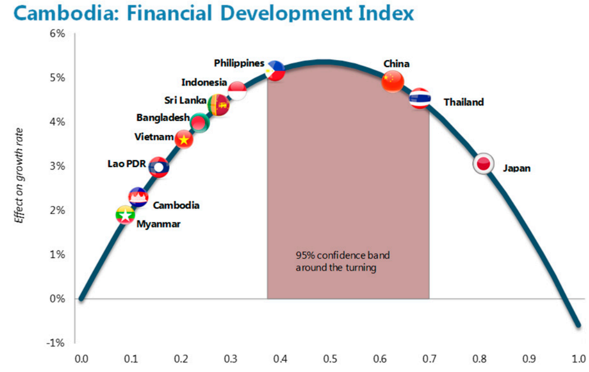
(In percent; the share of foreign currency deposits in total deposits; data as of 2015)



Sources: IMF staff estimates and calculations.

21. Advancing financial sector development. Promoting development of the interbank, equity (including for small and medium-sized enterprises), government and corporate bond, and foreign exchange markets could further promote local currency usage and allow for the eventual implementation of an effective monetary policy framework. Specifically, authorities should improve functioning of the market for NCDs and develop an online trading platform to make the interbank market more liquid and move towards auction pricing and, continue restructuring the foreign exchange market and encourage banks (instead of money changers) to play a greater role.

Cambodia: Financial Development Index



Sources: Financial Development Index; Rethinking Financial Deepening: Stability and Growth in Emerging Markets; and IMF Staff calculations.

22. Policies to further financial inclusion. Financial deepening has improved inclusion, including through access to MFI credit and emerging use of mobile services. However, there are still large gaps in access and use of formal financial services. Few households have an account and firms identify access to finance as one of their major constraints (Box 4). The authorities have made efforts to incorporate financial literacy into education programs, introduced a literacy campaign and plan to reduce operational costs of smaller financial institutions by improving interoperability between ATMs and point of sale systems. Further inclusion can be achieved by promoting the use of financial technology, reducing costs (including through development of the interbank market to mobilize excess Riel reserves and developing financial infrastructure), diversifying products, as well as improving financial literacy. Finally, an adequate legal and regulatory framework is needed to protect consumers, and to effectively address all relevant risks (including those emerging from new actors and products), while at the same time fostering innovation and competition.

23. External sector assessment. The current account deficit is projected to remain broadly stable over the medium-term. Based on the IMF's External Balance Assessment (EBA)-lite methodology, the external position is assessed to be moderately weaker than the level implied by fundamentals and desirable policies (Appendix III). The moderate REER overvaluation calls for policies to consolidate the fiscal position, diversify export markets and improve productivity and competitiveness, including ensuring that future wage increases are linked to productivity improvements. While reserves appear adequate when measured against traditional metrics, there are benefits to further reserve accumulation given high dollarization and elevated financial vulnerabilities. The current closely managed exchange rate regime is appropriate given high dollarization and a concentration in U.S. dollar-invoiced exports (primarily garments). As capacity improves and the economy diversifies, gradually introducing greater flexibility is recommended to better absorb external shocks, enable monetary policy implementation and to support further Riel use.

24. Authorities' views. The authorities remain committed to IDP implementation and emphasized their efforts to improve the business environment, including through more power generation capacity, improving reliability and reducing the cost of electricity, as well as education reforms (especially vocational training). They pointed to progress in promoting financial inclusion, including improvements in payments infrastructure, and were formulating a financial inclusion strategy. The recent Financial Sector Development Strategy outlined comprehensive measures to support further financial market development. The authorities agreed with staff on measures to promote use of Riel, stressing the importance of collaboration and building confidence in local currency. The authorities noted their efforts to diversify their Cambodia's export products and destinations to compensate for the eventual loss of trade preferences owing to their graduation to lower-middle income status. Foreign reserves increased strongly in the first half of 2017, and the authorities projected moderate further accumulation going forward.

STAFF APPRAISAL

25. Economic outlook and risks. Growth is projected to remain robust, supported by higher public spending and strong construction and tourism activity. Inflation is expected to remain elevated in the short-term. Private sector credit growth, increasingly concentrated in real estate related sectors, has slowed and is projected to moderate further looking forward. Growth is projected to decline over the medium-term owing to a moderation in the credit and real estate cycles and ongoing challenges in improving economic diversification and competitiveness. The external position is assessed to be moderately weaker than suggested by fundamentals and desirable policies. This positive outlook is subject to significant downside risks. These include, in particular, risks stemming from elevated financial sector vulnerabilities and the impact of wage increases on competitiveness, as well as risks related to the external outlook, including from weaker growth in China.

26. Macro-financial policies. Continuing to build resilience through targeted prudential policies will be key to containing macro-financial risks. Priorities include strengthening regulations on loan classification to better manage credit risk; introduction of further well-designed and targeted macro-prudential policies, including gradually increasing reserve requirements on foreign exchange liabilities to build liquidity buffers; and expediting collection of data on the real-estate sector. Improving sectoral asset classification would enable the introduction of sectoral concentration limits and/or higher risk weights for real-estate loans. With the growing systemic relevance of large MFIs, strengthening regulation to prevent regulatory arbitrage is warranted. The authorities should introduce a comprehensive crisis management framework. Strong supervision, supported by sufficient resources to respond to increasing demands, is essential to ensure proper risk identification and enforcement of prudential policies. In this respect, the implementation of outstanding FSAP recommendations should be expedited.

27. Financial market development. High dollarization increases banks' vulnerability and limits the scope for exchange rate and monetary policies. Further measures are needed to encourage Riel use, including reallocating the remuneration currently paid on U.S. dollar reserves to Riel denominated reserves; gradually increasing the reserve requirement on foreign exchange liabilities; monitoring unhedged exchange rate risk exposures; systematically factoring in dollarization risk in prudential regulation and enforcing the requirement for businesses to post prices in Riel. Moreover, a multi-pronged strategy and close inter-agency collaboration is needed. Reforms to develop the equity, interbank, government and corporate bond, and foreign exchange markets in line with the Financial Sector Development Strategy are needed to promote local currency use and build an effective monetary policy framework.

28. Financial inclusion. Financial access, especially in rural areas, has increased thanks to rapid growth of MFIs and mobile banking services, and welcome steps taken by the authorities to promote inclusion. Further efforts should focus on reducing costs, diversifying products and services, and improving financial literacy and consumer protection, as well as promoting the use of financial technology. A comprehensive financial inclusion strategy would help address risks while at the same time fostering innovation and competition.

29. Fiscal policy. Fiscal deficits should be contained to safeguard fiscal and external sustainability. To ensure that the recent revenue gains are sustained over the medium term, further improvements in revenue administration and modernizing tax policy are needed. On the expenditure side, further public wage increases should be fiscally sustainable and be accompanied by continued progress in public administration reforms. This includes strong efforts to strengthen human resource management, including to increase skills and labor productivity, improve spending efficiency, and enhance transparency. The planned framework for social protection is welcome but education and health spending should be prioritized. Developing a medium-term budget framework to systematically allocate expenditures and improve spending efficiency remains a priority. While PPPs can increase efficiency relative to public financing for investment, they do not necessarily increase fiscal space, and strengthening the PPP framework is needed to manage fiscal costs and risks.

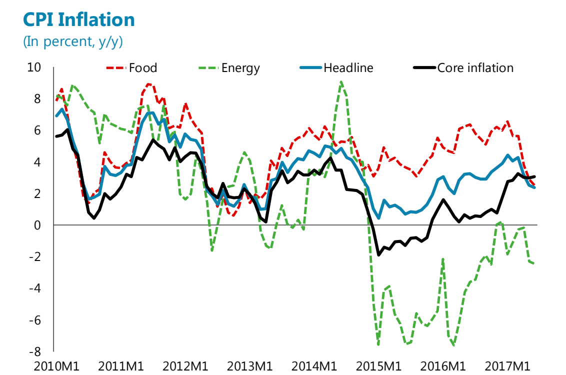
30. Structural reforms. Accelerated implementation of structural reforms is needed to increase resilience and secure strong, sustained and inclusive growth. These should include promoting diversification, enhancing competitiveness, and improving the business climate and inclusiveness. A focus should be on accelerating IDP implementation to boost investor confidence, implementing key infrastructure projects, strengthening governance, the rule of law and transparency of business regulation, and further investing in education. Including climate change impact in the design of macroeconomic and structural policies, especially in the agriculture sector, would improve resilience.

31. It is recommended that the next Article IV consultation takes place on the standard 12-month cycle.

Box 1. Cambodia: Inflation Drivers[1]

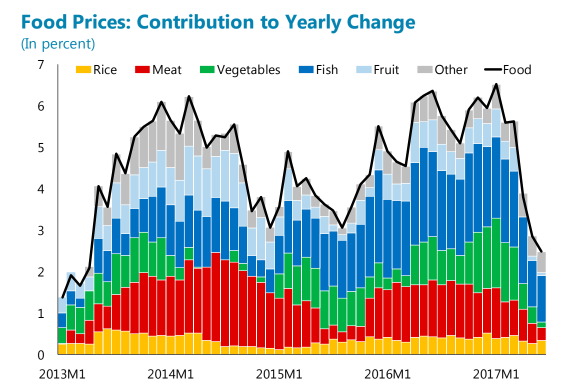
Recent pick-up in inflation has been driven by higher food and fuel prices, in part owing to imported inflation, and some upward pressure from rising wages. Policies should aim to contain production and transportation costs and link wage increases to improvements in productivity.

Food and energy prices are the main drivers. Food accounts for close to 45 percent of the CPI basket while energy, combined with electricity, directly accounts for about 10 percent. Food prices are affected by weather-related supply shocks and, recently, upward pressure from rising wages and imported inflation. However, food prices also often move in tandem with energy prices, suggesting indirect effects from energy prices and related products/services (especially transportation) on food production costs. Core inflation has closely followed movements in food and energy prices, suggesting pass-through to prices of other goods and services in the economy. Finally, wage increases in both private and public sectors have contributed to higher domestic demand and production costs.



Sources: Cambodian authorities; and IMF staff estimates and calculations.

Imported inflation has become more important. Food prices traditionally move in line with rice prices, reflecting its importance in the economy (despite its small share in CPI, at about 6 percent). However, imports of some food components, especially meat and vegetables (which account for large shares, about 10 and 5 percent of CPI, respectively) have recently increased.[2] As a result, those prices move more closely with prices in main import partners, with a significant impact on food CPI.



Sources: Cambodian authorities; and Fund staff calculation.

Policies should aim to contain increases in production and transportation costs, and wages. The focus should be on structural policies to support a stable food supply and reduction in production and transportation costs. Investments in energy and transport infrastructure, as well as to increase agricultural productivity (e.g. through irrigation) should be prioritized. Wage increases should be linked to improvements in productivity to maintain competitiveness and stable inflation. At the same time, policy-makers should remain vigilant for any signs of overheating and undue inflation pressures from possible second-round effects on inflation expectations.

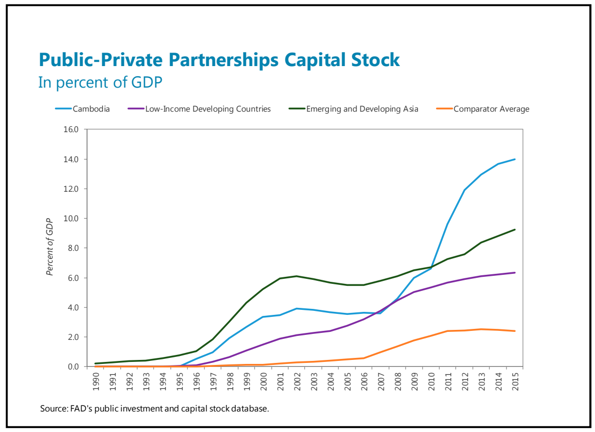
1/ Prepared by Tadaaki Ikoma.

2/ About half of the vegetables consumed in the country are estimated to be imported.

Box 2. Cambodia: Managing Fiscal Costs and Risks from PPPs[1]

Infrastructure bottlenecks remain a critical constraint for economic diversification and sustainable growth. However, the use of PPPs to finance public infrastructure calls for strengthening the institutional, legal and budgetary frameworks to better manage fiscal costs and risks.

Although PPPs offer many benefits, they do not necessarily increase fiscal space. Investment financed by PPPs has grown considerably, especially in the electricity sector, and Cambodia now stands as a leader relative to its peers. The government has plans to further expand public investment through PPPs, including projects in electricity, roads, ports, railways, water, education and health.[2] PPPs can increase efficiency and help transfer risks, thus providing value for money relative to public financing. However, off-balance sheet obligations arising from PPPs are difficult to control and make the fiscal position more vulnerable to shocks. Obligations to make payments to PPPs over the long term also reduce the governments' future financial flexibility, much as traditional debt does.



Improvements in the PPP framework are needed. The government has already initiated important changes in the framework for PPPs.[3] Priority reforms include:

- **Accounting for and controlling fiscal costs.** The government's accounting system, designed to control publicly-financed investment, does not help monitor PPP-related obligations. The MEF has introduced a 4-percent of GDP limit on guaranteed payments for PPPs in the electricity sector. Although this is a positive development, the current limit is too high to fully protect against excessive exposure. As an alternative, the government could limit the present value of guaranteed payments and total annual investments in PPPs.

- **Strengthening the institutional framework for managing PPPs.** The role of the MEF under the current institutional framework is limited to endorsing the final decision. The MEF should be responsible for safeguarding public finances through a gateway process, which would empower it to veto a project if it does not offer value for money or is not fiscally affordable.

- **Strengthening the PPP legal framework**. Changes in the institutional framework should be accompanied by changes in PPP governance, including the legal and regulatory framework. The MEF should be given the authority to apply the gateway process and to establish mechanisms for competitive bidding. Budgeting, accounting and reporting requirements should be strengthened to ensure a more consistent monitoring of liabilities and provision of on fiscal risks.

Strengthening public investment management (PIM). PPP projects should be reclassified as public investments and be subject to the same planning and allocation processes. Before fully integrating PPPs in the PIM process, all PPP proposals should be reviewed by the new inter-ministerial committee in charge of PPPs until the formal gateway process is put in place. Finally, the government should include information about financial obligation arising from PPPs in its budget documents.

1/ Prepared by Maximilien Queyranne, Genevieve Verdier and Yong Sarah Zhou.

2/ Planned investments amount to more than $6billion over time.

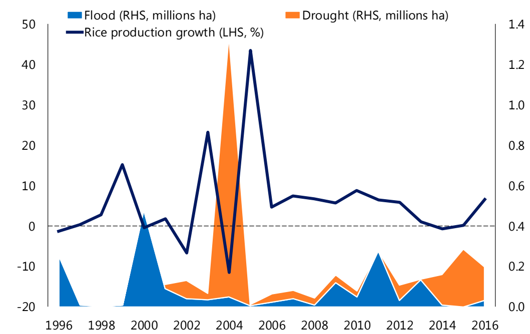
3/ See government's policy paper "PPPs for Public Investment Project Management".

Box 3. Cambodia: Macroeconomic Implications of Climate Change[1]

Climate change risks having a negative impact on climate-sensitive sectors, especially agriculture, lowering growth and worsening the fiscal position. The impact would be aggravated by low adaptive capacity.

Recent extreme weather events suggest that climate change may already be having an impact. Climate change leads to higher temperature, more frequent and intensified extreme weather events – like severe droughts in 2004 and 2015/16 and floods in 2000, 2011, and 2013 in Cambodia – and sea level rise. Its direct impact on the economy includes reduced agricultural production, tourists shifting their destination to less affected regions, and lower labor productivity due to increased climate-related diseases and heat stress. Extreme weather events have already had a significant negative impact on agricultural production in Cambodia.

Rice: Production and Fields Damaged by Natural Disasters



Sources: Cambodian authorities; FAOSTAT; and Fund staff calculations.

Cambodia is among the most vulnerable countries. Cambodia, along with other countries in Southeast Asia, is expected to be severely affected by climate change. Cambodia is particularly vulnerable, given the importance of climate-sensitive sectors, especially agriculture and tourism (agriculture alone accounts for about 30 percent of total GDP and half of total employment). Weak adaptation capacity, including low income, gaps in key infrastructure (e.g., lack of irrigation), and low literacy rate add to vulnerabilities. Cambodia Climate Change Financing Framework (2015) estimates that Cambodia's cumulative output loss would be equivalent to about 25–50 percent of its potential GDP by 2050.

Negative growth impact and adaptation costs would have negative spillovers. Climate related expenditure is currently estimated at just below 2 percent of GDP, mostly focused on adaptation and funded by donors.[2] Future fiscal costs for adaptation would be large and thus put further pressures on fiscal position.[3] Agricultural losses would also result in worsening of the trade balance, increased non-performing agricultural loans, aggravation of poverty given both reliance on agriculture and low adaptive capacity among rural, low-income households.

Impacts warrant integration of climate change issues into the macroeconomic policy framework. Preserving debt sustainability requires accounting for fiscal risks from climate change, improving spending efficiency, and mobilizing further revenues (including through introduction of carbon taxes). Structural reforms to improve productivity especially in agriculture and to diversify the economy and livelihoods, i.e. reducing dependency on climate-sensitive sectors, would increase resilience.

1/ Prepared by Tadaaki Ikoma.

2/ Climate Public Expenditure and Institutional Review (2012).

3/ The optimal level of adaptation costs could amount to around 3.3 percent of GDP annually over the long term (Cambodian Climate Change Financing Framework).

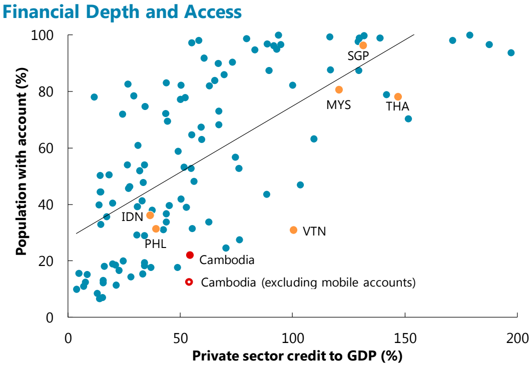
Box 4. Cambodia: Advancing Financial Inclusion[1]

Financial deepening has improved inclusion, including through access to microfinance credit and emerging use of mobile services. However, gaps remain and further efforts are needed to reduce transaction costs, expand products, and promote financial literacy and consumer protection.

Financial inclusion remains low despite rapid financial deepening. The growth of MFIs has increased access to credit, especially in rural areas, with MFIs serving more than twice the clients served by commercial banks. The rapid penetration of mobile financial services provides access to low-cost services, including in areas that are otherwise underserved by financial institutions. Nevertheless, financial inclusion, as reflected in the share of the population with accounts and SME access to financing, remains relatively low.

Limited access reflects high costs, limited products and services, and low financial literacy. Providing financial services in remote rural areas, poor information on customers and weak contract enforcement result in high intermediation costs, especially for small transactions. High funding costs, especially for Riel, also constrain financial access.[2] Mobile financial services provide low-cost services, but the service is mostly limited to payments and use remains low among the low-income and less-educated population.[3]

Financial Depth and Access



Sources: Global Financial Development Database (data as of 2014).

There is scope for further gains. Promoting the use of financial technology (e.g. through improving internet access in rural areas), promoting low-cost funding markets and developing financial infrastructure (e.g. improving information provided by the credit registry) will lower costs. Improving financial literacy is also key – the government's plan to incorporate financial education into national curriculum will help close the knowledge gap.

Improvements are needed to effectively address risks and protect consumers. Developing a consumer protection framework is crucial to address concerns, such as over-indebtedness related to high cost borrowing. An adequate legal framework protects the rights of consumers, mitigates credit risks from limited information, and ensures equity and transparency among participants. Also, policies to broaden financial access (i.e. on mobile financial services) require a concomitant widening of the regulatory and supervisory perimeter to minimize regulatory arbitrage and financial stability risks, while at the same time fostering innovation and competition.

1/ Prepared by Tadaaki Ikoma and Yong Sarah Zhou

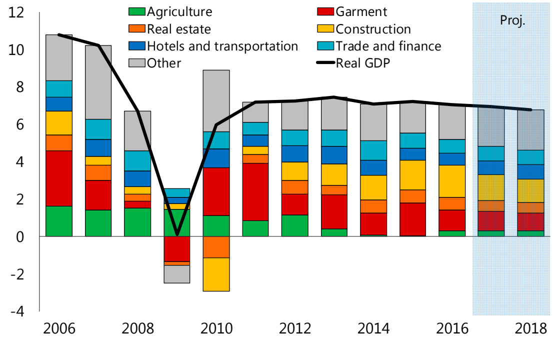
2/ For example, the weighted-average deposit rate in Riel is about 2 percent higher than in USD, resulting also in a higher Riel lending rate (by about 4 percent).

3/ FinScope Survey (2016) shows limited knowledge among top reasons for not using mobile services. Based on UNCDF-FinMark Trust 2015 survey, which covers broader financial services, the formal financial inclusion rate in Cambodia is 59 percent, of which 42 percent is through MFIs.

Figure 1. Cambodia: Robust Growth and Increasing Inflation

Economic growth remains robust.

