INTERNATIONAL MONETARY FUND

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CAMBODIA

December 2022

2022 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR CAMBODIA

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 2022 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 November 23, 2022, 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 November 23, 2022, following discussions that ended on September 20, 2022, 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 November 8, 2022.
- An **Informational Annex** prepared by the IMF staff.
- A **Debt Sustainability Analysis** prepared by the staffs of the IMF and the World Bank.
- A **Statement by the Executive Director** for Cambodia.

The documents listed below have been or will be separately released.

Selected Issues - SM/22/254

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PRESS RELEASE

PR22/439

IMF Executive Board Concludes 2022 Article IV Consultation with Cambodia

FOR IMMEDIATE RELEASE

Washington, DC – **December 18, 2022:** The Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Cambodia.

Cambodian GDP growth rebounded in the second half of 2021, driven mainly by exports of goods. But this year the economy has been buffeted by developments in China, the slowdown in consumer demand in advanced countries—the US and Europe are significant markets for Cambodian manufactures—and tighter global financial conditions (mainly via external demand, but also funding costs for some financial institutions). Inflation surged, following significant increases in fuel and fertilizer costs, export orders for the second half of the year have weakened, and the real estate market is slowing.

Despite the new pressures, the recovery is projected to continue. Real GDP growth is forecast to be 5 percent in 2022, after the strong export performance earlier in the year, and nearly 5½ percent in 2023, supported by the continued recovery of tourism and ongoing policy support, although dampened by external pressures and the impact of rising prices on real disposal income. Inflation is expected to peak this year, be lower in 2023, and decline further thereafter, assuming it remains mostly confined to imported goods.

Uncertainty around the outlook is particularly high, and risks are tilted to the downside. The most pressing risks are from rising private debt; conditions in key large economies; and inflation.

The public finances are expected to gradually improve. Spending pressures and lower-than-expected tax revenue resulted in a fiscal deficit of just over 7 percent of GDP in 2021. The deficit is expected to narrow to just over 4 percent of GDP in 2022 with a strong bounce-back in revenues, widen somewhat in 2023, and decrease further thereafter. Public debt-carrying capacity remains vulnerable to further shocks to exports and growth, but risks of external and overall debt distress remain low, so long as public debt is constrained in the future and the increase in private debt is not associated with an increase in contingent liabilities of the sovereign.

[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 welcomed Cambodia's strong economic recovery from the pandemic supported by the country's strong economic buffers and robust crisis response. Directors agreed that the growth outlook is broadly favorable, notwithstanding downside risks from slower external demand and rising domestic vulnerabilities including elevated levels of private debt. In that context, they encouraged the authorities to calibrate fiscal policy to help support vulnerable households, without compromising price stability, while also taking steps to address financial sector risks and corruption vulnerabilities.

Directors encouraged the National Bank of Cambodia to rein in credit growth by gradually restoring monetary conditions to pre-crisis levels. They saw merit in normalizing prudential conditions to pre-pandemic settings with heightened supervision and readiness to raise provisioning requirements. Directors also underscored the importance of implementing corporate insolvency, debt and bank restructuring, and deposit protection frameworks.

Directors supported the authorities' current fiscal plans to provide insurance against downside risks to aggregate demand while maintaining steady reduction in fiscal deficits over the medium term. However, given wide external imbalances and strong credit growth, they emphasized that fiscal support should be well targeted. Social protection measures should continue to be used to protect the poor against the effects of inflation, coupled with offsetting cuts elsewhere.

Directors noted the importance of policy frameworks to ensure resilience over the longer term. They encouraged efforts to enhance spending efficiency and strengthen revenue mobilization, including by broadening the tax base and rationalizing exemptions. A debt anchor in nominal terms, combined with an overall deficit ceiling, would provide a credible framework, particularly as Cambodia seeks to develop a market for sovereign debt. The recent issuance of the first domestic government bond is a welcome development.

Directors underscored the importance of complementary structural policies to support strong, inclusive growth. They welcomed the progress made in implementing anti-corruption action plans and encouraged continued efforts to strengthen governance frameworks more broadly. Directors also emphasized the need for structural measures to boost productivity to help raise living standards and to durably restore external balances, given the pegged nominal exchange rate. They also underscored the importance of improving data quality through capacity development and encouraged the authorities to build on recent efforts to strengthen climate adaptation and mitigation.

It is expected that the next Article IV consultation with Cambodia will be held on the standard 12-month cycle.

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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.

Table 1. Cambodia: Selected Economic Indicators, 2019–23

Per capita GDP (2021, US$) : 1,648 Life expectancy (2019, years) : 75.5
Population (2021, million) : 16.3 Literacy rate (2019, percent) : 87.7

	2019	2020	2021	2022	2023
			Est.	Proj.	
Output and prices (annual percent change)					
GDP in constant prices	7.1	-3.1	3.0	5.0	5.4
Inflation (end-year)	3.1	2.9	3.7	5.8	3.5
(Annual average)	1.9	2.9	2.9	5.8	3.5
Saving and investment balance (in percent of GDP)					
Gross national saving	9.2	16.4	-22.0	-5.0	10.9
Government saving	8.4	3.4	0.4	3.1	4.1
Private saving	0.8	13.0	-22.3	-8.1	6.9
Gross fixed investment	24.2	24.9	25.5	25.0	25.0
Government investment	7.4	8.8	9.0	8.9	9.0
Private investment	16.8	16.1	16.5	16.1	16.0
Money and credit (annual percent change, unless otherwise indicated)					
Broad money	18.2	15.3	16.3	18.5	12.6
Private sector credit	28.0	17.2	23.4	18.0	15.0
Velocity of money 1/	0.9	0.8	0.7	0.6	0.6
Public finance (in percent of GDP)					
Revenue	26.8	23.9	21.6	22.1	22.0
Domestic revenue	24.8	22.0	20.0	21.4	21.1
Of which: Tax revenue	21.7	19.7	18.0	19.4	19.1
Grants	2.0	1.9	1.6	0.7	0.8
Expenditure	23.8	27.3	28.6	26.1	26.9
Expense	16.4	18.6	19.6	17.3	17.9
Net acquisition of nonfinancial assets	7.4	8.8	9.0	8.9	9.0
Net lending (+)/borrowing(-)	3.0	-3.4	-7.1	-4.1	-5.0
Net lending (+)/borrowing(-) excluding grants	1.0	-5.3	-8.6	-4.8	-5.8
Net acquisition of financial assets	8.8	0.6	-4.0	-1.1	-1.7
Net incurrence of liabilities 2/	5.8	4.0	3.0	3.0	3.3
Balance of payments (in millions of dollars, unless otherwise indicated)					
Exports, f.o.b.	14,998	18,470	19,469	22,062	24,061
(Annual percent change)	15.6	23.2	5.4	13.3	9.1
Imports, f.o.b.	-22,251	-20,993	-30,726	-29,340	-28,220
(Annual percent change)	18.3	-5.7	46.4	-4.5	-3.8
Current account (including official transfers)	-4,067	-2,182	-12,624	-8,587	-4,318
(In percent of GDP)	-15.0	-8.5	-47.5	-30.0	-14.1
Gross official reserves 3/	18,763	21,334	20,941	20,747	22,304
(In months of prospective imports)	9.8	7.8	7.8	8.0	8.1
External debt (in millions of dollars, unless otherwise indicated)					
Public external debt	7,596	8,810	9,493	10,284	11,086
(In percent of GDP)	28.2	34.4	35.9	36.1	36.3
Public debt service	309	360	384	408	426
(In percent of exports of goods and services)	1.5	1.8	1.9	1.7	1.6
Memorandum items:					
Nominal GDP (in billions of Riels)	110,014	105,892	110,506	120,315	130,477
(In millions of U.S. dollars)	27,087	25,771	26,601	28,647	30,729
Exchange rate (Riels per dollar; period average)	4,062	4,109	4,154	..	..