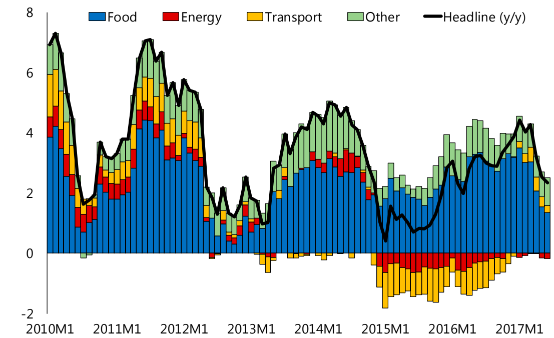
Contribution to Real GDP Growth
(In percent)



Sources: Cambodian authorities; and IMF staff estimates and calculations.

Inflation has picked up driven by higher food and fuel prices.

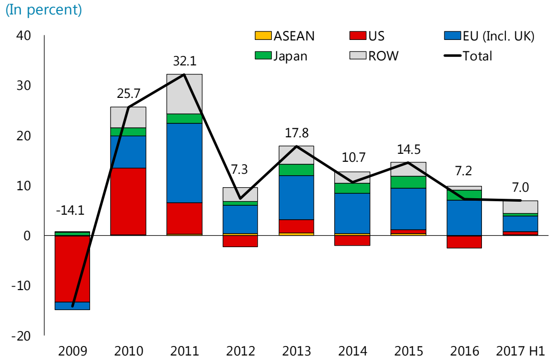
CPI Inflation: Contribution to Change
(In percent)



Sources: Cambodian authorities; and IMF staff calculations.

Exports to Europe are weak while exports to US are recovering.

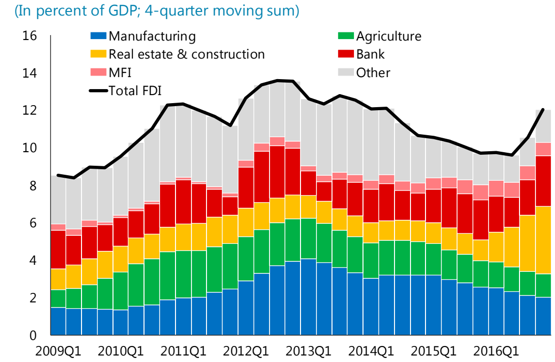
Garment Exports (Value): Contribution to Growth
(In percent)



Sources: GDCE; and IMF staff calculations.

Real estate activity was supported by strong foreign investment inflow as well as by domestic credit.

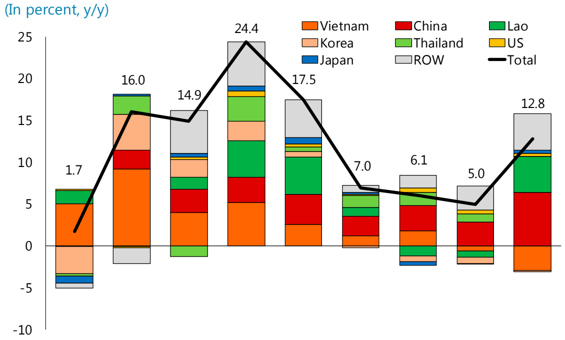
FDI Inflow by Sector
(In percent of GDP; 4-quarter moving sum)



Sources: Cambodian authorities; and IMF staff calculations.

Tourist arrivals from China continue to support tourism growth.

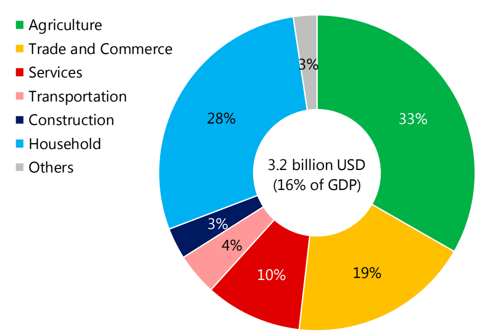
Tourism: Contribution to Arrivals Growth
(In percent, y/y)



Sources: Cambodian authorities; and IMF staff calculations.

Microfinance credit supports agriculture and household consumptions.

MFI Credit Stock by Sector
(In percent; as of end-2016)



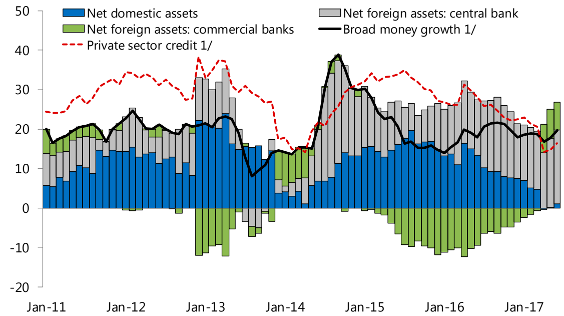
Sources: Cambodian authorities.

Figure 2. Cambodia: Elevated Vulnerabilities Despite Moderating Credit Growth

Broad money increased by 18 percent (y/y) by end 2016, while NFA in the banking sector remains negative…

Monetary Developments

(In percent)

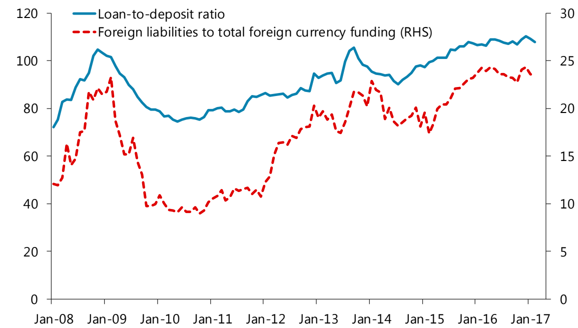


Sources: Cambodian authorities; and IMF staff calculations.
1/ Year-on-year percent change.

….reflecting a reliance on external borrowing.

Foreign Liabilities to Total Foreign Funding

(In percent)

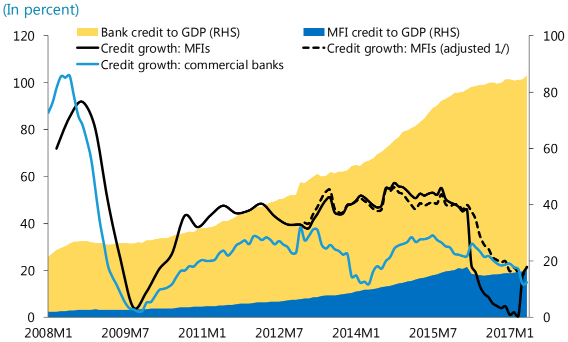


Sources: Cambodian authorities; and IMF staff calculations.

Credit growth is moderating while credit-to-GDP ratio continues to rise.

Private Sector Credit: MFIs and Commercial Banks

(In percent)

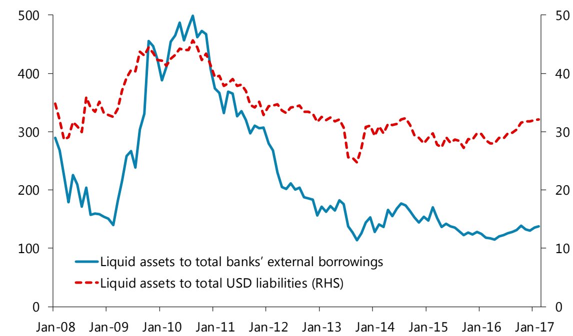


Sources: NBC; and IMF staff calculations.
1/ Excludes credit of the second-largest MFI, which was reclassified into a commercial bank in 2016.

Liquid assets to external borrowing has risen marginally.

Liquid Assets to Banks' External Liabilities

(In percent)

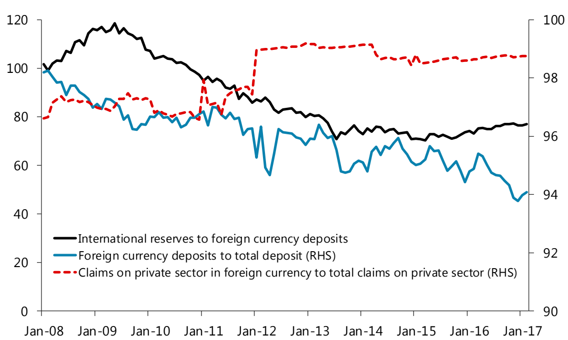


Sources: Cambodian authorities; and IMF staff calculations.

Cambodia's dollarization level remains high.

Dollarization

(In percent)

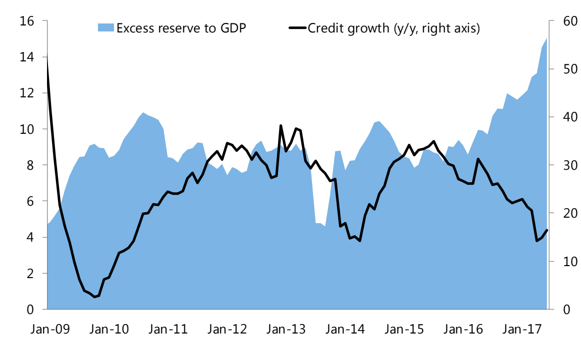


Sources: Cambodian authorities; and IMF staff calculations.

Excess reserves-to-GDP remains high reflecting underdeveloped interbank market and precaution.

Credit to the Economy and Excess Reserves

(In percent)



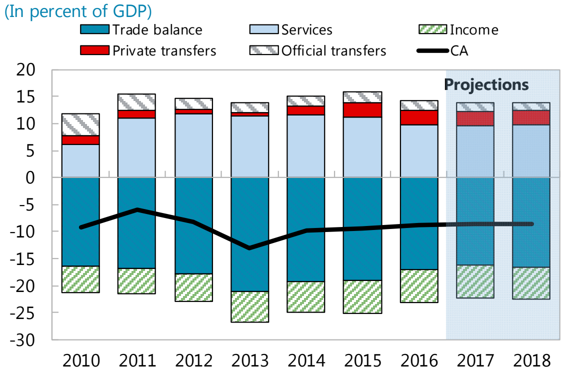
Sources: Cambodian authorities; and IMF staff calculations.

Figure 3. Cambodia: Stable External Position

The current account deficit narrowed in 2016 thanks to lower imports….

Current Account

(In percent of GDP)

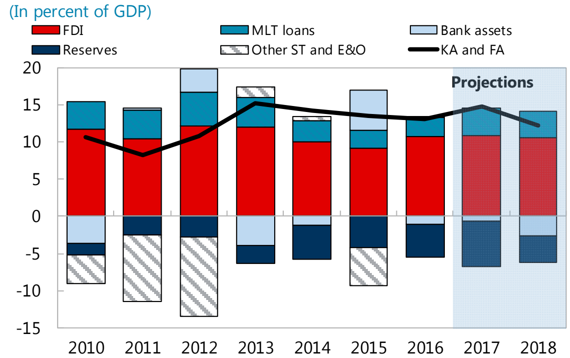


Sources: Cambodian authorities; and IMF staff calculations.

… and was financed primarily with FDI inflows.

Current Account Financing

(In percent of GDP)

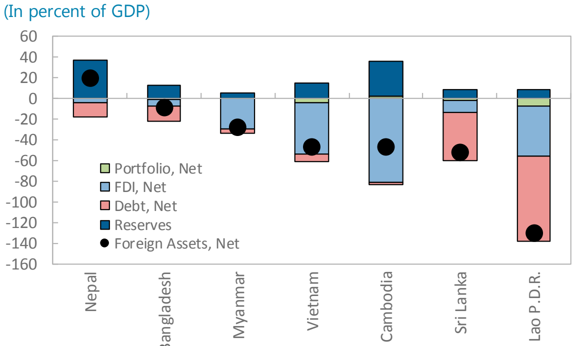


Sources: Cambodian authorities; and IMF staff calculations.

The NFA is in line with peers and composed primarily of FDI liabilities.

Selected Economies: Net Foreign Assets

(In percent of GDP)

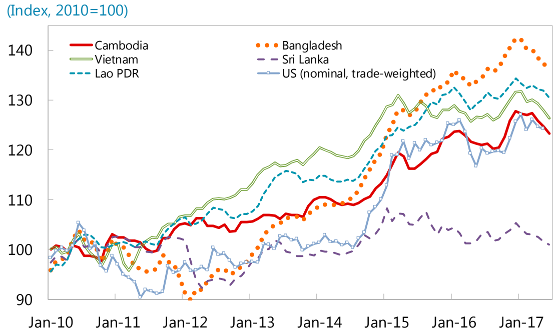


Sources: Cambodian authorities; External Wealth of Nations; IMF staff calculations.
Note: Latest data available for Cambodia is 2016. For rest of countries, latest data is 2015.

The real effective exchange rate continued to appreciate in line with the U.S. dollar, but less than in peer countries.

Real Effective Exchange Rate

(Index, 2010=100)

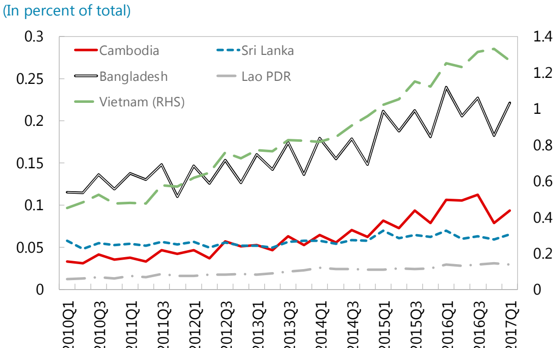


Sources: Cambodian authorities; Bloomberg L.P.; and IMF staff calculations.

Cambodia's export market share continued to improve.

Selected Economies: Share of World Imports

(In percent of total)

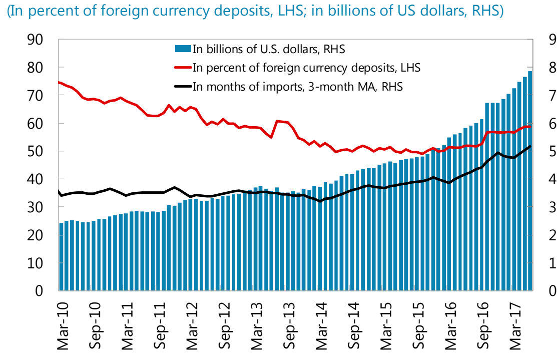


Sources: IMF, *Directions Of Trade Statistics* (DOTS), and IMF staff calculations.

There was further reserves accumulation, and reserve coverage in terms of FX deposits stabilized.

Gross Official Reserves

(In percent of foreign currency deposits, LHS; in billions of US dollars, RHS)

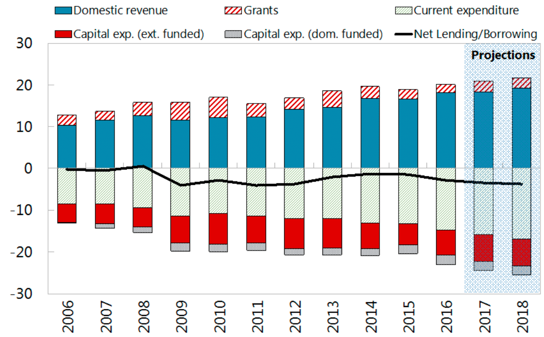


Sources: Cambodian authorities; and IMF staff calculations.

Figure 4. Cambodia: Robust Revenue Performance Amid Spending Pressures

Fiscal performance is still strong owing to robust revenue performance but the spending mix is deteriorating.

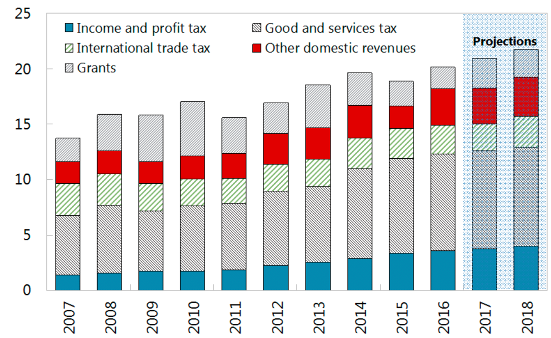
Fiscal Balance
(In percent of GDP)



Sources: Cambodian authorities; and IMF staff calculations.

Revenue performance continues to be enhanced by strong one-off collection efforts.

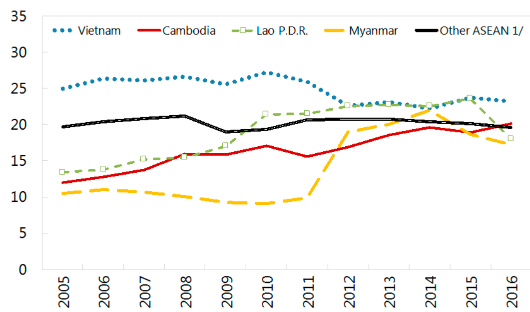
Fiscal Revenues
(In percent of GDP)



Sources: Cambodian authorities; and IMF staff calculations.

Revenue efforts has seen Cambodia reach the regional average…

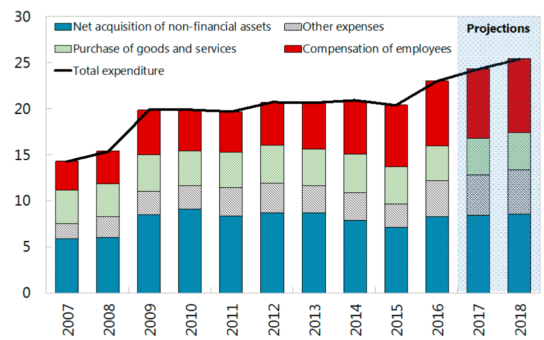
Total Revenue and Grants in Asian LICs
(In percent of GDP)



Sources: Cambodian authorities; and IMF staff calculations.
1/ Average of Indonesia, Malaysia, Singapore, Philippines, and Thailand.

…however, public wage has also been rising, squeezing other expenditures…

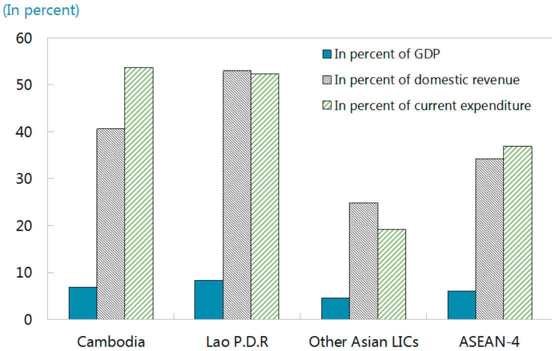
Goverment Spending
(In percent of GDP)



Sources: Cambodian authorities; and IMF staff calculations.

…resulting in public wages that are higher than in most other Asian LICs.

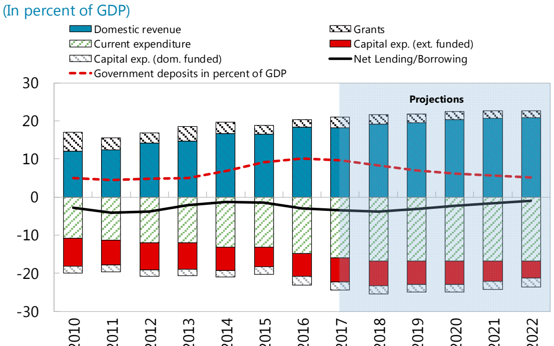
Wage Spending, 2016
(In percent)



Sources: Cambodian authorities; and IMF staff calculations.

Efforts are needed to maintain the level of government deposits, and make space for development spending.

Medium-term Fiscal Outlook
(In percent of GDP)

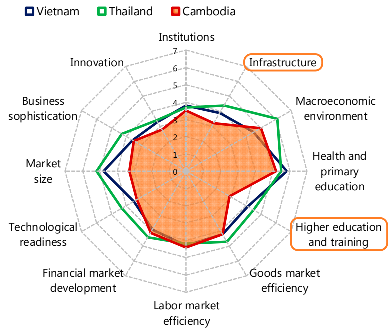


Sources: Cambodian authorities; and IMF staff calculations.

Figure 5. Cambodia: Structural Challenges to Growth

Cambodia lags its peers on some business environment, including infrastructure and human capital.

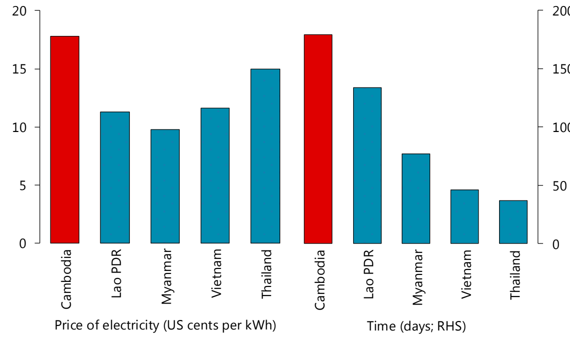
Global Competitiveness Index
(Index; 1=lowest, 7=highest)



Source: World Economic Forum, *Global Competitiveness Index 2016*.

Access to electricity is limited and relatively costly.

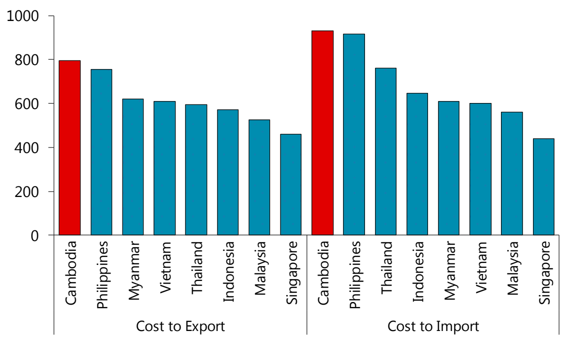
Cost of Getting Electricity



Source: World Bank, *Doing Business 2017*.

Costs of both exports and imports are higher compared to peers.

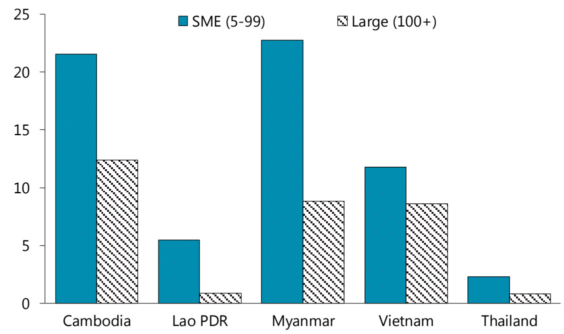
Selected Economies: Cost to Export & Import
(In US dollars per container)



Source: World Bank, *Doing Business 2017*.

Access to finance by SMEs is limited.

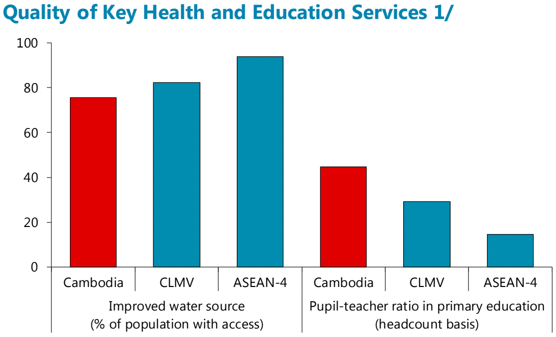
Firms Identifying Access to Finance as a Major Constraint
(In percent)



Source: World Bank *Enterprise Survey* (Cambodia as of 2016; others latest available).

Quality of key health and education services is limited, affecting human capital.

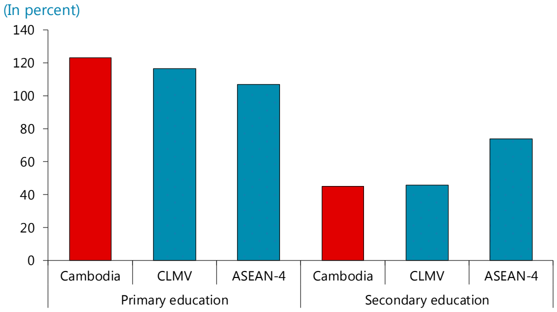
Quality of Key Health and Education Services 1/



Sources: UNESCO Institute for Statistics; and IMF staff calculations (2010 for hospital beds, 2015 for improved water source, and 2014 for pupil-teacher ratio in primary education).
1/ CLMV includes Cambodia, Lao P.D.R., Myanmar, and Vietnam. ASEAN-4 includes Malaysia, Indonesia, Thailand, and the Philippines.

Cambodia lags in secondary education achievement, despite significant progress in primary education.

Enrollment of Primary & Secondary Education 1/
(In percent)



Sources: UNESCO Institute for Statistics; and IMF staff calculations (2013 for primary education and 2008 for secondary education).
1/ Total enrollment in primary or secondary education, regardless of age, expressed as a percentage of the population of official relevant education age. Values can exceed 100% due to the inclusion of over-aged and under-aged students because of early or late school entrance and grade repetition.

Table 1. Cambodia: Selected Economic Indicators, 2012–18

	2012	2013	2014	2015	2016	2017	2018
					Est.	Proj.	Proj.
Output and prices (annual percent change)							
GDP in constant prices	7.3	7.4	7.1	7.2	7.0	6.9	6.8
(Excluding agriculture)	8.3	9.5	9.2	9.2	8.5	8.3	8.0
Inflation (end-year)	2.5	4.7	1.0	2.8	3.9	3.1	3.4
(Annual average)	2.9	3.0	3.9	1.2	3.0	3.7	3.5
Saving and investment balance (in percent of GDP)							
Gross national saving	15.3	10.5	13.4	13.1	14.1	13.6	13.4
Government saving	1.9	2.2	3.4	3.8	2.8	1.5	0.4
Private saving	13.4	8.4	10.0	9.3	11.3	12.2	13.0
Gross fixed investment	23.5	23.5	23.2	22.4	22.9	22.2	22.0
Government investment	9.0	8.9	8.0	6.9	7.8	8.2	8.6
Private investment	14.5	14.6	15.2	15.5	15.1	14.0	13.4
Money and credit (annual percent change, unless otherwise indicated)							
Broad money	20.9	14.6	29.9	14.7	18.0	14.4	12.9
Private sector credit	38.3	17.3	31.3	27.1	22.5	12.5	10.0
Velocity of money 1/	2.2	2.0	1.8	1.6	1.6	1.4	1.3
Public finance (in percent of GDP)							
Revenue	16.9	18.5	19.8	18.8	19.8	19.5	19.6
Domestic revenue	14.2	14.6	16.9	16.5	17.9	18.0	18.1
Of which : Tax revenue	11.3	11.8	13.8	14.5	15.3	15.3	15.3
Grants	2.8	3.9	3.0	2.3	2.0	1.5	1.5
Expenditure	20.7	20.7	21.0	20.4	22.7	23.2	24.1
Expense	12.0	12.0	13.1	13.2	14.9	15.0	15.6
Net acquisition of nonfinancial assets	8.7	8.7	7.9	7.1	7.8	8.2	8.5
Net lending (+)/borrowing(-)	-3.8	-2.1	-1.1	-1.6	-2.8	-3.7	-4.6
Net lending (+)/borrowing(-) excluding grants 2/	-6.3	-6.4	-4.2	-3.2	-4.7	-5.2	-6.0
Net acquisition of financial assets	0.6	0.5	2.3	2.8	2.1	0.6	-0.5
Net incurrence of liabilities 3/	4.4	2.6	3.5	4.4	4.9	4.2	4.1
Of which: Domestic financing	0.7	-0.5	-1.5	-0.7	0.2	0.0	1.0
Government deposits	4.9	5.0	6.9	9.1	10.1	9.7	8.3
Balance of payments (in millions of dollars, unless otherwise indicated)							
Exports, f.o.b.	5,633	6,530	7,407	8,453	9,233	10,112	11,041
(Annual percent change)	11.9	15.9	13.4	14.1	9.2	9.5	9.2
Imports, f.o.b.	-8,139	-9,749	-10,613	-11,920	-12,649	-13,717	-15,053
(Annual percent change)	13.4	19.8	8.9	12.3	6.1	8.4	9.7
Current account (including official transfers)	-1,150	-1,979	-1,641	-1,694	-1,776	-1,904	-2,098
(In percent of GDP)	-8.2	-13.0	-9.8	-9.3	-8.8	-8.6	-8.6
Gross official reserves 4/	3,463	3,642	4,391	5,093	6,731	8,097	8,955
(In months of prospective imports)	3.6	3.5	3.8	4.2	5.0	5.5	5.6
External debt (in millions of dollars, unless otherwise indicated)							
Public external debt	4,852	5,269	5,610	6,457	7,267	8,216	9,100
(In percent of GDP)	31.6	31.6	31.8	30.8	31.9	32.8	34.0
Public debt service	112	143	172	239	244	192	313
(In percent of exports of goods and services)	1.3	1.4	1.5	1.9	1.8	1.3	1.9
Memorandum items:							
Nominal GDP (in billions of riels)	56,650	61,414	67,485	73,694	81,703	90,325	99,753
(In millions of U.S. dollars)	14,049	15,249	16,714	18,150	20,157	22,252	24,307
Exchange rate (riels per dollar; period average)	4,032	4,027	4,038	4,060	4,053	…	…

Sources: Cambodian authorities; and IMF staff estimates and projections.

1/ Ratio of nominal GDP to the average stock of broad money.

2/ According to GFS 86 used by Cambodian authorities.

3/ Includes statistical discrepancy.

4/ Excludes unrestricted foreign currency deposits held as reserves at the National Bank of Cambodia; starting in 2009, includes the new SDR allocations made by the IMF of SDR 68.4 million.

Table 2. Cambodia: Medium-Term Macroeconomic Framework, 2012–22

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
					Est.			Proj.			
Output and prices (percent change)											
GDP at constant prices	7.3	7.4	7.1	7.2	7.0	6.9	6.8	6.8	6.5	6.3	6.0
GDP deflator	1.4	0.9	2.6	1.9	3.6	3.4	3.4	3.5	3.4	3.5	3.4
Consumer prices (end-year)	2.5	4.7	1.0	2.8	3.9	3.1	3.4	3.2	3.1	3.0	3.0
Consumer prices (average)	2.9	3.0	3.9	1.2	3.0	3.7	3.5	3.3	3.2	3.1	3.0
Saving and investment balance (in percent of GDP)											
Gross national saving	15.3	10.5	13.4	13.1	14.1	13.6	13.4	13.5	13.4	13.4	13.6
Government saving	1.9	2.2	3.4	3.8	2.8	1.5	0.4	0.8	1.7	2.4	2.6
Private saving	13.4	8.4	10.0	9.3	11.3	12.2	13.0	12.8	11.7	11.0	11.0
Gross fixed investment	23.5	23.5	23.2	22.4	22.9	22.2	22.0	22.0	21.8	21.7	21.6
Government investment	9.0	8.9	8.0	6.9	7.8	8.2	8.6	8.5	8.5	8.5	8.6
Private investment 1/	14.5	14.6	15.2	15.5	15.1	14.0	13.4	13.5	13.3	13.2	13.0
Private credit growth (percent change)	38.3	17.3	31.3	27.1	22.5	12.5	10.0	11.0	11.0	11.0	11.0
Public finance (in percent of GDP)											
Revenue	16.9	18.5	19.8	18.8	19.8	19.5	19.6	19.7	20.1	20.2	20.4
Of which: Tax revenue	11.3	11.8	13.8	14.5	15.3	15.3	15.3	15.3	15.5	15.7	15.8
Grants	2.8	3.9	3.0	2.3	2.0	1.5	1.5	1.4	1.3	1.1	1.1
Total expenditure	20.7	20.7	21.0	20.4	22.7	23.2	24.1	24.1	24.1	24.2	24.2
Expense	12.0	12.0	13.1	13.2	14.9	15.0	15.6	15.7	15.7	15.7	15.7
Net acquisition of nonfinancial assets	8.7	8.7	7.9	7.1	7.8	8.2	8.5	8.5	8.5	8.5	8.5
Of which: Domestically-financed	1.6	1.7	1.7	2.3	2.5	2.4	2.9	3.0	3.2	3.3	3.4
Net lending (+)/borrowing(-)	-3.8	-2.1	-1.1	-1.6	-2.8	-3.7	-4.6	-4.4	-4.0	-4.0	-3.8
Net lending (+)/borrowing(-) excluding grants	-6.3	-6.4	-4.2	-3.2	-4.8	-5.2	-6.0	-5.8	-5.3	-5.1	-4.9
Net acquisition of financial assets	0.6	0.5	2.3	2.8	2.1	0.6	-0.5	-0.5	-0.2	-0.1	0.0
Net incurrence of liabilities	4.4	2.6	3.5	4.4	4.9	4.2	4.1	3.9	3.8	3.9	3.8
Domestic financing, net	0.7	-0.5	-1.5	-0.7	0.2	0.0	1.0	1.1	0.9	0.8	0.7
Government deposits	4.9	5.0	6.9	9.1	10.1	9.7	8.3	7.1	6.2	5.6	5.1
Balance of payments (in percent of GDP, unless otherwise indicated)											
Exports (percent change) 2/	11.9	15.9	13.4	14.1	9.2	9.5	9.2	9.7	10.2	9.8	8.5
Imports (percent change) 3/	13.4	19.8	8.9	12.3	6.1	8.4	9.7	9.5	9.8	9.4	8.2
Current account balance (including transfers)	-8.2	-13.0	-9.8	-9.3	-8.8	-8.6	-8.6	-8.5	-8.4	-8.3	-8.0
(Excluding transfers)	-10.2	-14.9	-11.8	-11.3	-10.7	-10.1	-10.1	-9.9	-9.7	-9.5	-9.1
Foreign direct investment	12.1	12.0	10.0	9.1	10.7	10.9	10.6	10.3	10.0	9.7	9.4
Other flows 4/	-1.1	3.4	4.3	4.5	2.4	3.8	1.6	1.4	1.6	1.7	1.6
Overall balance	2.8	2.4	4.5	4.3	4.3	6.1	3.5	3.2	3.2	3.0	3.0
Gross official reserves (in millions of U.S. dollars) 5/	3,463	3,642	4,391	5,093	6,731	8,097	8,955	9,811	10,739	11,699	12,714
(In months of next year's imports)	3.6	3.5	3.8	4.2	5.0	5.5	5.6	5.6	5.6	5.6	5.7
Public external debt (in millions of U.S. dollars)	4,852	5,269	5,610	6,457	7,267	8,216	9,100	10,006	11,006	12,068	13,187
(In percent of GDP)	31.6	31.6	31.8	30.8	31.9	32.8	34.0	34.4	34.8	35.1	35.5
Public external debt service (in millions of U.S. dollars)	112	143	172	192	244	192	313	362	382	411	412
(In percent of exports of goods and services)	1.3	1.4	1.5	1.9	1.8	1.3	1.9	2.1	2.0	2.0	1.8

Sources: Cambodian authorities; and IMF staff estimates and projections.

1/ Includes nonbudgetary, grant-financed investment, and, from 2011, public-private partnerships in the power sector projects.

2/ Excludes re-exported goods.

3/ Excludes imported goods for re-export; from 2011, includes imports related to public-private power sector projects.

4/ Net official disbursements, exceptional financing, and official transfers.

5/ Excludes unrestricted foreign currency deposits held as reserves at the National Bank of Cambodia; starting in 2009, includes the new SDR allocations made by the IMF.

Table 3. Cambodia: Balance of Payments, 2012–22 (BPM5)

(In millions of U.S. dollars, unless otherwise indicated)

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
						Proj.					
Current account (including official transfers)	-1,150	-1,979	-1,641	-1,694	-1,776	-1,904	-2,098	-2,250	-2,438	-2,617	-2,733
(Excluding official transfers)	-1,438	-2,270	-1,966	-2,043	-2,162	-2,246	-2,453	-2,618	-2,803	-2,979	-3,108
Trade balance	-2,506	-3,219	-3,206	-3,467	-3,415	-3,605	-4,012	-4,381	-4,770	-5,173	-5,554
Exports, f.o.b.	5,633	6,530	7,407	8,453	9,233	10,112	11,041	12,107	13,342	14,646	15,892
Of which: Garments	4,245	4,911	5,334	5,881	6,347	6,748	7,160	7,625	8,120	8,667	9,168
Imports, f.o.b. 1/	-8,139	-9,749	-10,613	-11,920	-12,649	-13,717	-15,053	-16,488	-18,112	-19,819	-21,446
Of which: Garments-related	-2,012	-2,483	-2,572	-2,950	-3,226	-3,430	-3,639	-3,876	-4,127	-4,406	-4,660
Petroleum	-1,179	-1,123	-1,145	-1,300	-1,465	-1,626	-1,703	-1,859	-2,014	-2,175	-2,339
Services and income (net)	944	860	972	925	728	779	901	1,017	1,126	1,247	1,385
Services (net)	1,658	1,735	1,927	2,032	1,975	2,137	2,366	2,595	2,822	3,068	3,334
Of which: Tourism (credit)	2,463	2,660	2,953	3,136	3,212	3,639	4,004	4,357	4,712	5,092	5,344
Income (net)	-714	-875	-955	-1,107	-1,247	-1,358	-1,465	-1,578	-1,697	-1,821	-1,949
Private transfers (net)	124	89	268	498	525	580	658	746	841	947	1,061
Official transfers (net)	288	291	325	350	386	342	355	368	365	362	375
Capital and financial account	1,538	2,341	2,396	2,469	2,649	3,270	2,956	3,106	3,367	3,577	3,748
Medium- and long-term loans (net)	649	613	473	451	517	806	857	881	903	997	1,059
Disbursements	695	676	555	558	689	959	1,046	1,103	1,176	1,293	1,387
Amortization	-47	-63	-83	-108	-172	-152	-189	-222	-274	-296	-328
Foreign direct investment 2/	1,698	1,825	1,677	1,654	2,166	2,425	2,577	2,736	2,895	3,054	3,210
Net foreign assets of deposit money banks 3/	445	-600	-213	986	-224	-134	-649	-683	-602	-646	-693
Unrestricted foreign currency deposit at NBC	-256	-59	-95	-257	-657	-398	-399	-418	-322	-351	-383
Commercial banks	701	-541	-118	1,243	433	264	-250	-265	-280	-295	-310
Other short-term flows and errors and omissions	-1,475	227	117	-899	19	0	0	0	0	0	0
Overall balance	388	363	755	775	873	1,366	858	856	929	960	1,015
Financing	-388	-363	-755	-775	-873	-1,366	-858	-856	-929	-960	-1,015
Change in gross official reserves 4/	-388	-363	-755	-775	-873	-1,366	-858	-856	-929	-960	-1,015
Accumulation of arrears	0	0	0	0	0	0	0	0	0	0	0
Memorandum items:											
Current account balance (in percent of GDP)											
Excluding official transfers	-10.2	-14.9	-11.8	-11.3	-10.7	-10.1	-10.1	-9.9	-9.7	-9.5	-9.1
Including official transfers	-8.2	-13.0	-9.8	-9.3	-8.8	-8.6	-8.6	-8.5	-8.4	-8.3	-8.0
Trade balance (in percent of GDP)	-17.8	-21.1	-19.2	-19.1	-16.9	-16.2	-16.5	-16.5	-16.5	-16.4	-16.3
Gross official reserves 5/	3,463	3,642	4,391	5,093	6,731	8,097	8,955	9,811	10,739	11,699	12,714
(In months of next year's imports)	3.6	3.5	3.8	4.2	5.0	5.5	5.6	5.6	5.6	5.6	5.7

Sources: Cambodian authorities; and IMF staff estimates and projections.

1/ From 2011, includes imports related to public-private power sector projects.
2/ From 2011, includes FDI related to public-private power sector projects.
3/ Includes unrestricted foreign currency deposits (FCDs) held as reserves at the National Bank of Cambodia (NBC).
4/ Excludes changes in unrestricted FCDs held as reserves at the NBC, and changes in gold holdings and valuation.
5/ Excludes unrestricted FCDs held at the NBC; starting in 2009, includes the new SDR allocations made by the IMF of SDR 68.4 million; starting 2016, renminbi holdings are considered part of reserves following inclusion of renminbi in the SDR basket.

Table 3. Cambodia: Balance of Payments, 2012–22 (BPM5) (Concluded)

(In percent of GDP, unless otherwise indicated)

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
								Proj.			
Current account (including official transfers)	-8.2	-13.0	-9.8	-9.3	-8.8	-8.6	-8.6	-8.5	-8.4	-8.3	-8.0
(Excluding official transfers)	-10.2	-14.9	-11.8	-11.3	-10.7	-10.1	-10.1	-9.9	-9.7	-9.5	-9.1
Trade balance	-17.8	-21.1	-19.2	-19.1	-16.9	-16.2	-16.5	-16.5	-16.5	-16.4	-16.3
Exports, f.o.b.	40.1	42.8	44.3	46.6	45.8	45.4	45.4	45.6	46.1	46.5	46.5
Of which: Garments	30.2	32.2	31.9	32.4	31.5	30.3	29.5	28.7	28.1	27.5	26.8
Imports, f.o.b. 1/	-57.9	-63.9	-63.5	-65.7	-62.7	-61.6	-61.9	-62.1	-62.6	-62.9	-62.8
Of which: Garments-related	-14.3	-16.3	-15.4	-16.3	-16.0	-15.4	-15.0	-14.6	-14.3	-14.0	-13.6
Petroleum	-8.4	-7.4	-6.9	-7.2	-7.3	-7.3	-7.0	-7.0	-7.0	-6.9	-6.8
Services and income (net)	6.7	5.6	5.8	5.1	3.6	3.5	3.7	3.8	3.9	4.0	4.1
Services (net)	11.8	11.4	11.5	11.2	9.8	9.6	9.7	9.8	9.7	9.7	9.8
Of which: Tourism (credit)	17.5	17.4	17.7	17.3	15.9	16.4	16.5	16.4	16.3	16.2	15.6
Income (net)	-5.1	-5.7	-5.7	-6.1	-6.2	-6.1	-6.0	-5.9	-5.9	-5.8	-5.7
Private transfers (net)	0.9	0.6	1.6	2.7	2.6	2.6	2.7	2.8	2.9	3.0	3.1
Official transfers (net)	2.1	1.9	1.9	1.9	1.9	1.5	1.5	1.4	1.3	1.1	1.1
Capital and financial account	10.9	15.4	14.3	13.6	13.1	14.7	12.2	11.7	11.6	11.4	11.0
Medium- and long-term loans (net)	4.6	4.0	2.8	2.5	2.6	3.6	3.5	3.3	3.1	3.2	3.1
Disbursements	4.9	4.4	3.3	3.1	3.4	4.3	4.3	4.2	4.1	4.1	4.1
Amortization	-0.3	-0.4	-0.5	-0.6	-0.9	-0.7	-0.8	-0.8	-0.9	-0.9	-1.0
Foreign direct investment 2/	12.1	12.0	10.0	9.1	10.7	10.9	10.6	10.3	10.0	9.7	9.4
Net foreign assets of deposit money banks 3/	3.2	-3.9	-1.3	5.4	-1.1	-0.6	-2.7	-2.6	-2.1	-2.1	-2.0
Unrestricted foreign currency deposit at NBC	-1.8	-0.4	-0.6	-1.4	-3.3	-1.8	-1.6	-1.6	-1.1	-1.1	-1.1
Commercial banks	5.0	-3.5	-0.7	6.8	2.1	1.2	-1.0	-1.0	-1.0	-0.9	-0.9
Other short-term flows and errors and omissions	-10.5	1.5	0.7	-5.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	2.8	2.4	4.5	4.3	4.3	6.1	3.5	3.2	3.2	3.0	3.0
Financing	-2.8	-2.4	-4.5	-4.3	-4.3	-6.1	-3.5	-3.2	-3.2	-3.0	-3.0
Change in gross official reserves 4/	-2.8	-2.4	-4.5	-4.3	-4.3	-6.1	-3.5	-3.2	-3.2	-3.0	-3.0
Accumulation of arrears	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:											
Current account balance (in percent of GDP)											
Excluding official transfers	-10.2	-14.9	-11.8	-11.3	-10.7	-10.1	-10.1	-9.9	-9.7	-9.5	-9.1
Including official transfers	-8.2	-13.0	-9.8	-9.3	-8.8	-8.6	-8.6	-8.5	-8.4	-8.3	-8.0
Trade balance (in percent of GDP)	-17.8	-21.1	-19.2	-19.1	-16.9	-16.2	-16.5	-16.5	-16.5	-16.4	-16.3
Gross official reserves 5/	24.6	23.9	26.3	28.1	33.4	36.4	36.8	36.9	37.1	37.2	37.2
(In months of next year's imports)	3.6	3.5	3.8	4.2	5.0	5.5	5.6	5.6	5.6	5.6	5.7

Sources: Cambodian authorities; and IMF staff estimates and projections.