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

1/ Ratio of nominal GDP to the average stock of broad money.
2/ Includes statistical discrepancy.
3/ Includes unrestricted foreign currency deposits held at the National Bank of Cambodia.

INTERNATIONAL MONETARY FUND

CAMBODIA

STAFF REPORT FOR THE 2022 ARTICLE IV CONSULTATION

November 12, 2022

KEY ISSUES

Context: After suffering a recession during the pandemic, the Cambodian economy was on a steady recovery path, but is facing new pressures in 2022 that have buffeted external demand and increased inflation rates. The authorities have largely continued with crisis policy responses and have pressed on with policy reforms. The recovery is projected to continue, notwithstanding external stresses. Risks of public debt distress remain low. However, the level of private debt raises concerns about potential debt overhang.

Recommendations:

- *Financial:* The supervisor has taken the welcome step of reintroducing provisioning requirements. It should continue to normalize prudential conditions to pre-pandemic settings, take a highly conservative approach to supervision, and be prepared to further raise provisioning requirements and instruct lenders facing solvency problems to proactively increase capital. High private debt levels combined with large outstanding amounts of restructured loans emphasize the importance of strengthening corporate insolvency regimes and bank resolution frameworks, and the need to introduce deposit protection schemes.

- *Monetary and exchange rate policy:* The central bank should complement prudential measures by gradually restoring minimum reserve requirements to pre-crisis levels, to help reign in credit growth and mitigate the risk of domestic inflation risks going forward. Given the managed peg exchange rate regime and extensive dollarization, addressing external imbalances falls to gradual fiscal consolidation and structural reforms.

- *Fiscal:* Current fiscal plans appropriately balance some continued stimulus in the near term with steady reductions in the deficit over the medium term. Social protection measures should continue to be used to protect the poor against the effects of the new external shocks, with care to ensure all public spending is well targeted. Revenue mobilization (including rationalizing exemptions) and diversification are paramount over the medium term; simplification of the tax

- system would encourage compliance. A debt anchor in nominal terms, combined with an overall deficit ceiling, would provide a credible framework.

- *Governance:* Notable efforts have been made to improve governance frameworks. However, vulnerabilities remain, which would be ameliorated by passage of key legislation, digitization of reporting and monitoring processes, and securing sufficient human and technological resources for investigative and monitoring agencies.

Approved by
Anne-Marie Gulde-Wolf (APD) and Andrea Schaechter (SPR)

Discussions took place from September 7–20, 2022. The staff team was comprised of Juliana Araujo, Alessia De Stefani, Yasuhisa Ojima (IMF resident representative), Ryoichi Okuma, Alasdair Scott (head) (all APD), Camilo Enciso (LEG), Dyna Heng, and Luisa Zanforlin (both ICD). Kuchsa Dy, Pirun Chan, and Chenda Pich supported the mission from the IMF's office in Phnom Penh. Hibah Khan and Mariam Souleyman assisted from IMF HQ. Meetings were also attended, variously, by IMF Executive Director Rosemary Lim and Sukjai Wongwaisiriwat (OEDST).

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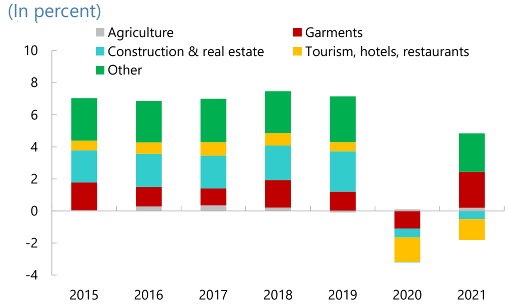
RECENT DEVELOPMENTS

1. The Cambodian economy was hit hard by the pandemic, but damage was mitigated by policy measures that benefited from buffers built up before the crisis.

- The pandemic brought a collapse of tourism and, initially, a falling demand for manufactured goods. In 2021, the economy was set back by community spread of the virus and some lockdowns. As a result, the economy fell into recession in 2020 and had relatively slow growth in 2021.