1/ From 2011, includes imports related to public-private power sector projects.

2/ From 2011, includes FDI related to public-private power sector projects.

3/ Includes unrestricted foreign currency deposits (FCDs) held as reserves at the National Bank of Cambodia (NBC).

4/ Excludes changes in unrestricted FCDs held as reserves at the NBC, and changes in gold holdings and valuation.

5/ Excludes unrestricted FCDs held at the NBC; starting in 2009, includes the new SDR allocations made by the IMF of SDR 68.4 million; starting 2016, renminbi holdings are considered part of reserves following inclusion of renminbi in the SDR basket.

Table 4. Cambodia: General Government Operations, 2012–22 (GFSM 2001)

	2012	2013	2014	2015	2016		2017		2018	2019	2020	2021	2022
	Actual	Actual	Actual	Actual	Budget	Proj.	Budget	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
						(In billions of riels)							
Revenue	9,590	11,372	13,395	13,838	14,288	16,214	16,314	17,617	19,510	21,759	24,431	26,969	29,878
Of which: Nongrant	8,017	8,971	11,398	12,169	14,038	14,589	15,715	16,226	18,053	20,231	22,898	25,436	28,271
Tax	6,424	7,265	9,297	10,719	11,453	12,521	13,360	13,796	15,249	16,855	18,795	20,916	23,163
Income, profits, and capital gains	1,276	1,561	1,964	2,472	2,472	2,953	3,276	3,374	3,835	4,280	4,856	5,448	6,212
Good and services	3,815	4,210	5,450	6,238	6,462	7,423	7,884	8,156	9,012	9,908	11,000	12,205	13,373
International trade and transactions	1,333	1,493	1,883	2,009	2,519	2,145	2,200	2,266	2,402	2,667	2,938	3,264	3,579
Grants	1,572	2,401	1,997	1,669	250	1,625	599	1,390	1,457	1,527	1,533	1,534	1,607
Other revenues 1/	1,593	1,706	2,101	1,450	2,585	2,069	2,355	2,431	2,804	3,376	4,103	4,520	5,107
Total expenditure	11,741	12,686	14,160	15,000	18,163	18,524	20,011	20,943	24,054	26,601	29,297	32,266	35,455
Expense	6,818	7,351	8,838	9,740	11,885	12,149	13,543	13,543	15,527	17,265	19,006	20,904	22,955
Compensation of employees	2,660	3,119	3,952	4,941	5,636	5,805	7,134	7,134	8,337	9,212	10,147	11,160	12236.9
Purchase of goods and services	2,310	2,400	2,798	2,941	3,474	3,256	4,347	4,347	4,801	5,305	5,844	6,427	7,047
Interest	305	439	232	223	335	336	342	342	424	421	399	431	436
Expense not elsewhere classified	1,543	1,393	1,856	1,635	2,440	2,752	1,720	1,720	1,965	2,327	2,616	2,886	3,235
Net acquisition of nonfinancial assets	4,922	5,335	5,322	5,260	6,279	6,375	6,468	7,400	8,527	9,337	10,291	11,361	12,499
Of which: Externally financed	4,023	4,306	4,147	3,566	4,228	4,356	4,284	5,217	5,684	6,036	6,394	6,944	7,480
Net lending (+)/borrowing(-)	-2,151	-1,314	-765	-1,161	-3,875	-2,309	-3,794	-3,326	-4,543	-4,843	-4,866	-5,296	-5,576
Net acquisition of financial assets	363	308	1,564	2,070	0	1,720	0	500	-480	-514	-204	-105	56
Net incurrence of liabilities 2/	2,514	1,623	2,329	3,231	3,875	4,029	3,794	3,826	4,063	4,328	4,662	5,192	5,632
Of which: External	2,350	1,943	2,115	1,806	3,875	2,296	3,794	3,465	3,720	3,866	4,008	4,463	4,784
						(In percent of GDP)							
Revenue	16.9	18.5	19.8	18.8	17.5	19.8	18.1	19.5	19.6	19.7	20.1	20.2	20.4
Nongrant	14.2	14.6	16.9	16.5	17.2	17.9	17.4	18.0	18.1	18.4	18.9	19.0	19.3
Tax	11.3	11.8	13.8	14.5	14.0	15.3	14.8	15.3	15.3	15.3	15.5	15.7	15.8
Income, profits, and capital gains tax	2.3	2.5	2.9	3.4	3.0	3.6	3.6	3.7	3.8	3.9	4.0	4.1	4.2
Good and services tax	6.7	6.9	8.1	8.5	7.9	9.1	8.7	9.0	9.0	9.0	9.1	9.1	9.1
International trade and transactions tax	2.4	2.4	2.8	2.7	3.1	2.6	2.4	2.5	2.4	2.4	2.4	2.4	2.4
Grants	2.8	3.9	3.0	2.3	0.3	2.0	0.7	1.5	1.5	1.4	1.3	1.1	1.1
Other revenues	2.8	2.8	3.1	2.0	3.2	2.5	2.6	2.7	2.8	3.1	3.4	3.4	3.5
Total expenditure	20.7	20.7	21.0	20.4	22.2	22.7	22.2	23.2	24.1	24.1	24.1	24.2	24.2
Expense	12.0	12.0	13.1	13.2	14.5	14.9	15.0	15.0	15.6	15.7	15.7	15.7	15.7
Compensation of employees	4.7	5.1	5.9	6.7	6.9	7.1	7.9	7.9	8.4	8.4	8.4	8.4	8.4
Purchase of goods and services	4.1	3.9	4.1	4.0	4.3	4.0	4.8	4.8	4.8	4.8	4.8	4.8	4.8
Interest	0.5	0.7	0.3	0.3	0.4	0.4	0.4	0.4	0.4	0.4	0.3	0.3	0.3
Expense not elsewhere classified	2.7	2.3	2.8	2.2	3.0	3.4	1.9	1.9	2.0	2.1	2.2	2.2	2.2
Net acquisition of nonfinancial assets	8.7	8.7	7.9	7.1	7.7	7.8	7.2	8.2	8.5	8.5	8.5	8.5	8.5
Of which: Externally-financed	7.1	7.0	6.1	4.8	5.2	5.3	4.7	5.8	5.7	5.5	5.3	5.2	5.1
Net lending (+)/borrowing(-)	-3.8	-2.1	-1.1	-1.6	-4.7	-2.8	-4.2	-3.7	-4.6	-4.4	-4.0	-4.0	-3.8
Net acquisition of financial assets	0.6	0.5	2.3	2.8	0.0	2.1	0.0	0.6	-0.5	-0.5	-0.2	-0.1	0.0
Net incurrence of liabilities	4.4	2.6	3.5	4.4	4.7	4.9	4.2	4.2	4.1	3.9	3.8	3.9	3.8
Of which: External	4.1	3.2	3.1	2.5	4.7	2.8	4.2	3.8	3.7	3.5	3.3	3.3	3.3
Memorandum items:													
Net lending (+)/borrowing(-) excluding grant	-6.3	-6.4	-4.1	-2.9	-4.8	-4.6	-4.7	-5.2	-6.0	-5.8	-5.3	-5.1	-4.9
Domestic financing	0.7	-0.5	-1.5	-0.7	0.0	0.2	1.0	0.0	1.0	1.1	0.9	0.8	0.7
Government deposits	4.9	5.0	6.9	9.1	…	10.1	…	9.7	8.3	7.1	6.2	5.6	5.1
GDP (in billions of riels)	56,650	61,414	67,485	73,694	81,703	81,703	90,325	90,325	99,753	110,221	121,416	133,535	146,417

Sources: Data provided by the Cambodian authorities; and IMF staff estimates and projections.

1/ Includes provincial tax and nontax revenue.

2/ Includes statistical discrepancy.

Table 5. Cambodia: Monetary Survey, 2012–18

	2012	2013	2014	2015	2016	2017	2018
						Proj.	
				(In billions of riels)			
Net foreign assets	18,172	21,285	26,742	26,707	31,814	36,608	45,054
National Bank of Cambodia	18,583	19,535	24,476	29,490	36,336	42,258	48,263
Foreign assets	19,003	19,957	24,880	29,875	36,707	42,629	48,633
Foreign liabilities	421	421	404	385	371	371	371
Deposit money banks	-411	1,750	2,266	-2,782	-4,522	-5,650	-3,209
Foreign assets	5,628	8,589	10,048	9,481	10,875	11,991	13,214
Foreign liabilities	6,038	6,839	7,782	12,263	15,397	17,641	16,423
Net domestic assets	10,420	11,483	15,817	22,116	25,802	29,320	29,383
Domestic credit	21,056	24,827	31,885	39,642	48,310	55,377	61,729
Government (net)	-2,486	-2,795	-4,359	-6,429	-8,148	-8,139	-8,139
Private sector	23,537	27,609	36,245	46,071	56,459	63,516	69,868
Other items (net)	-10,636	-13,344	-16,068	-17,526	-22,508	-26,057	-32,346
Broad money	28,592	32,768	42,560	48,823	57,617	65,928	74,437
Narrow money	4,046	4,878	6,308	6,741	7,273	8,320	9,391
Currency in circulation	3,756	4,454	5,593	5,897	6,473	7,407	8,364
Demand deposits	290	424	715	845	800	913	1,027
Quasi-money	24,546	27,890	36,251	42,082	50,344	57,608	65,046
Time deposits	780	945	1,090	1,550	2,386	2,731	3,083
Foreign currency deposits	23,766	26,945	35,161	40,532	47,957	54,877	61,963
				(12-month percentage change)			
Net foreign assets	-1.4	17.1	25.6	-0.1	19.1	15.1	23.1
Private sector credit	38.3	17.3	31.3	27.1	22.5	12.5	10.0
Broad money	20.9	14.6	29.9	14.7	18.0	14.4	12.9
Of which: Currency in circulation	-0.4	18.6	25.6	5.4	9.8	14.4	12.9
Foreign currency deposits	24.3	13.4	30.5	15.3	18.3	14.4	12.9
				(Contribution to year-on-year growth of broad money, in percentage points)			
Net foreign assets	-1.1	10.9	16.7	-0.1	10.5	8.3	12.8
Net domestic assets	22.0	3.7	13.2	14.8	7.6	6.1	0.1
Domestic credit 1/	26.0	13.2	21.5	18.2	17.8	12.3	9.6
Government (net)	-1.5	-1.1	-4.8	-4.9	-3.5	0.0	0.0
Private sector	27.6	14.2	26.4	23.1	21.3	12.2	9.6
Other items (net)	-4.0	-9.5	-8.3	-3.4	-10.2	-6.2	-9.5
Memorandum items:							
Foreign currency deposits (in millions of U.S. dollars)	5,949	6,745	8,628	10,008	11,879	13,446	15,017
(In percent of broad money)	83.1	82.2	82.6	83.0	83.2	83.2	83.2
Riel component of broad money	4,826	5,823	7,399	8,291	9,659	11,051	12,474
(In percent of broad money)	16.9	17.8	17.4	17.0	16.8	16.8	16.8
Credit to the private sector (in millions of U.S. dollars)	5,892	6,911	8,894	11,376	13,985	15,562	16,932
(In percent of GDP)	41.5	45.0	53.5	62.7	68.7	70.2	70.1
Foreign Currency Loans	23,345	27,368	35,677	45,424	55,741	62,709	68,979
Loan-to-deposit ratio (in percent) 2/	98.2	101.6	101.5	112.1	116.2	114.3	111.3
Velocity 3/	2.2	2.0	1.8	1.6	1.6	1.4	1.4
Money multiplier (broad money/reserve money)	2.2	2.2	2.3	2.2	2.0	2.1	2.2
Reserve money (12-month percent change)	19.0	13.0	24.6	21.7	25.0	10.1	10.1

Sources: Cambodian authorities; and IMF staff estimates and projections.
1/ Excludes banks' credits to nonresident.
2/ Foreign currency loans and deposits only.
3/ The ratio of nominal GDP to the year-to-date average stock of broad money.

Table 6. Cambodia: Core Financial Soundness Indicators (FSIs), 2013–17

(In percent)

	2013				2014				2015				2016				2017
	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.	Mar.
Capital-based FSIs																	
Regulatory capital to risk-weighted assets	24.9	25.0	25.2	24.2	23.9	22.6	21.3	20.4	22.0	21.6	20.9	20.3	20.8	20.6	21.0	20.9	22.6
Regulatory tier 1 capital to risk-weighted assets	26.1	25.7	25.9	24.8	25.1	24.1	22.9	21.7	25.1	24.1	22.9	21.7	20.4	19.2	18.0	16.8	20.1
Nonperforming loans net of provisions to capital	3.4	3.7	4.1	3.9	3.3	3.7	4.0	3.3	4.1	4.6	4.4	3.4	5.1	6.5	6.4	4.5	4.8
Return on equity 1/	14.3	13.0	13.2	12.1	15.3	15.7	15.8	15.5	17.4	17.5	17.2	16.3	16.8	16.0	15.4	14.5	15.2
Net open position in foreign exchange to capital	2.9	3.4	4.6	9.4	4.3	4.4	4.2	4.1	3.6	3.8	3.8	3.6	2.9	3.2	3.3	2.6	2.1
Asset-based FSIs																	
Nonperforming loans to total gross loans	2.1	2.3	2.3	2.3	1.9	1.9	2.0	1.6	1.9	2.0	1.9	1.6	2.1	2.6	2.7	2.1	2.2
Return on assets 1/	2.7	2.5	2.6	2.4	3.0	3.0	3.0	2.9	3.1	3.1	3.1	2.9	2.9	2.7	2.6	2.5	2.6
Liquid assets to total assets	16.2	16.0	16.8	17.9	15.2	17.8	17.6	16.2	16.6	16.3	15.5	16.6	15.9	16.1	15.3	15.8	16.2
Liquid assets to short-term liabilities	21.5	21.4	23.2	24.2	21.5	25.1	24.6	23.1	23.9	23.8	23.3	25.4	24.4	24.4	23.6	24.3	24.9
Sectoral distribution of loans to total gross loans																	
Residents	93.3	93.1	92.6	92.8	90.8	93.3	93.6	94.6	94.9	95.2	95.0	96.0	95.8	98.0	98.7	99.5	98.2
Deposit-takers	0.5	0.5	0.6	1.1	0.9	0.5	1.1	1.4	1.4	1.5	1.5	1.8	1.9	1.9	1.4	1.4	1.3
Central bank	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Other financial corporations	-	-	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
General government	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Nonfinancial corporations	75.4	74.4	73.3	71.9	72.5	74.7	74.3	74.8	74.9	74.8	72.3	72.1	71.4	72.4	72.8	73.1	72.1
Other domestic sectors	17.4	18.3	18.7	19.6	17.3	17.9	18.1	18.3	18.4	18.8	21.2	22.0	22.4	23.6	24.5	24.9	24.7
Nonresidents	6.7	6.9	7.4	7.2	9.2	6.7	6.4	5.4	5.1	4.8	5.0	4.0	4.2	2.0	1.3	0.5	1.8
Income- and expense-based FSIs																	
Interest margin to gross income	69.7	67.9	69.3	68.6	71.6	72.9	72.5	72.9	50.5	57.3	60.2	63.1	70.5	66.2	67.4	65.3	63.5
Noninterest expenses to gross income	49.5	51.3	51.0	52.4	56.6	55.3	55.2	55.1	67.4	63.5	61.5	60.6	56.5	59.6	59.3	59.7	58.7

Source: National Bank of Cambodia.

1/ Annualized.

Table 7. Cambodia: Key FSAP Recommendations of High Priority

Recommendation	Timeframe 1/	Status
General Stability		
• Improve the quality of data to enable an appropriate assessment of risks, and to enhance the reliability of stress tests, including through strengthening supervision; and collecting additional credit-related information.	Short-term	In process
• Ensure that banks retain an appropriate level of liquid assets to be able to meet short-term obligations by enforcing existing regulations.	Short-term	Improved but still in process
• Upgrade law to formalize delineation of responsibilities among supervisors, and establish procedures, through MOUs, for practical information exchange, coordination and accountability among domestic supervisors (NBC, MEF, SECC), and with foreign supervisors.	Short-term	Improved but still in process
• Upgrade both the number and capacity of staff in the areas of banking, insurance, securities and payment system supervision; develop training programs for financial institutions on accounting, corporate governance, risk management, and for the external audit profession.	Medium-term	In process
• Develop and implement a strategic plan to address the conflicts and overlaps in the financial sector legal and regulatory framework.	Medium-term	In process
Supervision and Regulation		
Banking		
• Develop supervisory strategy to deal with banks that cannot meet the new capital. requirement.	Short-term	Done
• Conduct comprehensive upgrades to the legal framework.	Short-term	In process
• Reprioritize the work performed by the staff to facilitate forward-looking, risk-based supervision.	Short-term	In process
• Impose a moratorium on the issuance of new bank licenses as long as supervisory capacity and resources remain inadequate.	Short-term	Overruled: large increase of the number of banks and MFIs
Non-Bank Financial Sector		
• Revise capital regulations in concert with liability, investment and accounting rules to better reflect the risks in a growing insurance market.	Short-term	Done
• Enhance powers for intervention, corrective measures, and enforcement.	Short-term	In process
• Conduct a readiness study prior to the launch of the stock exchange.	Short-term	Done
Access to Finance		
• Enhance supervisory practices to keep pace with the development of microfinance deposit-taking institutions, and impose a moratorium as long as supervisory capacity and resources remain inadequate.	Medium-term	In process
Crisis Management Framework		
• Revise PCA framework by developing additional triggers for asset quality, liquidity, and earlier intervention based on the solvency ratio.	Medium-term	In process
• Introduce regulation allowing banks to use their fixed deposits at the NBC and any issue of government (including government bodies) or government-guaranteed securities as eligible collateral for interbank and NBC repos.	Short term	Done
• Develop a crisis management framework.	Medium-term	In preparation
Transparency of Monetary and Financial Policies		
• Introduce due process for the dismissal of NBC Board members and the Governor by specifying the legal grounds for doing so, and defining an appeal process.	Medium-term	In preparation
• Amend the law to reduce the government's representation on the Board of the NBC; and to reflect the practice of appointing two Deputy Governors.	Short-term	In preparation
Corporate governance of banks		
• Draft and/or implement banking regulations on internal audit and controls, risk management, and compliance functions at banks.	Short-term	Risk management to be done
AML/CFT 2/		
• Introduce new rules measures for conducting overall AML/CFT risk assessments and risk profiling of financial institutions.	Short-term	In process

Source: IMF staff.
1/ Short term: up to one year; medium term: one to three years.
2/ Since the 2010 FSAP, Cambodia has made progress in addressing deficiencies in its legal and regulatory framework against the 2003 FATF standard, and was removed from the FATF's On-Going Global AML/CFT Compliance Process in February2015. However, the issues identified in the 2016 APG (Asia/Pacific Group on Money Laundering) assessment against the 2012 FATF standard need to be urgently addressed.

Table 8. Cambodia: Millennium Development Goals (MDG) Indicators, 1990–2015

	1990	1995	2000	2005	2009	2010	2011	2012	2013	2014	2015	2015 MDG Target
Goal 1: Eradicate extreme poverty and hunger												
Percentage share of income or consumption held by poorest 20 percent	...	8.5	...	...	8	8	9	9	...	...	...	11
Population below minimum level of dietary energy consumption (percent)	...	29	32	21	17	17	17	16	16	15	14	21
Poverty headcount ratio at $1.25 per day (PPP, percent of population)	...	...	...	...	5	5	3	2	...	...	...	20
Poverty headcount ratio at national poverty line (percent of population)	...	...	...	...	24	22	21	18	...	...	...	
Prevalence of underweight in children (under five years of age)	...	43	40	28	...	29	...	...	...	...		26
Goal 2: Achieve universal primary education												
Net primary enrollment (percent of relevant age group)	...	92	...	...	...	93	98	97	...	95	89	100
Primary completion rate, total (percent of relevant age group)	...	42	47	85	83	85	87	93	94	96	95	100
Proportion of pupils starting grade 1 who reach grade 5	...	...	63	...	...	69	73	70	58	...	...	100
Youth literacy rate (percent of ages 15–24)	...	...	...	...	87	...	...	...	...	...	92	100
Goal 3: Promote gender equality and empower women												
Proportion of seats held by women in national parliament (percent)	...	...	7	10	21	21	20	20	20	20	20	30
Ratio of girls to boys in primary and secondary education (percent)	...	...	82	...	...	...	...	...	...	...	...	100
Ratio of young literate females to males (percent ages 15–24)	81	84	89	90	97	...	...	...	...	...	101	100
Share of women employed in the nonagricultural sector (percent)	..	..	41	..	...	41	...	41	...	...	...	...
Goal 4: Reduce child mortality												
Immunization, measles (percent of children ages 12–23 months)	34	62	65	79	92	89	83	79	76	80	81	90
Infant mortality rate (per 1,000 live births)	85	88	80	53	40	37	34	31	28	26	25	50
Under five mortality rate (per 1,000)	117	122	108	65	47	43	39	36	33	31	29	38
Goal 5: Improve maternal health												
Births attended by skilled health staff (percent of total)	..	..	32	44	...	71	72	74	...	89	...	80
Maternal mortality ratio (modeled estimate, per 100,000 live births)	1020	730	484	315	217	202	188	178	173	167	161	250
Goal 6: Combat HIV/AIDS, malaria, and other diseases												
Incidence of tuberculosis (per 100,000 people)	585	557	575	511	450	436	423	411	400	390	380	...
Prevalence of HIV, total (percent of population 15–49)	0	1	2	1	1	1	1	1	1	1	1	...
Goal 7: Ensure environmental sustainability												
Access to an improved water source (percent of population)	23	30	42	53	62	64	67	69	71	73	76	...
Access to improved sanitation (percent of population)	3	8	16	25	32	34	35	37	39	41	42	...
Nationally protected areas (percent of total land area)	0	...	23	...	...	...	...	...	...	26	...	...
Goal 8: Develop a global partnership for development												
Aid per capita (current U.S. dollars)	5	52	32	40	51	51	54	54	54	52	43	...
Fixed line and mobile phone subscribers (per 100 people)	0	0	1	8	45	59	98	132	137	135	135	...
Internet users (per 1,000 people)	0	...	0	0	1	1	3	5	7	14	19	...
Total debt service (percent of exports of goods and services)	...	1	1	1	1	1	4	6	6	6	6	...
Goal 9: De-mining, UXO and assistance												
Annual numbers of civilian casualties recorded	...	1,691	...	797	244	286	240	240	...	...	...	0
Percentage of suspected contaminated areas cleared	...	10	...	50	53	59	56	56	...	...	...	100
Other												
Fertility rate, total (births per woman)	6	5	4	3	3	3	3	3	3	3	3	...
GNI per capita, Atlas method (current U.S. dollars)	...	300	300	460	690	750	810	880	960	1020	1070	...
GNI, Atlas method (current, in billions of U.S. dollars)	...	3	4	6	10	11	12	13	14	16	17	...
Gross capital formation (percent of GDP)	...	15	18	18	21	17	17	19	20	22	22	...
Life expectancy at birth, total (years)	54	55	58	63	66	66	67	67	68	68	69	...
Literacy rate, adult total (percent of people ages 15 and above)	...	...	...	...	74	...	...	...	...	...	78	...
Population, total (millions)	9	11	12	13	14	14	15	15	15	15	16	...
Trade (percent of GDP)	...	78	112	137	105	114	114	121	128	129	128	...

Sources: World Bank database, *World Development Indicators,* and *Poverty Assessment* (2009); UN Human Development Indicators Report (2003); Cambodia MDG 2011 update; UN MDG Indicators 2011 (http://mdgs.un.org); and IMF staff estimates.

Appendix I. Risk Assessment Matrix

	Event	Risk Horizon	Up/ Down -side	Prob.	Impact	Transmission	Policy Recommendations
Domestic Risks	Revenue shortfall	Medium-term	↓	**High**	**Medium**	Fiscal position deteriorates -fiscal deficits widen and government deposits deplete sharply.	Steadfast implementation of RMS, while rationalizing non-developmental current expenditure.
	A large correction in real estate prices.	Short-term	↓	**Medium**	**High**	Turning of the credit cycle and fallout from excess household and corporate leverage (incl. in FX) as investors withdraw FX deposits, generating disorderly deleveraging.	Increase reserve requirements to slow down credit growth, implement macro prudential measures, strengthen micro-prudential regulation and supervision, ensure adequate emergency liquidity, strengthen supervision and regulation for MFIs. Preemptively strengthen the crisis management framework.
	Recurrent political uncertainty and/or labor market disruptions	Short-term	↓	**Medium**	**High**	Large deposit withdrawal, drag in FDI and export growth and weaker investor confidence.	Ensure continued macroeconomic stability to support confidence in the economy
	Extreme weather	Short-term	↓	**Medium**	**Medium**	Weaker agricultural production and exports, weaker tourism, and wider income inequality.	Expedite structural reforms to accelerate diversification, improve infrastructure, and increase transfers to the rural poor after creating fiscal space.
External Risks	Retreat from cross-border integration	Short-term	↓	**Medium**	**High**	Weaker garments export growth.	Expedite structural reforms to accelerate diversification, by expanding the narrow range of export products, while finding new export markets for existing products.
	Structurally weak growth in key advanced economies	Short-term	↓	**High**	**High**	Weaker garments export growth.	Expedite structural reforms to accelerate diversification, by expanding the narrow range of export products, while finding new export markets for existing products.
	Significant China slowdown	Short-term	↓	**Medium**	**Medium/ High**	Lower exports coupled with weaker FDI and banking sector flows.	Expedite structural reforms to accelerate diversification. Ensure adequate emergency liquidity.
	Tighter global financial conditions and strengthening of the US dollar	Short-term	↓	**High**	**High**	Higher rates would lead to FX deposit outflows, foreign reserves fall.	Build up foreign reserve buffers against external shocks; where appropriate release limited short-term liquidity to troubled banks; expedite work on a crisis management framework; increasing reserve requirements on foreign deposits substantially would create a buffer that could be liberated when foreign deposits flow out in response to external shocks.
					Medium	Stronger US dollar would lead to weaker exports, tourism receipts, FDI, and bank lending from other partner countries.	Maintain macroeconomic stability and develop interbank and foreign exchange markets to enhance monetary policy effectiveness and to reduce dollarization. Expedite structural reforms to boost non-price competitiveness.

The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. "Short term" and "medium term" are meant to indicate that the risk could materialize within 1 year and 3 years, respectively.

Appendix II. Past Fund Advice

The authorities are strengthening public financial management, in line with past Fund advice. They continue to improve tax administration by implementing their Revenue Mobilization Strategy (RMS). Notable progress has been made in strengthening core tax functions, improving human resource management and increasing automation. The government has been expanding the role of public-private partnerships (PPPs) for infrastructure financing. Progress has been slower in adopting other tax policy and administration reforms, public administration reform, as well as developing a medium-term budget framework. The authorities are implementing policies, such as the newly introduced liquidity coverage ratio and higher minimum capital requirements, to address financial stability risks and are in progress of introducing further prudential measures based on past Fund advice. Finally, the authorities are undertaking reforms in the education sector to improve the quality of basic education.

Appendix III. External Sector Assessment[1]

The external position of Cambodia in 2016 was moderately weaker than the level consistent with medium-term fundamentals and desirable policy settings. Policies to consolidate the fiscal position diversify export markets, and improve productivity and competitiveness should help improve the external balance position. There is room to build reserves given high dollarization and elevated financial vulnerabilities.

1. **Foreign asset and liability position.** Cambodia's Net Foreign Asset (NFA) position was -48 percent of GDP in 2016, placing it in the mid-range of its peers (Figure 2). It is almost entirely composed of FDI liabilities and as such does not pose a major concern for external sustainability at the moment. The NFA position is projected to increase over the medium term, in line with continuing FDI inflows. Based on the External Sustainability (ES) model a current account (CA) norm that stabilizes the NFA at its 2016 level implies 7.3 percent REER overvaluation, using EBA-lite elasticities. [2]Allowing NFA to reach 60 percent over the medium term would imply an overvaluation of 5.3 percent.

2016 External Balance Assessment Results

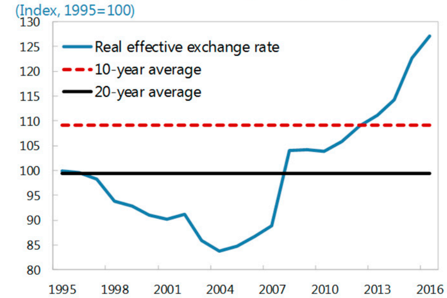
	CA model	REER model	ES model[1/]
Actual CA	-8.8		-8.0
CA norm	-3.9		-4.2
CA gap	-4.9		-3.8
REER gap[2/]	**9.5**	**18.8**	**7.3**

1/ For External Sustainability (ES) model, actual CA is the medium-term CA projection and CA norm is the CA that stabilizes NFA at the 2016 level of 48 percent GDP.
2/ Implied over(+)/under(-) valuation.

2. **Current account.** The CA deficit narrowed from 9.3 percent of GDP in 2015 to 8.8 percent in 2016, led by declining imports. The 2016 CA is assessed to be moderately weaker than the CA norm of 3.9 percent, which is the CA level suggested by fundamentals and desirable policy settings using the CA model. The resulting CA gap of -4.9 percent of GDP translates into an REER overvaluation of 9.5 percent. Part of this gap reflects the fact that the CA model does not fully take into account the very young population in Cambodia, which implies a fundamentally lower level of savings and a higher CA deficit. If the model were to use total instead of old-age dependency ratio, the CA norm would be expected to show a larger deficit, resulting in a smaller CA gap.

3. **Real effective exchange rate.** The REER on average appreciated by 4 percent between 2015 and 2016, reflecting a stronger U.S. dollar, buoyant economic growth, and capital inflows. In 2016 it was 16 percent higher than the 10-year average. Given that Cambodia primarily trades with advanced economies, the inflation differential is likely to contribute to further REER appreciation, until Cambodia diversifies into other markets. The REER model of EBA-lite suggests a somewhat higher level of overvaluation at 19 percent compared to the level implied by fundamentals and desirable policies. These results need to be taken with

Cambodia: Real Effective Exchange Rate (REER)
(Index, 1995=100)



Sources: INS; and IMF staff estimates.

[1] Prepared by Katsiaryna Svirydzenka.
[2] See "Methodological Note on EBA-Lite" (2016).

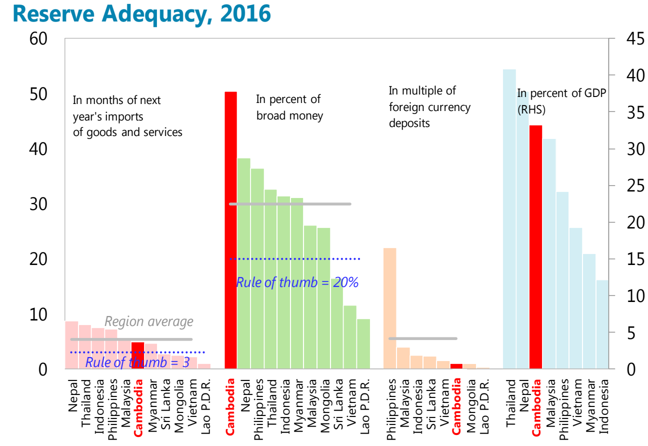
caution as the REER model is sensitive to the time sample used and may not fit well countries that are undergoing rapid structural change, such as Cambodia. While the REER in Cambodia continued to appreciate, it did so less than in peer countries and Cambodia's export market share continued to improve (Figure 2).

4. Recommended policies. To improve the external balance position and adjust the CA deficit to a more sustainable level, a policy package will be needed to consolidate the fiscal position diversify export markets, and improve productivity and competitiveness including through moderating minimum wage growth and improving infrastructure and education.

5. Capital flows. Cambodia continues to attract sizable capital inflows, with FDI inflows more than financing the CA deficit and contributing to the reserves buildup. While the composition of flows has a favorable risk profile, there is a risk that FDI inflows are helping fuel rapid real estate growth (Figure 1) and that Cambodia may experience smaller inflows as the global financial conditions tighten.

6. FX intervention and reserve adequacy. The current exchange rate regime is based on keeping the Riel broadly stable against the U.S. dollar and is appropriate for Cambodia given high dollarization and a concentration in U.S. dollar-invoiced exports. Over the last seven years, Cambodia has been consistently accumulating international reserves. Measured against several traditional metrics, Cambodia's gross international reserves appear to be adequate.[3] As of end 2016, reserves were equivalent to about 5 months of prospective imports of goods and services and 50 percent of broad money. Given the long-term nature of Cambodia's external debt, the third traditional metric – reserves in percent of short-term debt – is not as relevant. Applying the Assessing Reserve Adequacy (ARA) tool for Credit-Constrained Economies with fixed exchange rate regime to Cambodia suggests an optimal level of reserves of 4 months of current imports of goods and services, which is below the current reserve level.[4] However, gross official reserves covered only 57 percent of foreign currency deposits, which severely limits the central bank's lender of last resort capacity and is below regional comparators. Continued financial deepening in the context of near full dollarization suggests that foreign currency deposits are likely to continue to grow. This suggests that further accumulation of reserves beyond the level indicated by traditional reserve adequacy metrics, along with measures encouraging use of the Riel, are necessary to enhance resilience against financial sector vulnerabilities and rapid capital flow reversals.

Reserve Adequacy, 2016



Sources: IMF staff calculations.

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[3] See "Guidance Note on Assessing Reserve Adequacy and Related Considerations" (2016).

[4] Cambodia is assessed to be "credit constrained" for the purposes of this exercise given that it does not regularly borrow from international capital markets – defined as at least one issuance of bonds per year in the last five years – and is not rated to be "investment grade."

INTERNATIONAL MONETARY FUND

CAMBODIA

August 30, 2017

STAFF REPORT FOR THE 2017 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By

Asia and Pacific Department
(In consultation with other departments)

CONTENTS

FUND RELATIONS

(As of June 29, 2017)

Membership Status

Joined December 31, 1969; accepted the obligations under Article VIII, Sections 2, 3, and 4 on January 1, 2002.

General Resources Account:	**SDR Million**	**Percent Quota**
Quota	175.00	100.0
Fund holdings of currency (Exchange Rate)	153.13	87.50
Reserve Tranche Position	21.88	12.50

SDR Department:	**SDR Million**	**Percent Allocation**
Net cumulative allocation	83.92	100.00
Holdings	88.37	105.30

Outstanding Purchases and Loans: None

Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
ECF [1/]	Oct. 22, 1999	Feb. 28, 2003	58.50	58.50
ECF [1/]	May 06, 1994	Aug. 31, 1997	84.00	42.00

[1/] Formerly PRGF.

Overdue Obligations and Projected Payments to the Fund [2/]
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2016	2017	2018	2019	2020
Principal					
Charges/Interest		0.00	0.00	0.00	0.00
Total		0.00	0.00	0.00	0.00

[2/] When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Multilateral Debt Relief Initiative

As part of the Multilateral Debt Relief Initiative (MDRI), the IMF Executive Board on January 5, 2006, approved relief on 100 percent of debt incurred by Cambodia to the IMF before January 1, 2005. This resulted in the forgiving of all of Cambodia's outstanding debt to the IMF, a total of SDR 56.8 million (about US$82 million). The authorities intend to spend the resources over a number of years, initially on rural irrigation projects. The National Bank of Cambodia (NBC) transferred the full MDRI proceeds to the Ministry of Economy and Finance effective March 2006.

Safeguards Assessment

A voluntary safeguards assessment of the NBC was completed in January 2010 at the request of the authorities, which updated the previous March 2004 voluntary assessment. The update assessment found that the NBC had taken steps to strengthen aspects of its safeguards framework; however, important recommendations proposed in 2004 were still outstanding, and some new risks had emerged in the area of external audit.

Exchange Rate Arrangement and Payments System

Cambodia's exchange regime is classified as *other-managed arrangement*. The *de jure* regime is a *managed float*. The official exchange rate, which is expressed in riels per U.S. dollar, applies to all official external transactions conducted by the central government and state enterprises, and is used for accounting purposes by the NBC. It is determined by the foreign exchange market, with the official rate adjusted to be within 1 percent of the market rate on a daily basis.

Cambodia accepted the obligations of Article VIII, Sections 2, 3, and 4 on January 1, 2002. Cambodia maintains an exchange system that is free of restrictions on the making of payments and transfers for current international transactions.

Article IV Consultation

Cambodia is on the standard 12-month Article IV consultation cycle. The last Article IV consultation discussions were held in Phnom Penh during July 6-20, 2016. The Executive Board concluded the staff report (IMF Country Report 16/340) on October 19, 2016.

Financial Sector Assessment Program (FSAP)

The joint IMF-World Bank FSAP mission took place in March 2010 and the assessment was completed in October 2010.

Technical Assistance

Technical assistance is currently focused on bank supervision, financial stability, de-dollarization, monetary operations, AML/CFT, fiscal risks management, tax policy, and administration including customs administration, macro-fiscal and revenue forecasting, financial sector supervision, and macro-financial statistics. Delivery is through a resident advisor at the NBC and MEF, peripatetic experts, and short-term visits from headquarters.

Resident Representative

Ms. Yong Sarah Zhou has been the IMF Resident Representative in Phnom Penh since July 2015.

IMF-WORLD BANK COLLABORATION

(July 2017)

The Bank and the IMF teams for Cambodia, led by Ms. Deepak Mishra (Practice Manager GMFDR) and Mr. Jarkko Turunen (IMF Mission Chief for Cambodia), maintain a close working relationship and have an active dialogue on a range of macroeconomic and structural issues.

Recent key areas of cooperation and coordination include:

- **Macroeconomic policy advice to the authorities.** The IMF and the World Bank staffs have consulted each other on key macroeconomic policy messages to the authorities to avoid sending conflicting messages. Bank staff share and discuss the bi-annual Country and East-Asia and Pacific Economic Updates. IMF staff share policy notes and analytical background notes related to Article IV consultation missions. The World Bank and IMF staff regularly meet with policymakers from the Ministry of Economy and Finance and the National Bank of Cambodia to timely address emerging issues related to macroeconomic performance and management.

- **Financial sector reform and FSAP.** The World Bank and the IMF teams have worked closely together since the FSAP in 2010. In line with the FSAP recommendations, technical assistance missions supporting financial sector resilience are now ongoing and close coordination between the IMF and the World Bank continues. The IMF and the World Bank Group (WBG) have jointly worked to support financial sector stability in Cambodia, especially in the areas of crisis management, macro-prudential and financial stability. Both IMF and WBG have encouraged the National Bank of Cambodia to enhance its risk-based supervision by providing technical support on both legislative system and supervisory regime. The World Bank and the IMF teams currently are working together to support capacity building through knowledge sharing and south-south exchanges for the Ministry of Economy and Finance, the Securities and Exchange Commission of Cambodia, and the National Bank of Cambodia.

- **Public financial management and tax and customs administration reform.** Both institutions are working closely together under the Public Financial Management Reform Program (PFMRP) including 2014–18 revenue mobilization strategy as well as tax and customs administration reform. Both teams are members of the Development Partner Committee (DPC) of the PFMRP, a coordination mechanism for all Development Partners' support for the PFMRP under a Sector Wide Approach, and share information on the work done in this area. The WBG's multi-donor trust funded project, Public Financial Management Modernization Project, contributed to an improved revenue administration, comprehensive transaction processing, improved financial control, and an improved and more transparent financial report generation facility. The FMIS, which was implemented under the project, is a system of record and is fully operational at central offices of MEF and all 25 provincial treasuries. Central offices of the MEF including the ITD, GDNT (Accounting Department), GDSNAF, Budget, FAD, DI and DCDM connect to the system through remote terminals. Transactions for the districts and communes are processed at the respective provincial treasuries. With all transactions processed through the FMIS starting January 1, 2017, the system is capable of generating important information for management purposes. In addition, the IMF and the World Bank are closely communicating in the context of the preparation of a tax policy review (IMF) and an assessment of tax incentives (World Bank, under an ongoing Public Expenditure Review).