Contribution to GDP Growth
(In percent)

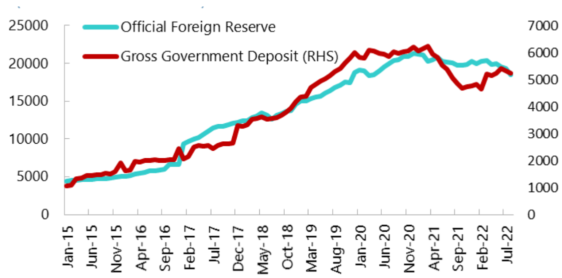


Sources: Cambodia authorities.

- A managed exchange rate meant limited ability to use monetary policy, but, in part because of substantial foreign exchange reserves, the exchange rate did not come under significant pressure. Large fiscal buffers provided room for increased spending on health care, employment support, and cash transfers to households. Without these measures, growth would have been even worse, as would likely have been the increase in poverty.[1]

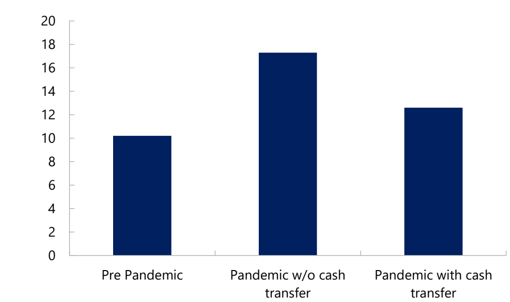
- Spending pressures combined with lower-than-expected tax revenue resulted in a larger fiscal deficit than expected in 2021. Tax revenue from imported goods was weak in 2021 (Figure 2). Compared to 2020, spending as a share of GDP remained almost unchanged with increased Covid-19 related public spending compensated by reductions in other current and capital spending.

Government Deposit and Foreign Reserves.
(In millions of US dollars)



Sources: Cambodia authorities.

Share of households living below 1.9 USD/worker/day
(In percent)



Sources: IMF staff calculations based on 2019/2020 Cambodia Socio Economic Survey

2. From the second half of 2021, the Cambodian economy showed stronger signs of recovery from pandemic stresses (Figure 1). Growth was driven mainly by exports of goods

[1] See De Stefani, Laws, and Sollaci (2022), IMF WP22/064.

(garments, electronics, and vehicle parts), which grew by around 40 percent (yoy, ytd), while the recovery in construction and real estate—a large contributor to growth before the crisis—was relatively weak. The recovery was boosted by rapid vaccination during 2021 and reductions of Covid-19 infection rates. In March 2022, the country fully relaxed entry restrictions on foreigners, providing a boost to the beleaguered tourism industry.

3. **2022 has brought new stresses.** The external environment has become more challenging:

- The slowdown and further lockdowns in China have slowed the recovery through lower foreign investment, particularly in real estate, and supplies of textiles to the garments industry. Continued restrictions on movement have also delayed a quick return to precrisis numbers of foreign tourists, given the pre-pandemic importance of Chinese tourists to Cambodia.

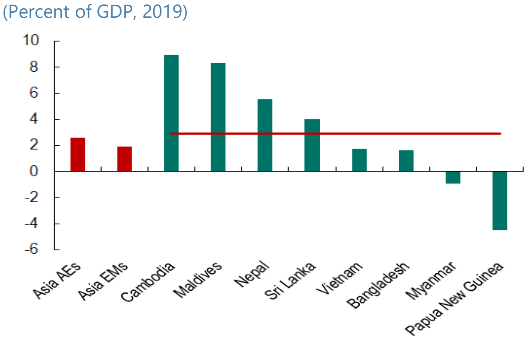
- Cambodia has limited export and financial exposure to Ukraine and Russia, but the war has affected Cambodia through demand in Europe, which is a major market for manufactures, second only to the US. The tightening of monetary conditions in advanced economies has mainly indirect effects through external demand, as the financial system is mostly reliant on domestic deposit funding.[2]

4. **These new stresses have been associated with a surge in inflation and a slowdown in growth.**

- Inflation reached 7.8 percent y/y in June 2022, before retreating to 4.4 percent y/y in September. Cambodia imports food and fertilizers; its reliance on imported fuel is higher than many other regional comparators. Consequently, the recent increases in global fuel, food, and fertilizer prices have resulted in historically high inflation rates, like neighboring countries. The contribution of core items has increased, but remains muted so far.