- **Trade facilitation and private sector development**. Both institutions are providing technical support to GDCE/MEF on customs and border reform, regulatory reform, and streamlined import and export procedures. The WBG Trade Related-Assistance in Cambodia program (TRAC) has contributed to enhanced information/improvements in the areas of nontariff measures (NTM), phytosanitary standards, improved trade logistics, trade repository, investment incentive policy, and integration into regional production networks. The WBG Trade Facilitation Facility (TFF) supported the GDCE/MEF to develop Cambodia National Single Window (CNSW) blueprint.

- **Trade Development Support Program (TDSP).** The TDSP continues to support the implementation of a trade sector wide approach (Trade SWAP) expansion of ASYCUDA to 58 customs checkpoints across the geography, covering 95 percent of imports and exports transactions; support to MAFF on SPS automation system; and technical assistance to MOC on certification of country origin automation, trade-marks registration system, business registration automation system, and trade training research institution (TTRI). TSDP also supports the private sector development on export training, value chain study, labor and commercial dispute resolution through the arbitration council foundation (ACF) and the national council arbitration of Cambodia (NCAC). Cambodia gained ranking 56 places in the Logistics Performance Indicators (LPI) in 2010–16, and abolished unnecessary certificates of origin (CO) required by the importing countries.

- **Article IV consultations.** IMF Article IV consultations regularly share their macroeconomic data with the World Bank and hold working sessions to try and reconcile macroeconomic data sets. The collaboration is closest on the debt sustainability analysis, a joint product, but extends more broadly into other areas of the consultation as well. World Bank staff are also invited to attend key meetings. The IMF also joined in some of the WB capacity building TA missions on contingent liabilities. Both institutions are considering using the TA mission findings to further strengthen the DSA analysis.

- **Structural reforms.** The IMF staff and the World Bank teams have worked together to share views on a range of other issues, including structural reforms for improving investment climate, economic diversification, public investment management, customs modernization, and rural development. The World Bank and IMF staff have worked together to encourage the authorities to speed up civil service reforms to improve public sector performance on public service delivery as well as to boost competitiveness.

Based on the above partnership, the World Bank and the IMF share a common view about Cambodia's macroeconomic and structural reform priorities. These include:

- **Sustaining growth.** Growth remains robust although there are signs of deceleration. While decelerating, the garment sector together with construction, and services, in particular finance and real estate, continues to propel growth. Overall macroeconomic management remains appropriate but there are emerging challenges to external competitiveness, partly derived from U.S. dollar appreciation and rising wages. Improving the business climate, reducing infrastructure, energy, and skills bottlenecks, promoting private sector development and economic diversification, improving governance and the delivery of public services and supporting rural development continue to be essential to promote self-sustaining and inclusive growth.

- **Managing public finances and debt.** Fiscal policy remains the main instrument for macroeconomic management given high dollarization. Prudent fiscal management is, therefore, critical and needs to be underpinned by continued improvements in revenue collection, prioritized spending, and better monitoring of contingent liabilities, including through the budgetary and public debt management framework and further progress in budgetary transparency.

- **Safeguarding financial system stability and improving the effectiveness of monetary policy.** Implementing the key recommendations of the 2010 FSAP remains critical to safeguarding financial stability. These include implementing a moratorium on new bank licenses, strengthening coordinated supervision, developing the foreign exchange market, establishing a domestic bond market, improving the supervisory capacity, enhancing efficient and stable payment system, improving quality of financial data, and encouraging a close coordination among financial regulators. Financial stability risks from the buoyant real estate markets need to be managed through strengthened supervision and improved data collection. Developing an interbank market remains a necessary step for a transition to more effective and market-based monetary policy operations.

- **Improving governance.** Both the World Bank and IMF have stressed the critical role of governance in improving the quality of service delivery and fostering private sector development, which is the engine of growth.

- **The teams are committed to continue the close cooperation going forward.** The table below details the specific activities planned by the two country teams over the next 12-month period along with their expected deliveries.

Cambodia: Joint Managerial Action Plan, 2017–18

Title	Products	Provisional and Actual Timing	Expected and Actual Delivery Date
	A. Mutual Information on Relevant Work Programs		
The World Bank's Work program in the next 12 Months	**Macroeconomic monitoring** • Semi-annual East Asia and Pacific economic updates • Cambodia Economic Update	Ongoing	Once every six months: tentatively in Apr. and Oct.
	Financial sector • FSAP follow-up technical assistance to implement IFRS roadmap for accounting and auditing practices in financial institutions. FSAP follow-up technical assistance to implement crisis management framework • FSAP follow-up technical assistance on prudential regulations and risk-based supervision in order to promote financial stability • FSAP follow up technical assistance on development in financial sector to promote financial inclusion agenda in Cambodia including micro-insurance	Ongoing	Two or three missions a year.
	• TA on AML/CFT, payment system road map, and financial education	Ongoing	June 2017
	Public sector management • Public Financial Management Reform Program (PFMRP) • Public administration reform (PAR) potential technical assistance support envisioned • Public Expenditure Review (PER under elaboration, to cover tax incentives, public investment management and key sectors such as agriculture and education • Preparation for Cambodia's systematic country diagnostic looking into sources of growth including drivers of growth and key constraints and bottlenecks	Ongoing	
	Trade and Private Sector Development • Trade Related Assistance in Cambodia (TRAC under Bank Execution) • Trade Dev. Support Program (TDSP under Recipient Execution) • Trade Logistic Blueprint and Connectivity • Customs modernization and reform • Nontariff measure (NTR) and trade repository • Investment incentive policy • SPS automation system, • Certification of country origin automation, • Trade mark registration and Intellectual Property Rights • Business registration automation system		
The IMF's Work Program in the next 12 Months	**Macroeconomic policy analysis and advice** • 2017 Article IV consultation • Policy notes on request	July 2017 Ongoing	September 2017
	Technical assistance • Fiscal sector: Tax and customs administration, tax policy, resident macro-fiscal advisor, PFM • Financial sector: FSAP follow-up work, resident banking supervision advisor, consolidated supervision, foreign exchange market, liquidity management, data improvement • Statistics: Government finance, monetary and financial sector, balance of payments • AML/CFT: legal drafting, FIU development/capacity building and risk based AML/CFT Supervision	Ongoing	
	B. Agreement on Joint Products and Missions		
Joint Products in the next 12 months	• Debt sustainability analysis	2017 Article IV	During Article IV

RELATIONS WITH THE ASIAN DEVELOPMENT BANK

(July 2017)

As of June 30, 2017, Cambodia has received $2.87 billion in Asian Development Bank (AsDB) lending, grants, and technical assistance, including: (i) 89 Asian Development Fund (ADF) loan projects and programs for $2,120.3 million with low interest; (ii) 3 Ordinary Capital Resources (OCR) loans for $89.6 million; (iii) 21 ADF grants for $255.71 million; and (iv) 2 special fund grants for $6.0 million.[1] Cumulative disbursements to Cambodia for sovereign and non-sovereign lending and grants are $1,982.8 million.

The sector composition of active lending, grants, and technical assistances totaling $1,070.31 million comprises: (i) Agriculture, Natural Resources and Rural Development $252.4 million (23.6 percent); (ii) Transport and Communications $197.8 million (18 percent); (iii) Water Supply and Urban Infrastructure and services $181.8 million (17 percent); (iv) Multisector $75.0 million (7.0 percent); (v) Education $95.0 million (9 percent); (vi) Industry and Trade $83.0 million (8 percent); (vii) Energy $45.0 million (4 percent); (viii) Public Sector Management (PSM) $30.1 million (3 percent); (ix) Health, Nutrition and Social Protection $10.0 million (1 percent).

The AsDB Cambodia Country Partnership Strategy (CPS), 2014–2018, endorsed by the Board on November 28, 2014, aligns with Cambodia's strategic planning cycle and the priorities reflected in the Rectangular Strategy for Growth, Employment, Equity and Efficiency, Phase III (RSIII) and the National Strategic Development Plan (NSDP, 2014–2018). Consistent with the Royal Government of Cambodia's economic reform priorities, the impact of the CPS will be reduction in poverty and vulnerability. The CPS embeds the three strategic agendas of the Midterm Review of Strategy 2020 into all AsDB operations: (i) inclusive economic growth; (ii) environmentally sustainable growth; and (iii) regional cooperation and integration (RCI).

The 2014–18 CPS builds on two strategic pillars for AsDB's activities in Cambodia: (i) rural-urban-regional links, and (ii) human and social development, and one facilitating pillar: PSM. Expanding rural-urban-regional links is an integrated approach to developing those areas where most poor people live and focuses on transport and economic corridor development to link national value chains with the region and the world. This pillar develops rural-urban-regional infrastructure (including irrigation and water management, rural electrification, rural roads, rural water supply, urban infrastructure, road maintenance, and trade facilitation) and supports the commercialization of farms and competitiveness of agribusiness through improved connectivity. The second pillar, targeted human and social development, supports access to, and the quality of, secondary education, and targeted skills development through technical and vocational education and training linked to evolving demands of the labor market. PSM covers decentralization and deconcentration

[1] Following the combination of ADF lending operations with the ordinary capital resources balance sheet on January 1, 2017, concessional ordinary capital resources lending (COL) has replaced ADF lending. The modalities and conditions for ADF and COL loans are the same.

and public financial management reforms and acts as facilitating pillar to improve country and sector governance and mitigate project-level fiduciary risks.

AsDB has been a leading development partner of the finance sector in Cambodia since 1999. A comprehensive approach was required to rebuild the financial system in a devastated economy that had no finance sector. The Third Financial Sector Program (FSP) (2011–2014) supported implementation of recommendations of the 2010 Financial Sector Assessment Program (FSAP) and initial stages of the government's Financial Sector Development Strategy (FSDS), 2011–2020. After successfully rebuilding the basic foundation of the banking industry under the First and Second FSP, the Third FSP supported the sector's expansion to cover the important subsectors of nonbanking services and capital markets, and to boost investor's and beneficiaries' confidence in the system with a stronger legal and regulatory framework, necessary infrastructure, and better quality of services, including consumer protection. The Inclusive Financial Sector Development Program (2016-2021) consists of three subprograms as part of implementation of the FSDP 2016–2025, which has been prepared with technical assistance by AsDB, and is supporting a growing, resilient, inclusive, and efficient financial system with expanded coverage. First, the program is supporting the completion of a draft national strategy for financial inclusion for rural areas, agriculture, and SME development. The program is also enhancing financial stability and confidence, which represents a key prerequisite for financial inclusion. Finally, the program is supporting finalization of draft laws and lay the foundation for strengthening financial system infrastructure.

Under the CPS 2014–2018, AsDB's private sector operations focus on finance sector development, including private equity, transport, agribusiness, water supply and sanitation, and trade and supply chain finance for SMEs, while targeting synergies with AsDB's public sector assistance.

AsDB has assisted the government to review existing policies, laws, regulations, and institutional arrangements for Public Private Partnerships (PPPs) and supported development of the Policy Paper on PPPs For Public Investment Project Management. Under a capacity development technical assistance project, AsDB is currently helping to build the institutional capacity of government agencies which will be involved in developing future PPPs. Through a project preparatory technical assistance, AsDB has in early 2016 started to support the government in establishing a legal and institutional framework for development of PPPs, and will help to develop a pathfinder PPP project pipeline and pilot project.

Asian Development Bank: Loans/Grants Commitments and Disbursements to Cambodia, 1992–2017

(In millions of U.S. dollars, as of June 30, 2017)

No.	Year	Loan/Grant Approvals [1]	Contract Awards/ Commitment	Disbursements
1	1992	69.4	0.0	0.0
2	1993	0.0	4.4	5.4
3	1994	28.2	35.9	12.2
4	1995	45.1	28.1	35.9
5	1996	105.0	15.3	32.1
6	1997	0.0	41.5	10.7
7	1998	40.0	29.1	29.3
8	1999	88.0	17.0	26.2
9	2000	109.6	114.4	50.8
10	2001	75.2	40.7	48.3
11	2002	116.5	64.4	78.9
12	2003	98.3	61.9	73.3
13	2004	65.0	62.4	76.7
14	2005	52.0	96.4	84.5
15	2006	69.8	44.3	55.1
16	2007	72.1	82.5	70.1
17	2008	84.1	140.7	137.7
18	2009	144.5	59.8	82.7
19	2010	160.8	64.3	71.4
20	2011	70.0	128.6	122.3
21	2012	275.5	79.5	60.5
22	2013	148.0	149.7	238.6
23	2014	226.0	104.0	98.7
24	2015	130.0	129.5	114.7
25	2016	198.6	143.2	147.5
26	2017	0.0	194.7	99.8
	TOTAL:	**2,471.0**	**1,932.1**	**1,863.3**

Source: Asian Development Bank as of June 30, 2017.

[1] Approvals include OCR Loans, ADF Loans, and Grants only.

STATISTICAL ISSUES

(July 2017)

I. Assessment of Data Adequacy for Surveillance
General. Data provision is broadly adequate for surveillance. Extensive technical assistance (TA) has been provided by the IMF, United Nations Development Programme, Asian Development Bank (ADB), and World Bank, as well as by bilateral partners, leading to substantial capacity improvements. Despite the progress made in improving data statistics, several shortcomings in macroeconomic data still hamper timely and comprehensive analysis.
National accounts. Despite improvements in recent years, weaknesses remain in the quality and timeliness of national accounts data. The quality of GDP estimates remains hampered by the lack of comprehensive and reliable source data on a production and expenditure basis, in part due to resource constraints and weak data collection techniques. In November 2011, a TA mission assessed current methodologies used to compile national accounts estimates and provided support with the development of the quarterly national accounts estimates. In February 2014, another TA mission was conducted mainly to assist the National Institute of Statistics (NIS) processing the results of Cambodia's first ever 2011 Economic Census of Cambodia (EC2011) for improving GDP estimates. The purpose of the EC2011 was not particularly focused on national accounts, hence TA concluded further improvements are needed to convert EC2011 data into national accounts data following the System of National Accounts (SNA) concepts and definitions. The TA mission also assessed the implementation of the previous mission recommendations and found that progress has stalled partly due to resource constraints. Statistics Sweden has been assisting the NIS for improving the national accounts compilation. In February 2015, a TA mission assessed current data compilation and dissemination practices and made recommendations on these issues.
Price statistics. The compilation of the consumer price index (CPI) suffers from insufficient geographic coverage. An updated CPI series was introduced starting in April 2012. Geographic coverage of the series has been expanded to include Phnom Penh plus five provinces. An STA TA mission visited Phnom Penh in April 2012 to assist with updating/improving the CPI. The authorities indicated a need for assistance with developing a producer price index (PPI), but no funds have been allocated to support the compilation of an ongoing PPI.
Government finance statistics (GFS). The Ministry of Economy and Finance began implementing reforms to the government accounting system and budgetary nomenclature in 2007, based on the Government Finance Statistics Manual (GFSM) 2001, with the assistance of the IMF. To facilitate policy dialog, the authorities should consider shifting from the Tableau des opérations financières de l'État (TOFE) based on GFSM 1986 to a GFSM 2014-based budget formulation and reporting framework. Over the past three years, progress has been made, and the authorities submit annual and monthly GFSM 1986 and 2001 data for central government budgetary operations and GFSM 1986 for local government budgetary operations, both on a cash basis to

the IMF's Statistics Department. Going forward, the priority is to improve data compilation, namely to compile financial balance sheet, and extend institutional coverage to include data for extrabudgetary entities and social security funds. Next steps include: (i) improving the CoA to allow automatic compilation of GFSM 2014 summary statements and detailed tables in the FMIS; (ii) mapping available source data on PAE to GFSM 2014 classifications; and (iii) reporting to the World Bank-IMF Public Sector Debt Statistics database. A mission on GFS conducted in late February 2017 provided recommendations and guidelines to further improve GFS statistics. A follow up mission is planned for mid-2018.	
Monetary and financial statistics. The NBC reports monetary data using the standardized report forms for the central bank and other depository corporations on a regular monthly basis. The NBC received TA during the FSAP on the compilation of financial soundness indicators (FSIs). In September 2015, another TA mission provided support for establishing procedures for compiling FSIs. The NBC now compiles monthly core FSIs and several encouraged FSIs, and has begun reporting them to the IMF on a regular basis since February 2016. Some data deficiencies and inconsistencies continue to pose a challenge to the compilation of FSIs, including deficiencies on sectoral classification. A TA mission on monetary and financial statistic (MFS) visited Phnom Penh in April 2017 to strengthen quality of MFS by ensuring that data procedures follow recommendations of Monetary and Financial Statistic Manual and Compilation Guide (MFSMCG) and enhancing coverage to other financial corporations (OFC) such as insurance companies and specialized banks.	
External sector statistics. Cambodia's quarterly balance of payments and international investment position (IIP) are compiled by the NBC according to the Balance of Payments Manual, fifth edition (BPM5). Data present some relevant shortcomings in terms of coverage, accuracy, and timeliness. Balance of payments and IIP are compiled relying on estimation methods. Inward foreign direct investment (FDI), a relevant component of Cambodia's external transactions and positions present large gaps despite recent survey improvements. General Department of Customs and Excise (GDCE) produce monthly and quarterly trade data. Monthly data are regularly provided to NBC to be used to estimate balance of payments trade figures. A number of technical assistances has been provided under the Project on Improvement of External Sector Statistics, funded by the government of Japan. Recent progress has been made, especially in enhancing the International Transactions Reporting System (ITRS) and in conducting a FDI survey. In September 2016, a TA mission on FDI data collection has been conducted to assess legal framework for FDI data collection and to provide guidance on determining survey population and sample survey frame.	
II. Data Standards and Quality	
Cambodia participates in the IMF's General Data Dissemination System.	No data ROSC are available.

Cambodia: Table of Common Indicators Required for Surveillance

(As of July 2017)

	Date of Latest Observation	Date Received	Frequency of Data[1]	Frequency of Reporting[1]	Frequency of Publication[1]
Exchange Rates	7/30/2017	7/31/2017	D	D	W
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[2]	6/2017	7/2017	M	M, 1 month lag	M
Reserve/Base Money	6/2017	7/2017	M	M, 1 month lag	M
Broad Money	6/2017	7/2017	M	M, 1 month lag	M
Central Bank Balance Sheet	6/2017	7/2017	M	M, 1 month lag	M
Consolidated Balance Sheet of the Banking System	6/2017	7/2017	M	M, 1 month lag	M
Interest Rates[3] (Loan and Deposit rates)	6/2017	7/2017	M	M, 1 month lag	M
Consumer Price Index	5/2017	7/2017	M	M, 1-2 month lag	M
Revenue, Expenditure, Balance and Composition of Financing[4]—General Government[5]	6/2017	7/2017	M	M, 4-6 week lag	M
Revenue, Expenditure, Balance and Composition of Financing[4]—Central Government	6/2017	7/2017	M	M, 4-6 week lag	M
Stocks of Central Government and Central Government-Guaranteed Debt[6]	6/2017	7/2017	M	M, 1-2 month lag	A
External Current Account Balance	3/2017	7/2017	Q	Q, 3-5 month lag	Q
Exports and Imports of Goods and Services	6/2017	7/2017	M	M, 1 month lag	M
GDP/GNP	2016	7/2017	A	A, 6 month lag	A
Gross External Debt	2016	7/2017	A	A, 6 month lag	A
International Investment Position	N/A	N/A	N/A	N/A	N/A

[1] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A), Irregular (I), and Not Available (N/A).
[2] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[3] Deposit and loan rates.
[4] Foreign, domestic bank, and domestic nonbank financing.
[5] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[6] Including currency and maturity composition.

MAIN WEBSITES OF DATA

National Bank of Cambodia (www.nbc.org.kh)

Exchange rates
Balance of payments

Ministry of Economy and Finance (www.mef.gov.kh)

Government budget
Fiscal revenue, expenditure, and financing

National Institute of Statistics (www.nis.gov.kh)

Consumer Price Index
National accounts
Population census
Labor force survey
Socioeconomic survey
Household survey

INTERNATIONAL MONETARY FUND

CAMBODIA

STAFF REPORT FOR THE 2017 ARTICLE IV CONSULTATION—DEBT SUSTAINABILITY ANALYSIS

August 30, 2017

Approved By
Markus Rodlauer and Yan Sun (IMF), and Lalita Moorty (IDA)

Prepared by Staff of the International Monetary Fund and the International Development Association.[1]

This Debt Sustainability Analysis (DSA) shows that Cambodia remains at low risk of external debt distress, with all debt burden indicators projected to remain below respective indicative thresholds.[2] However, the results also indicate that debt sustainability is becoming increasingly vulnerable to adverse macroeconomic shocks, including a fall in exports and a disorderly adjustment in the exchange rate, fiscal revenue shocks, and the materialization of contingent liabilities. Although the present value (PV) of debt-to-GDP threshold is breached under two stress tests, staff continues to assess Cambodia's external risk as low given the unique features of its economy. Specifically, a large exchange rate shock and export shock both lead to a breach of the external debt to GDP threshold. However, the exchange rate shock is unlikely to be a significant risk to debt sustainability given the country's high degree of dollarization. Furthermore, accounting for the structural break in exports growth in 2011 confirms the low external debt risk rating. Overall, the findings suggest increasing risks to Cambodia's debt outlook and reinforce the need for continued reforms to increase the economy's resilience to shocks, and further efforts to mobilize fiscal revenues.