Net Imports of Oil and Gas

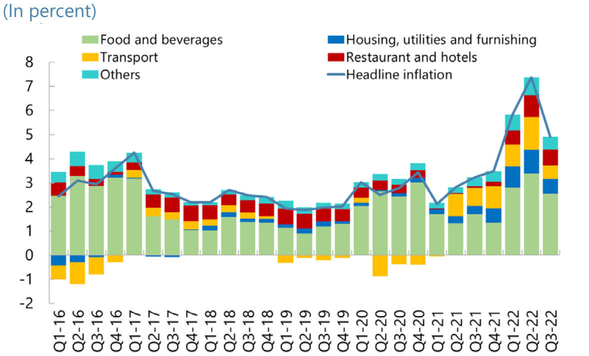
(Percent of GDP, 2019)



Source: IMF Country Desk Survey and IMF staff estimates.

Contribution to Inflation of Product Groups

(In percent)

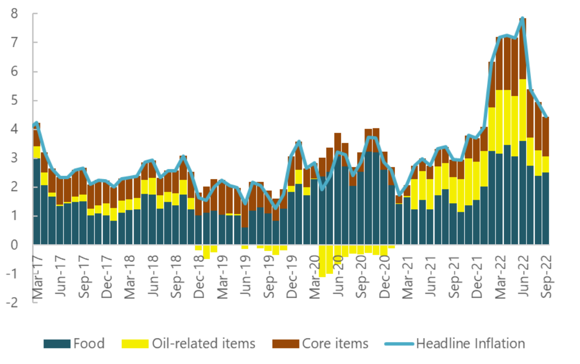


Sources: Cambodia authorities

[2] Anecdotal evidence suggests new manufacturing orders to be delayed.

Contribution to Headline Inflation

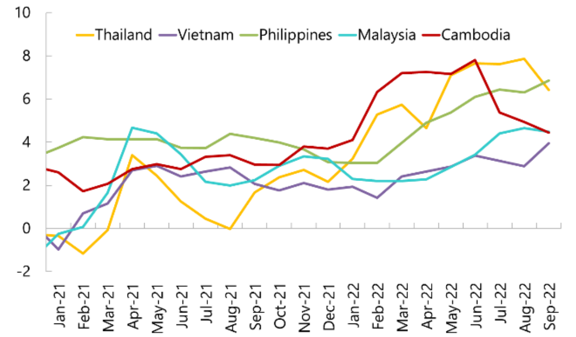
(Yoy, in percent)



Sources: Cambodia authorities

Consumer Price Index

(In percent, y/y)

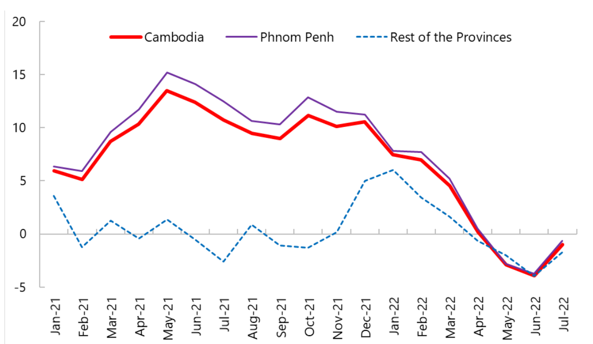


Sources: CEIC and Cambodia authorities

- There are signs that the domestic real estate market (both high-end residential and commercial) is experiencing a downturn. Yields indicate a growing surplus of commercial and high-end residential space. Rental prices for commercial developments, as well as purchase prices for high-end residential properties, appear to be falling after more than a decade of sustained growth. The sector is important in terms of both GDP share and exposure of the rest of the economy.

Cambodian Residential Property Price Index

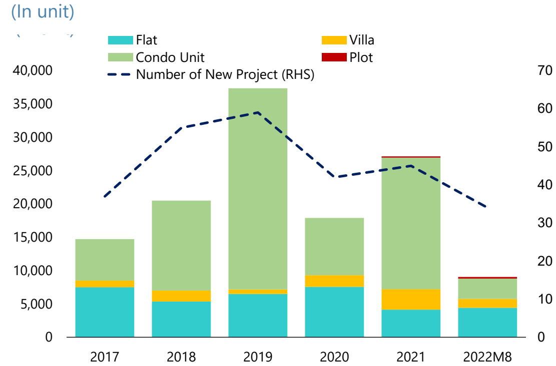
(Jan 2020 – July 2022, y/y)



Source: Cambodia authorities

Real Estate New Project

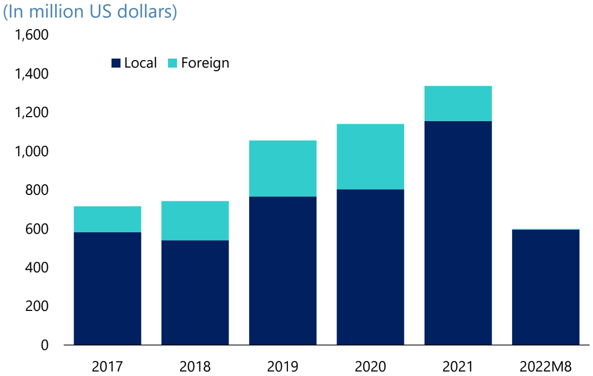
(In unit)



Source: NBFSA

Source of Investment Capital

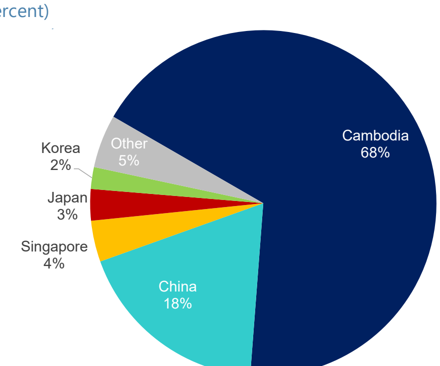
(In million US dollars)



Source: NBFSA

Project Origin by Country, 2010-2022M8

(In percent)



Source: NBFSA

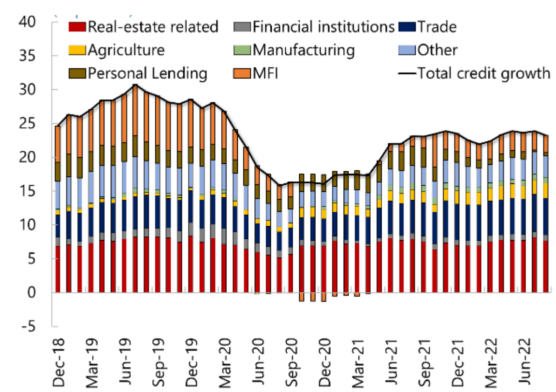
5. Despite the pressures of the past years, credit growth has continued to be strong, and private sector indebtedness is now significant (Selected Issues Paper).

- Credit growth has averaged around 24 percent y/y from 2013 to 2019 and slowed only mildly during the pandemic. Outstanding private sector credit reached 170 percent of GDP by end 2021, a ratio significantly above those of regional peers, suggesting that the level cannot be safely dismissed as driven by financial deepening. Credit growth has been strong across all sectors (text figure).[3] The number of loans has increased but the number of borrowers has increased at a slower pace, suggesting that some borrowers are becoming more leveraged.

- Credit growth was associated in 2020 and 2021 with growth in broad money that, although lower than that in 2019, was still stronger than growth in nominal GDP, driven in part by the expansion in the central bank's balance sheet as the government drew down on deposits at the central bank to finance fiscal support during the pandemic. It was also supported by the steady inflow of FX deposits in commercial banks,[4] and a steady increase in the loan-to-deposit ratio.