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[1] Prepared in consultation with the Cambodian authorities.

[2] Cambodia Country Policy and Institutional Assessment (CPIA) rating averaged 3.4 over 2014–2016 and the country is classified as having medium policy performance.

1. **Cambodia is at a low risk of debt distress.** The indicative debt distress thresholds remain unchanged from the 2016 Article IV DSA. Under the baseline scenario, the external and the public debt burden indicators never breach the policy-dependent indicative thresholds, and the present value (PV) of external debt follows a downward trend over the medium term. Downside risks to the baseline scenario include external arrears, macroeconomic shocks, such as a fall in exports and a disorderly adjustment in the exchange rate, and the materialization of contingent liabilities. The macroeconomic assumptions underlying the baseline scenario remain analogous to the 2016 DSA. Cambodia's Country Policy and Institutional Assessment (CPIA) rating remains unchanged at the level of a "medium performer."

CAMBODIA'S PUBLIC DEBT

2. **Cambodia's stock of external public debt, including arrears, stood at around US$6.45 billion or about 32 percent of GDP (26 percent of GDP in PV terms) as of end-2016.** The increase in external debt since the global financial crisis has been driven largely by disbursement of bilateral loans, particularly from China. The corresponding PV of external debt was 25.4 percent of GDP at end-2016.

Cambodia: External Public Debt

	U.S. dollar (U.S. millions)	Share of total External Debt	In percent of GDP
Total	6,457	100	31.9
Multilateral	2,088	35.9	10.3
Bilateral	4,369	64.1	21.7

Sources: Cambodia authorities; and World Bank estimates.

3. **Bilateral debt has been increasing since 2009, while the share of multilateral debt has continued to decline.** China remains the largest bilateral creditor, contributing to around 70 percent of the total bilateral debt stock, including arrears to the Russian Federation and the United States, as of end-2016. Cambodia remains in arrears to the Russian Federation and the United States (nearly 10 percent of total debt and about 3 percent of GDP), and the status of negotiations of these arrears has remained unchanged since the last DSA.[3] Cambodia is not servicing its debt with these two creditors and further efforts are needed to conclude agreements under the Paris Club framework. Since prospects for resolution remain unclear, this DSA continues to assume no debt restructuring.

4. **Public domestic debt remains negligible.** There is a small amount of bonds (US$3.2 million) issued in the early 2000s and some old claims on the government (the total equal to half percent of GDP, with no interest) that were carried over from the 1990s and remain to be recorded in the monetary survey.

[3] Based on Cambodia Public Debt Statistical Bulletin (see Table 13 "Old Debt Under Negotiation"). Data reflects principal amounts, i.e. excluding any accumulated interest.

5. The authorities have made considerable progress in monitoring contingent liabilities from PPPs through strengthening the institutional framework. In line with past Fund recommendations, reinforced by contingent liability management technical assistance provided by the Bank, the authorities adopted an annual ceiling at 4 percent of GDP on guaranteed payments for PPPs. With expected diminished access to concessional finance in the coming years (owing to the attainment of lower middle income status), and slow progress in developing domestic debt markets, the authorities have established a road map to have a full set of PPP mechanisms, including the necessary legal framework, in place by 2020. Although PPPs can increase efficiency and increase value for money relative to the public financing of investment, their fiscal implications can be sometimes hard to monitor and control. To enhance fiscal transparency, the authorities should list all contingent liabilities in the annual budget law.

MACROECONOMIC FRAMEWORK

6. The macroeconomic framework underlying the baseline scenario remains broadly in line with the previous DSA.

- **Growth and inflation**: Economic activity remains strong driven by robust exports, real estate, and construction. GDP growth is expected at around 7.0 percent in 2017 and is projected to slow to around 6.0 percent over the medium term (by 2022), assuming some product diversification and supportive policies. Inflation (CPI average) rose temporarily to 3.9 percent at end-2016 reflecting higher food and fuel prices, but is expected to decline over the medium-term.

- **External sector stability**: The current account deficit narrowed to 8.8 percent of GDP in 2016 from 9.3 percent in the preceding year. On the back of the lower current account deficit and strong FDI inflows, foreign reserves continued to grow, reaching $7.9 billion in June 2017, about 5.5 months of next year's imports. The current account deficit is projected to remain broadly stable in 2017 and over the medium-term. The trade balance is expected to improve with some product diversification amid ASEAN Economic Community integration, and a pickup in remittances is expected to compensate for some of the decline in official assistance. Gross official reserves are projected to rise to close to 6 months of prospective imports by 2022. Based on authorities' projections external bilateral debt disbursements are projected to average about US$1.16 billion annually during 2017–22 (about 6 percent of GDP on average), resulting in an external debt-to-GDP ratio of about 35.5 percent by 2022, after which the debt ratio is projected to decline.

- **Fiscal sustainability**: Revenue performance, supported by the implementation of the Revenue Mobilization Strategy (RMS), saw tax revenues rise to 15.3 percent of GDP in 2016 from 14.6 in 2015. However, the fiscal deficit widened to 2.8 percent of GDP in 2016 (but remained well below the budget target) due to high public sector wages and increased social spending. The level of government deposits (as a share of GDP) rose to 10.1 percent of GDP by end-2016. The fiscal deficit is projected to widen to about 3.7 percent of GDP in 2017 due a rising public sector wage bill, higher capital and social spending, which will more than offset expected gains from tax revenue mobilization. Over the medium-term, fiscal pressures are expected to emerge due to wage pressures even though some improvement in revenue performance is projected to continue as the tax administration measures contained in the RMS generate revenue gains. Medium-term fiscal policy should be anchored to safeguarding government deposits and long-term fiscal debt sustainability, while striking a balance between providing resources for Cambodia's vast development needs and rising wage and social spending pressures.

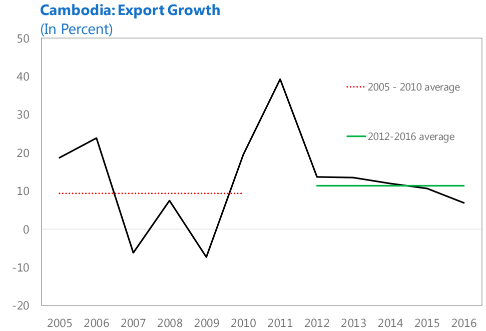
- **Domestic debt**: As Cambodia's financial sector continues to develop, it is expected that the government will start issuing domestic government bonds to provide additional fiscal financing. By issuing debt starting from ¼ ppt of GDP annually in 2022 and gradually increasing to about ½ ppt of GDP in 2035, the total stock of domestic debt would reach about 3.7 percent of GDP by 2035. This remains low compared to the average domestic debt in low-income countries (LICs) of about 15 percent of GDP. However, this conservative estimate is in line with the authorities' intention of not issuing domestic debt over the medium term and to focus more on mobilizing domestic revenue and raising government deposits (i.e., saving, not borrowing).

EXTERNAL AND PUBLIC SUSTAINABILITY

7. Under the baseline scenario, the external DSA shows that Cambodia's risk of debt distress is low. The PV of key ratios never breach their respective policy-dependent indicative thresholds and are projected to decline over the projection period. Moreover, the debt service-to-exports and debt service-to-revenue ratios remain well below the thresholds throughout the projection period, partly due to the concessional nature of most debt.

8. Standard stress tests highlight potential adverse impact from large shocks to the exchange rate or exports. A decline in export growth remains an important risk to debt sustainability. As shown in Table 2, this shock would bring the PV of debt-to-GDP to 43 percent in 2019–20 and 42 percent in 2021–22 (above the indicative threshold of 40 percent), declining to 25 percent in the long-term. However, this mechanical breach of the threshold is strongly influenced by a single outlier observation. Specifically, Cambodian exports grew by 40 percent in 2011 (well above average export growth, see text chart on export growth), reflecting improvements in preferential access to the European Union market resulting in a positive structural change.[4] As shown in Figure 1, a large one-off depreciation would bring the PV of debt-to-GDP to about 40 percent in 2022 (the level of the indicative threshold) and, following a protracted breach of the threshold subsequently

Cambodia: Export Growth
(In Percent)



Source: Cambodian authorities.

[4] Excluding the 2011 outlier year from the calculation of the export shock would imply a PV of debt-to-GDP that remains slightly below the threshold. Furthermore, applying the probability approach confirms the low rating in this case. The improvement in access to the European Union market reflected more favorable rules of origin for manufactured goods and new preferential access to milled rice (a key agricultural export product) (see WTO, (2011): *Cambodia Trade Policy Review*).

declining to 32 percent in the long-term. However, risks related to a disorderly adjustment in the exchange rate are mitigated by the high degree of dollarization (more than 90 percent of banking sector assets and most transactions are in dollars) which is expected to mitigate the impact of a depreciation on the debt to GDP ratio. Revenues accruing to the government principally in US dollars and significant buffers in the form of US dollar denominated government deposits and international reserves provide further protection against abrupt changes in the exchange rate. Finally, the authorities are committed to a closely managed exchange rate regime, as evidenced in the historically stable bilateral exchange rate. While these factors play a mitigating role and PV of external debt declines over the projection period, the deteriorating debt dynamics since the last DSA suggest the need for continuous monitoring, especially as Cambodia over time moves to greater use of its local currency.

9. Public debt is vulnerable to a large exchange rate depreciation shock and to weak revenue growth. Under a one-off real depreciation shock, the PV of total public debt-to-GDP would reach 37 percent in 2022, and then decline over time reaching 30 percent of GDP in the long-term. If the primary balance were to remain unchanged at the 2016 level, the PV of public debt-to-GDP would increase to about 32 percent by 2025, with debt projected to modestly decline over the long-term. While public debt is projected to decline over the medium-term in the baseline and extreme shock scenarios, and do not present any major vulnerability at present, the analysis implies that efforts to mobilize revenues to guarantee long-term debt sustainability should continue.

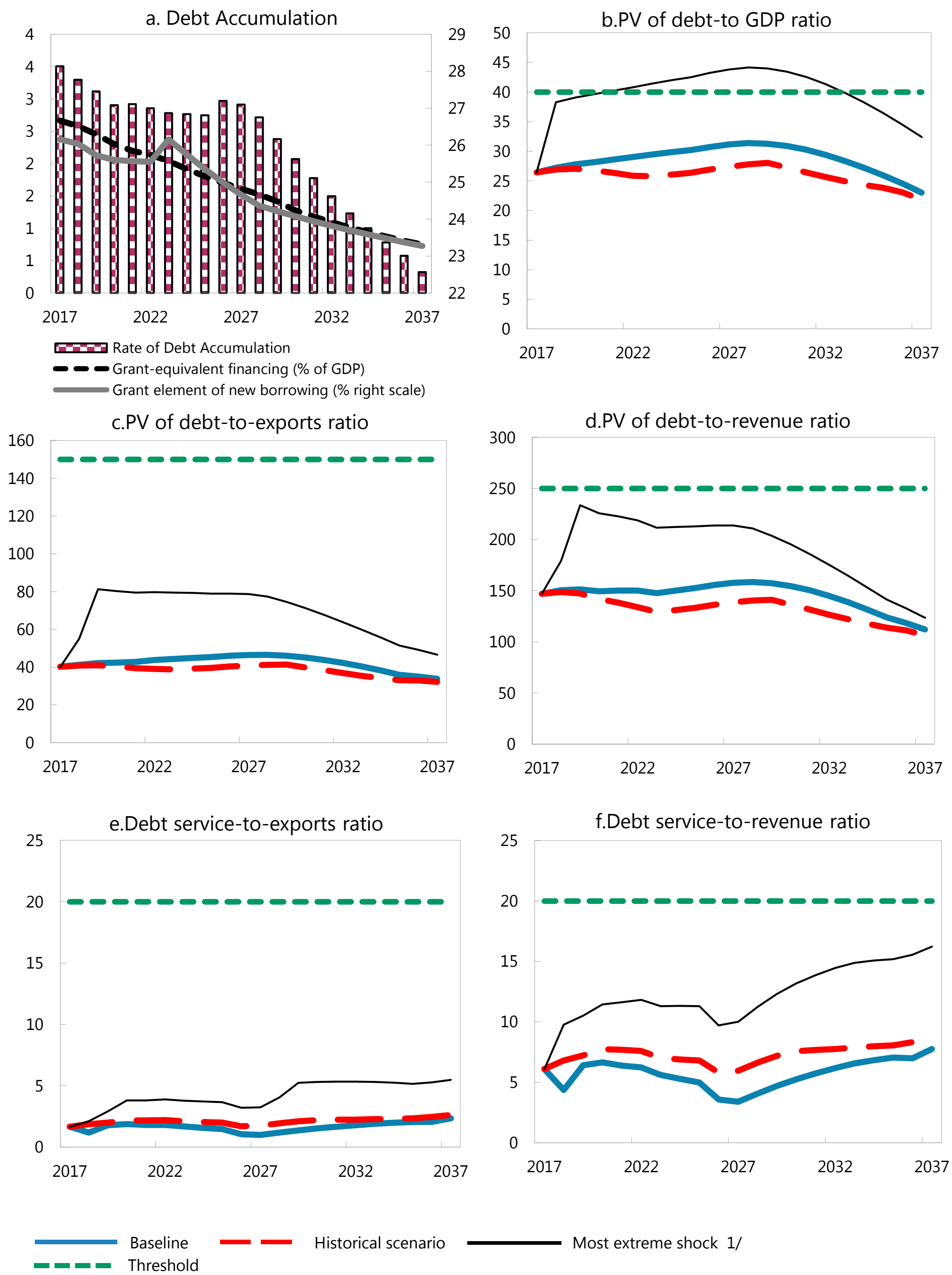
10. Public debt sustainability is at risk from a rise in contingent liabilities related to PPPs and potential financial stress. PPP investments in power generation and distribution projects are large, and in case of adverse scenarios, associated fiscal risks could arise and potentially add substantial liabilities to the debt stock. Other potential contingent liabilities include the fiscal costs to support the financial sector during a banking crisis.

11. The authorities broadly agree with the findings of the DSA exercise. The debt management unit at the Ministry of Economy and Finance (MEF) conducts its own internal DSA analysis, and has reached the same conclusion of low risk of debt distress. They use the results of these analyses to propose annual ceilings of new net debt disbursements. The authorities assume a similar loan disbursement profile and current account deficits, but are slightly more optimistic than staff on the medium-term real GDP growth assumption. The MEF expressed concern about the accumulation of contingent liabilities from PPPs and have imposed annual ceilings on PPP guarantees.

CONCLUSION

12. Cambodia remains at low risk of debt distress. While the risk of debt distress is currently assessed to be low, the baseline projections and the standard stress tests show increasing risks to external debt outlook. Downside risks to the baseline scenario include the materialization of contingent liabilities and issues arising from external arrears. The most extreme stress tests indicate that Cambodia's debt sustainability remains vulnerable to shocks to the exchange rate, economic growth, exports, and the fiscal position. This reinforces the importance of preserving macroeconomic stability and diversifying the economy and exports to increase resilience to external shocks, improving spending efficiency and the successful implementation of the revenue mobilization strategy.

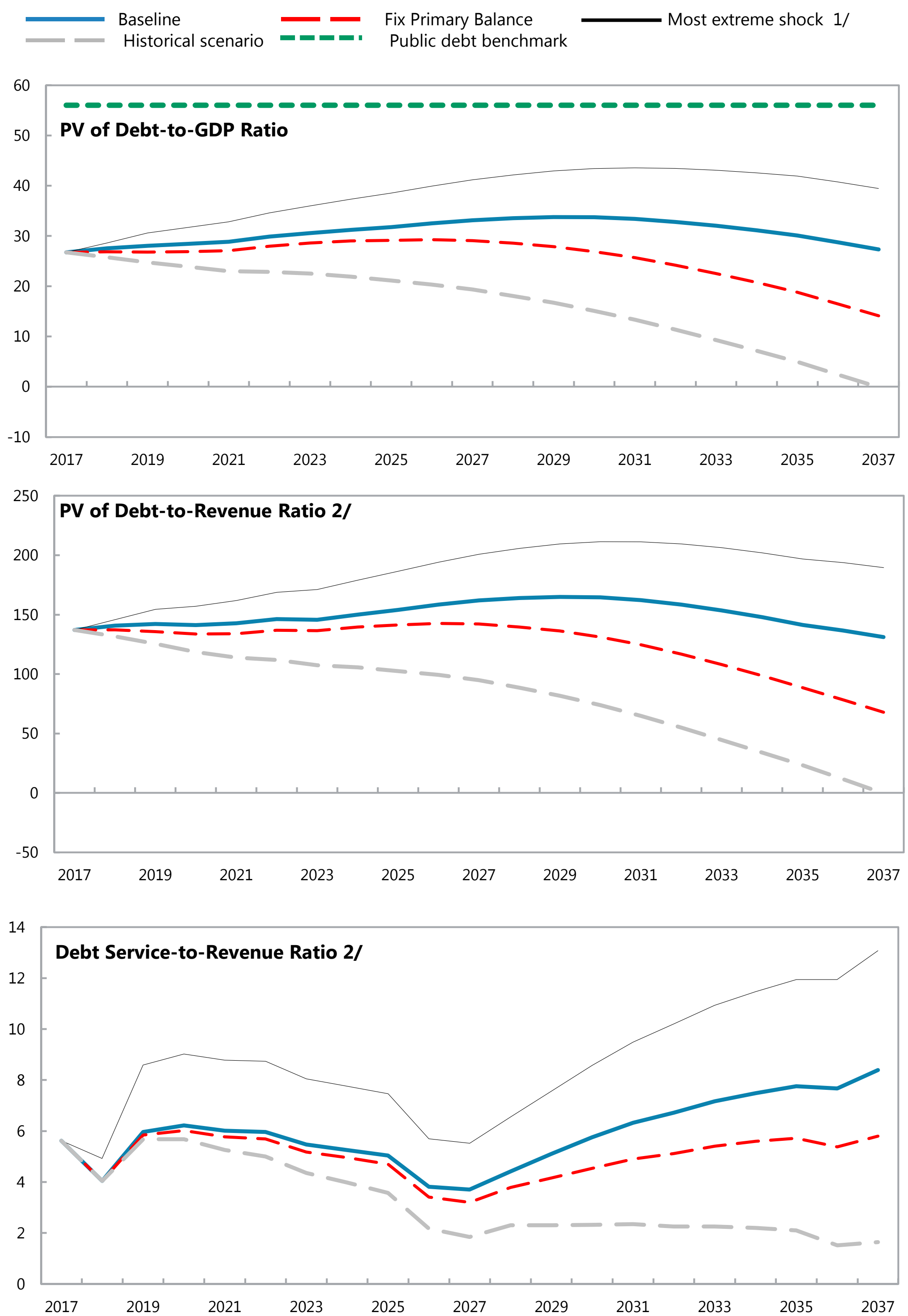
Figure 1a. Cambodia: Indicators of Public and Publicly Guaranteed External Debt under Alternative Scenarios, 2017–2037 1/



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio on or before 2027. In figure b. it corresponds to a One-time depreciation shock; in c. to a Exports shock; in d. to a Exports shock; in e. to a Exports shock and in figure f. to a One-time depreciation shock

Figure 1b. Cambodia: Indicators of Public Debt Under Alternative Scenarios, 2017–2037 1/



Sources: Country authorities; and staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio on or before 2027.
2/ Revenues are defined inclusive of grants.