Contribution to Private Credit Growth

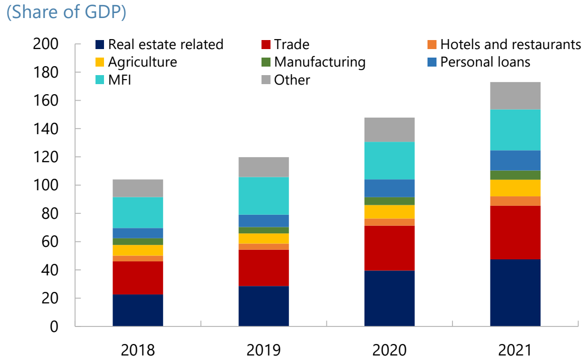
(In percent)



Source: Cambodia authorities

Private Sector Credit

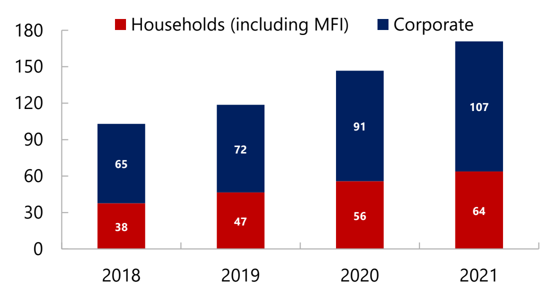
(Share of GDP)



Source: IMF staff calculations based on NBC monetary statistics.

Private Sector Credit

(Share of GDP)

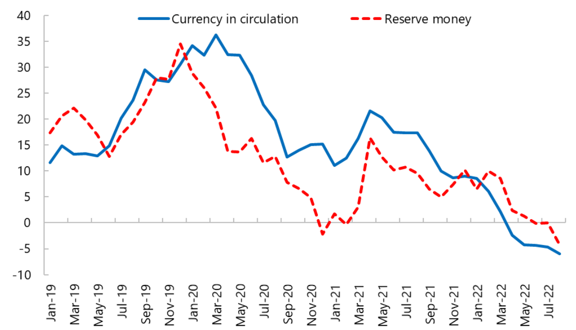


Source: IMF staff calculations based on NBC monetary statistics.

[3] The growth in credit is almost entirely to the private sector—that to government was less than one percent.

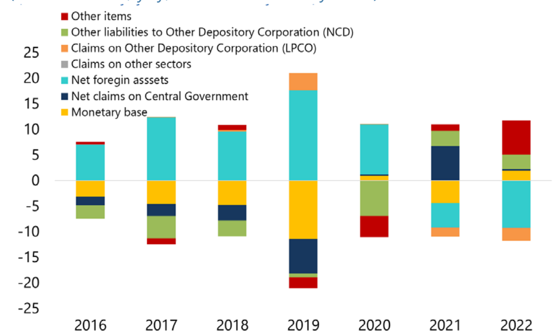
[4] The expansion in the central bank's balance sheet was only partially offset by reductions in FX reserves and liquidity operations.

Money Growth
(In percent y/y growth)



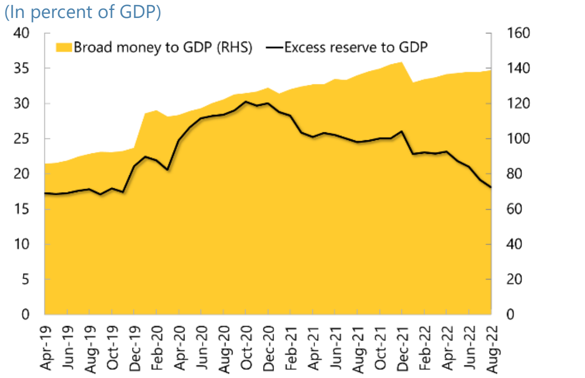
Source: Haver

Change in Main Items of NBC Balance Sheet
(In KHR trillion, yoy, data as end of July 2022)