Table 1. Cambodia: External Debt Sustainability Framework, Baseline Scenario, 2014–¬2037 1/
(In percent of GDP, unless otherwise indicated)

	Actual					Estimate	Projections								
	2014	2015	2016	Average 5/	Standard Deviation 5/	2017	2018	2019	2020	2021	2022	2017-22 Average	2027	2037	2023-37 Average
Public sector debt 1/	32.3	31.2	32.3			33.2	34.3	34.7	35.0	35.4	36.4		39.4	31.9	
of which: foreign-currency denominated	31.8	30.8	31.9			32.8	34.0	34.4	34.8	35.1	35.5		37.5	27.6	
Change in public sector debt	0.2	-1.0	1.0			0.9	1.1	0.4	0.3	0.4	1.0		0.6	-1.7	
Identified debt-creating flows	-1.2	-1.3	-0.3			0.9	1.7	1.5	1.2	1.1	1.1		1.8	2.7	
Primary deficit	0.8	1.2	2.5	1.8	1.7	3.3	4.2	4.1	3.7	3.7	3.6	3.7	4.5	4.9	4.6
Revenue and grants	19.8	18.8	19.8			19.5	19.6	19.7	20.1	20.2	20.4		20.5	20.8	
of which: grants	3.0	2.1	2.0			1.5	1.5	1.4	1.3	1.1	1.1		0.7	0.3	
Primary (noninterest) expenditure	20.6	20.0	22.3			22.8	23.7	23.8	23.8	23.9	24.0		24.9	25.7	
Automatic debt dynamics	-1.9	-2.5	-2.8			-2.3	-2.4	-2.6	-2.5	-2.6	-2.5		-2.7	-2.2	
Contribution from interest rate/growth differential	-2.7	-2.6	-2.2			-2.3	-2.3	-2.4	-2.4	-2.4	-2.4		-2.7	-1.9	
of which: contribution from average real interest rate	-0.6	-0.4	-0.1			-0.2	-0.2	-0.3	-0.3	-0.3	-0.4		-0.5	0.0	
of which: contribution from real GDP growth	-2.1	-2.2	-2.1			-2.1	-2.1	-2.2	-2.1	-2.1	-2.0		-2.2	-1.9	
Contribution from real exchange rate depreciation	0.7	0.0	-0.6			-0.1	-0.1	-0.1	-0.1	-0.1	-0.1		...	...	
Other identified debt-creating flows	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	1.4	0.3	1.4			0.0	-0.6	-1.1	-0.9	-0.8	-0.1		-1.2	-4.4	
Other Sustainability Indicators															
PV of public sector debt	...	...	25.8			26.7	27.5	28.0	28.4	28.8	29.9		33.1	27.3	
of which: foreign-currency denominated	...	...	25.4			26.4	27.2	27.8	28.2	28.6	29.0		31.2	23.0	
of which: external	...	...	25.4			26.4	27.2	27.8	28.2	28.6	29.0		31.2	23.0	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	2.0	2.5	4.0			4.7	5.2	5.5	5.2	5.1	5.0		5.3	6.7	
PV of public sector debt-to-revenue and grants ratio (in percent)	...	...	129.8			137.1	140.7	142.1	141.2	142.7	146.3		161.9	131.2	
PV of public sector debt-to-revenue ratio (in percent)	...	...	144.3			148.9	152.0	152.8	150.7	151.3	154.6		167.8	133.0	
of which: external 3/	...	...	142.3			147.1	150.4	151.3	149.4	150.1	150.3		157.8	112.2	
Debt service-to-revenue and grants ratio (in percent) 4/	4.3	5.0	6.1			5.6	4.0	6.0	6.2	6.0	6.0		3.7	8.4	
Debt service-to-revenue ratio (in percent) 4/	5.1	5.7	6.8			6.1	4.4	6.4	6.6	6.4	6.3		3.8	8.5	
Primary deficit that stabilizes the debt-to-GDP ratio	0.6	2.2	1.5			2.4	3.1	3.6	3.4	3.3	2.6		3.9	6.6	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	7.1	7.2	7.0	6.6	2.5	6.9	6.8	6.8	6.5	6.3	6.0	6.6	6.0	6.0	6.0
Average nominal interest rate on forex debt (in percent)	1.2	1.2	1.2	1.0	0.2	1.4	1.3	1.1	1.0	0.9	0.7	1.1	0.4	0.0	0.3
Average real interest rate on domestic debt (in percent)	-2.3	-1.6	-3.2	-3.3	2.9	-3.0	-3.1	-3.1	-3.1	-3.1	4.4	-1.8	2.5	0.9	1.9
Real exchange rate depreciation (in percent, + indicates depreciation)	2.5	0.1	-2.2	-1.4	3.5	-0.3	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	2.6	1.9	3.6	3.8	3.3	3.4	3.4	3.5	3.4	3.5	3.4	3.4	3.0	3.0	3.0
Growth of real primary spending (deflated by GDP deflator, in percent)	8.6	4.0	19.6	3.3	6.4	9.0	11.3	7.1	6.6	6.6	6.3	7.8	6.8	4.9	6.5
Grant element of new external borrowing (in percent)	...	...	...	...	...	26.2	26.0	25.7	25.6	25.6	25.5	25.8	24.7	23.3	...

Sources: Country authorities; and staff estimates and projections.

1/ [Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also whether net or gross debt is used.]

2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

3/ Revenues excluding grants.

4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 2. Cambodia: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2017–2037

(In percent)

	Projections							
	2017	2018	2019	2020	2021	2022	**2027**	2037
PV of debt-to GDP ratio								
Baseline	26	27	28	28	29	29	**31**	23
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	26	27	27	27	26	26	**27**	22
A2. New public sector loans on less favorable terms in 2017-2037 2	26	28	29	31	32	33	**39**	34
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	26	28	29	29	30	30	**33**	24
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	26	32	43	43	42	42	**42**	25
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	26	28	29	29	30	30	**32**	24
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	26	29	32	32	32	33	**34**	24
B5. Combination of B1-B4 using one-half standard deviation shocks	26	31	38	38	38	38	**39**	25
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	26	38	39	40	40	41	**44**	32
PV of debt-to-exports ratio								
Baseline	40	41	42	42	43	44	**46**	34
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	40	41	41	40	39	39	**41**	32
A2. New public sector loans on less favorable terms in 2017-2037 2	40	42	45	46	48	50	**57**	49
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	40	41	42	42	43	44	**46**	34
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	40	55	81	80	79	80	**79**	47
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	40	41	42	42	43	44	**46**	34
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	40	45	48	48	49	49	**51**	35
B5. Combination of B1-B4 using one-half standard deviation shocks	40	48	61	60	60	61	**61**	39
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	40	41	42	42	43	44	**46**	34
PV of debt-to-revenue ratio								
Baseline	147	150	151	149	150	150	**158**	112
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	147	149	147	142	138	134	**139**	107
A2. New public sector loans on less favorable terms in 2017-2037 2	147	155	160	163	168	172	**196**	164
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	147	153	158	156	157	157	**165**	117
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	147	179	234	226	223	219	**214**	124
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	147	153	157	155	156	156	**164**	116
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	147	163	174	171	170	169	**173**	115
B5. Combination of B1-B4 using one-half standard deviation shocks	147	171	205	199	198	196	**196**	122
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	147	212	213	210	211	211	**222**	158

Table 2. Cambodia: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2017–2037 (Concluded)

(In percent)

	Projections							
	2017	2018	2019	2020	2021	2022	**2027**	2037
PV of debt-to GDP ratio								
Debt service-to-exports ratio								
Baseline	2	1	2	2	2	2	**1**	2
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	2	2	2	2	2	2	**2**	3
A2. New public sector loans on less favorable terms in 2017-2037 2	2	2	2	2	2	3	**3**	5
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	2	2	2	2	2	2	**2**	3
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	2	2	3	4	4	4	**3**	5
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	2	2	2	2	2	2	**2**	3
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	2	2	2	3	3	3	**2**	4
B5. Combination of B1-B4 using one-half standard deviation shocks	2	2	2	3	3	3	**3**	4
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	2	2	2	2	2	2	**2**	3
Debt service-to-revenue ratio								
Baseline	6	4	6	7	6	6	**3**	8
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2017-2037 1/	6	7	7	8	8	8	**6**	9
A2. New public sector loans on less favorable terms in 2017-2037 2	6	7	7	8	9	9	**10**	16
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2018-2019	6	7	8	9	9	9	**7**	12
B2. Export value growth at historical average minus one standard deviation in 2018-2019 3/	6	7	8	11	11	11	**9**	15
B3. US dollar GDP deflator at historical average minus one standard deviation in 2018-2019	6	7	8	8	9	9	**7**	12
B4. Net non-debt creating flows at historical average minus one standard deviation in 2018-2019 4/	6	7	8	9	9	9	**8**	12
B5. Combination of B1-B4 using one-half standard deviation shocks	6	7	8	10	10	10	**8**	14
B6. One-time 30 percent nominal depreciation relative to the baseline in 2018 5/	6	10	10	11	12	12	**10**	16
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	23	23	23	23	23	23	**23**	23

Sources: Country authorities; and staff estimates and projections.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.
3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly a
an offsetting adjustment in import levels).
4/ Includes official and private transfers and FDI.
5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.
6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Table 3. Cambodia: Public Sector Debt Sustainability Framework, Baseline Scenario, 2014–2037

(In percent of GDP unless otherwise indicated)

	Actual					Estimate	Projections								
	2014	2015	2016	Average 5/	Standard Deviation 5/	2017	2018	2019	2020	2021	2022	2017-22 Average	2027	2037	2023-37 Average
Public sector debt 1/	32.3	31.2	32.3			33.2	34.3	34.7	35.0	35.4	36.4		39.4	31.9	
of which: foreign-currency denominated	31.8	30.8	31.9			32.8	34.0	34.4	34.8	35.1	35.5		37.5	27.6	
Change in public sector debt	0.2	-1.0	1.0			0.9	1.1	0.4	0.3	0.4	1.0		0.6	-1.7	
Identified debt-creating flows	-1.2	-1.3	-0.3			0.9	1.7	1.5	1.2	1.1	1.1		1.8	2.7	
Primary deficit	0.8	1.2	2.5	1.8	1.7	3.3	4.2	4.1	3.7	3.7	3.6	3.7	4.5	4.9	4.6
Revenue and grants	19.8	18.8	19.8			19.5	19.6	19.7	20.1	20.2	20.4		20.5	20.8	
of which: grants	3.0	2.1	2.0			1.5	1.5	1.4	1.3	1.1	1.1		0.7	0.3	
Primary (noninterest) expenditure	20.6	20.0	22.3			22.8	23.7	23.8	23.8	23.9	24.0		24.9	25.7	
Automatic debt dynamics	-1.9	-2.5	-2.8			-2.3	-2.4	-2.6	-2.5	-2.6	-2.5		-2.7	-2.2	
Contribution from interest rate/growth differential	-2.7	-2.6	-2.2			-2.3	-2.3	-2.4	-2.4	-2.4	-2.4		-2.7	-1.9	
of which: contribution from average real interest rate	-0.6	-0.4	-0.1			-0.2	-0.2	-0.3	-0.3	-0.3	-0.4		-0.5	0.0	
of which: contribution from real GDP growth	-2.1	-2.2	-2.1			-2.1	-2.1	-2.2	-2.1	-2.1	-2.0		-2.2	-1.9	
Contribution from real exchange rate depreciation	0.7	0.0	-0.6			-0.1	-0.1	-0.1	-0.1	-0.1	-0.1		...	...	
Other identified debt-creating flows	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	1.4	0.3	1.4			0.0	-0.6	-1.1	-0.9	-0.8	-0.1		-1.2	-4.4	
Other Sustainability Indicators															
PV of public sector debt	...	...	25.8			26.7	27.5	28.0	28.4	28.8	29.9		33.1	27.3	
of which: foreign-currency denominated	...	...	25.4			26.4	27.2	27.8	28.2	28.6	29.0		31.2	23.0	
of which: external	...	...	25.4			26.4	27.2	27.8	28.2	28.6	29.0		31.2	23.0	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	2.0	2.5	4.0			4.7	5.2	5.5	5.2	5.1	5.0		5.3	6.7	
PV of public sector debt-to-revenue and grants ratio (in percent)	...	...	129.8			137.1	140.7	142.1	141.2	142.7	146.3		161.9	131.2	
PV of public sector debt-to-revenue ratio (in percent)	...	...	144.3			148.9	152.0	152.8	150.7	151.3	154.6		167.8	133.0	
of which: external 3/	...	...	142.3			147.1	150.4	151.3	149.4	150.1	150.3		157.8	112.2	
Debt service-to-revenue and grants ratio (in percent) 4/	4.3	5.0	6.1			5.6	4.0	6.0	6.2	6.0	6.0		3.7	8.4	
Debt service-to-revenue ratio (in percent) 4/	5.1	5.7	6.8			6.1	4.4	6.4	6.6	6.4	6.3		3.8	8.5	
Primary deficit that stabilizes the debt-to-GDP ratio	0.6	2.2	1.5			2.4	3.1	3.6	3.4	3.3	2.6		3.9	6.6	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	7.1	7.2	7.0	6.6	2.5	6.9	6.8	6.8	6.5	6.3	6.0	6.6	6.0	6.0	6.0
Average nominal interest rate on forex debt (in percent)	1.2	1.2	1.2	1.0	0.2	1.4	1.3	1.1	1.0	0.9	0.7	1.1	0.4	0.0	0.3
Average real interest rate on domestic debt (in percent)	-2.3	-1.6	-3.2	-3.3	2.9	-3.0	-3.1	-3.1	-3.1	-3.1	4.4	-1.8	2.5	0.9	1.9
Real exchange rate depreciation (in percent, + indicates depreciation)	2.5	0.1	-2.2	-1.4	3.5	-0.3	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	2.6	1.9	3.6	3.8	3.3	3.4	3.4	3.5	3.4	3.5	3.4	3.4	3.0	3.0	3.0
Growth of real primary spending (deflated by GDP deflator, in percent)	8.6	4.0	19.6	3.3	6.4	9.0	11.3	7.1	6.6	6.6	6.3	7.8	6.8	4.9	6.5
Grant element of new external borrowing (in percent)	...	...	...	...	...	26.2	26.0	25.7	25.6	25.6	25.5	25.8	24.7	23.3	...

Sources: Country authorities; and staff estimates and projections.

1/ [Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also whether net or gross debt is used.]

2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

3/ Revenues excluding grants.

4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Statement by Juda Agung, Executive Director for Cambodia, Edna C. Villa, Alternate Executive Director, and Kaweevudh Sumawong, Senior Advisor to the Executive Director
September 22, 2017

1. The Cambodian authorities would like to express their sincere appreciation to the IMF mission team for the constructive and candid policy discussions, which centered on policies towards strong, inclusive and sustainable growth. The authorities welcome staff' acknowledgement of Cambodia's robust economic growth and broadly share staff's view on near-term risks and medium-term challenges. They are also in broad agreement with staff's recommendations and will take these into consideration when formulating future policies.

Recent Developments and Outlook

2. The Cambodian economy continues to perform well with 7 percent growth in 2016. Indeed, Cambodia has registered an annual average growth of more than 7 percent over the past 20 years and is regarded as one of the world's fastest growing economies. More importantly, this growth momentum is expected to remain robust on the back of strong exports and services, as well as real estate and construction activities. The economy is expected to continue to grow around 7 percent in 2017 and 2018.

3. Notwithstanding the recent pickup in headline inflation, the authorities expect headline inflation to decline to around 3 percent in 2018 due to a slowdown in food price increases, owing partly to the authorities' efforts to improve agricultural productivity and market access, and a deceleration in oil price increases. Credit growth has moderated to around 15 percent in the first half of 2017, following the introduction of policy measures, and is projected to continue to slow to 13 percent in 2018 from an average of 30 percent over the past five years. The authorities are mindful of the impact of these measures on growth and will continue to assess their impact before introducing further measures. The external position has also continued to improve with the current account deficit expected to narrow further to 8.3 percent of GDP in 2017. While gross official reserves continue to increase and cover almost 6 months' worth of imports of goods and services at end-June 2017, the authorities see merit in staff's recommendation to further build up the reserves buffer.

4. Despite the overall outlook remaining positive, the Cambodian economy still faces downside risks, particularly on the external front. The authorities share the view of staff that a growth slowdown in advanced economies, appreciation of the US dollar, or rise in protectionism could have an adverse impact on the Cambodian economy. Against this background, the authorities remain vigilant and are committed to undertaking measures and reforms to maintain economic and financial stability while ensuring sustainable growth.

Financial Policy

5. The authorities welcome staff's acknowledgement of sustained financial deepening, which has been a result of strong credit growth over the past years. While the banking sector has

been profitable, with adequate capital buffers and provisions, as reflected by the core financial soundness indicators, the authorities are mindful of a potential pocket of vulnerability arising from high credit growth and the concentration of loans associated with the real estate and construction sectors. As such, the Real Estate Data Collection and Coordination Working Group was established in January 2017 to collect and analyze data as well as monitor potential risks in the real estate sector in order to formulate well-targeted preemptive measures. The National Bank of Cambodia (NBC) has also introduced several policy measures to enhance the resilience of the financial system and rein in credit growth, including the phased implementation of the liquidity coverage ratio and bank-specific prudential measures such as higher minimum capital requirements for riskier and more systemically important banks. While these measures have helped bring down credit growth, the authorities will continue to closely monitor developments and remain committed to implementing prudent policies to stabilize credit growth and maintain a strong financial system.

6. The authorities agree with staff that Microfinancial Institutions (MFIs) have played an important role in financial inclusion in Cambodia and some deposit-taking MFIs (MDIs) are becoming more systemically important. The authorities have introduced an interest rate cap on lending by MFIs, MDIs and Rural Credit Operators to improve credit culture and operational efficiency of these financial institutions while protecting customers from excessive interest rate charged by institutions. More importantly, the authorities continue to step up efforts to enhance the supervision framework for banks and financial institutions. The authorities remain committed to a risk-based approach that is consistent with the FSAP recommendations. The NBC is in the process of strengthening regulations including the liquidity risk management framework, capital buffer and external audit requirements for banks and financial institutions. The authorities recognize the important role of the Fund in helping the Cambodian authorities strengthen financial system resilience, and look forward to continued close collaboration to further improve data collection and enhance the crisis resolution framework for the financial sector, in particular, the establishment of the financial stability committee.

Monetary Policy

7. The authorities concur with staff that a stable exchange rate against the US dollar remains appropriate, given high dollarization, as this continues to serve as an important nominal anchor. The authorities are aware that a high degree of dollarization limits the NBC's ability to implement monetary policy effectively. The authorities are therefore fully committed to developing the interbank and money markets as well as foreign exchange markets to promote greater use of the local currency (Khmer Riel) in order to allow for a more effective and flexible monetary framework. In this regard, the National Policy, which will serve as a comprehensive roadmap to promote the greater use of the Riel, has been developed and is being reviewed by the Economic and Financial Policy Committee before submission to the Cabinet for approval.

8. Meanwhile, the authorities have undertaken a number of important steps to promote the use of the Riel. The NBC established in October 2016 the Liquidity-Providing Collateralized Operation (LPCO) to provide Riel liquidity to banks and financial institutions against

negotiable certificate of deposits (NCDs). LPCOs have been issued on a regular basis to help facilitate banks' liquidity management and market-based monetary policy operations. In addition, the NBC implemented in December 2016, a measure requiring banks and financial institutions to lend at least 10 percent in Riel. This has resulted in an increase in lending in Riel by banks and financial institutions.

9. The authorities agree that the reserve requirement is an important instrument of monetary and prudential policy. While the authorities have already re-imposed the reserve requirement on banks' foreign borrowing in 2015, in line with the Fund's past recommendation, they believe that staff's recommendation to increase the reserve requirement on foreign exchange liabilities should be undertaken on a gradual and well-sequenced basis, given other regulations in the pipeline.

Fiscal Policy

10. The authorities underscore the important role of fiscal policy in promoting economic growth and development as well as in ensuring the success of their reform agenda. Tax revenue is projected to continue to perform well as a result of the Revenue Mobilization Strategy (RMS), and exceed the Budget Law for fiscal year 2017. Nevertheless, the fiscal deficit is expected to widen due to higher capital spending and increases in public sector wages, as planned.

11. To strengthen fiscal buffers, the authorities are determined to prioritize expenditure and further enhance revenue mobilization. On the expenditure side, the authorities agree on the importance of developing a medium term fiscal framework (MTFF) to improve expenditure allocation efficiency. Education, health and infrastructure will remain expenditure priorities while ensuring social protection. In addition, public sector wage increases will continue to be cautiously implemented and linked with public administration reform progress, in due recognition of its impact on fiscal sustainability and spending priorities. The authorities are in the process of drafting a new public-private partnership (PPP) law with a view to developing a well-designed PPP framework, while a few PPP projects will be implemented on a pilot basis in line with international best practices. On the revenue side, the authorities note the need to rationalize investment incentives and review other tax policies over the medium term and are committed to strengthening the implementation of the RMS. More importantly, the RMS II (2019 – 2023) is being developed to further enhance revenue mobilization and improve efficiency. In this regard, the authorities welcome the Fund's technical assistance to develop the MTFF and the RMS II, which will be crucial to ensure medium term fiscal sustainability.

12. The authorities note positively from the Debt Sustainability Analysis that Cambodia's risk of debt distress remains low. The authorities remain committed to maintaining the debt-to-GDP ratio at a sustainable level over the medium term to ensure debt sustainability in acknowledging that access to concessional loans will diminish given Cambodia's lower middle income status.

Continuing the Reform Agenda

13. The authorities are aware that the Cambodian economy is at an important juncture after sustaining high growth over the last two decades, and requires comprehensive structural reforms to ensure sustainable economic growth with an equitable distribution of wealth. In this connection, the authorities are committed to promoting sustainable and inclusive high economic growth through economic diversification, strengthening competitiveness and promoting productivity through the steadfast implementation of Industrial Development Policy. The completion of hydropower projects will result in more affordable electricity and contribute to enhancing Cambodia's business climate and competitiveness. At the same time, the authorities will continue to focus on infrastructure projects including roads and irrigation, that would play a vital role in addressing structural bottlenecks and further promoting rural development. More importantly, the authorities are also focusing on developing human capital through education reform, especially technical and vocational training, which in turn will strengthen productivity and further promote inclusive growth.

Conclusion

14. The Cambodian authorities are committed to preserving macroeconomic and financial stability, promoting sustainable and inclusive growth and stand ready to implement any measures deemed appropriate. While significant progress has been made to advance the Cambodia's economic growth and development, the authorities will continue their efforts to further improve the macroeconomic and financial sector regulatory frameworks in line with the Fund's policy recommendations. Finally, the authorities would like to express their appreciation to the Fund for its continuing support through policy advice and technical assistance and look forward to continued support from the Fund.