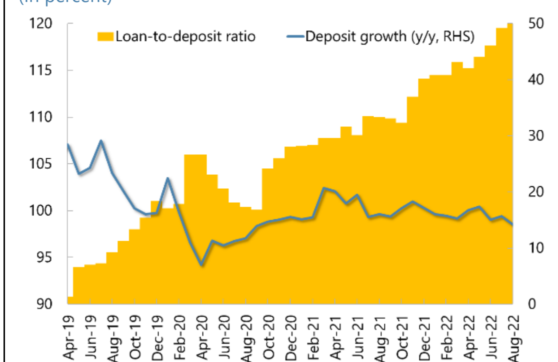
Sources: Cambodia authorities

Broad Money and (USD) Excess Reserves
(In percent of GDP)



Sources: Cambodia authorities

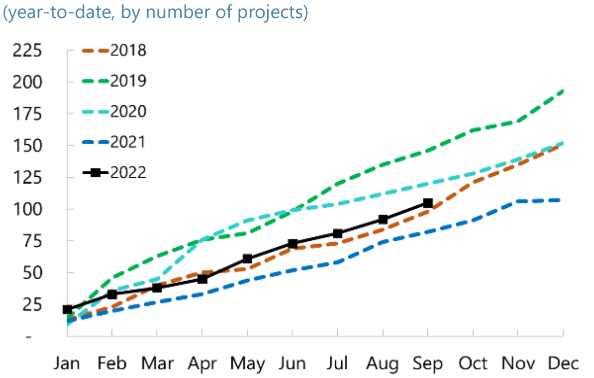
LTD and Deposit Growth
(In percent)



Sources: Cambodia authorities

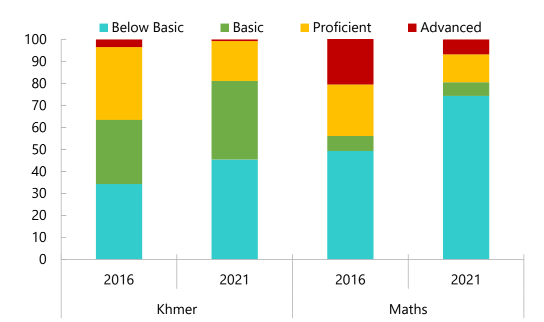
6. There are some signs of damage from the crisis. Lack of unemployment data makes it difficult to assess scarring effects in the labor market. But test scores indicate that lost schooling hours during the pandemic has damaged human capital attainment. Approvals of large projects (foreign-financed) remain lower than before the pandemic. Business registration appears to be recovering gradually, while business liquidations have been on the rise. Around 7 percent of the total stock of outstanding credit has been restructured (amounting to 13 percent of GDP).

Investment Approvals
(year-to-date, by number of projects)



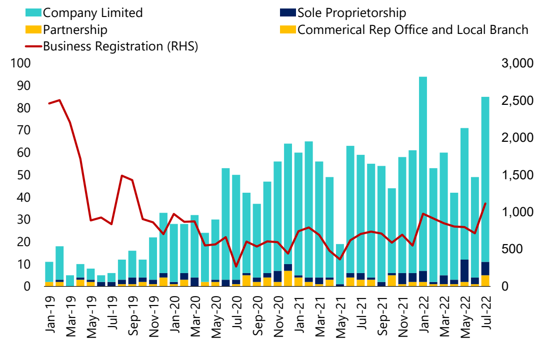
Sources: Cambodia authorities

Grade 6 Proficiency Levels in Khmer and Maths, public schools



Source: MoEYS "The National Learning Assessment

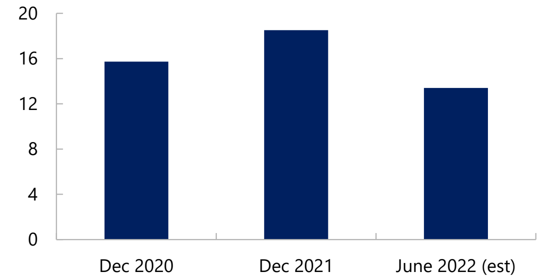
Business Liquidation and Registration



Sources: Cambodia authories

Stock of Restructured Loans

(Share of GPD)



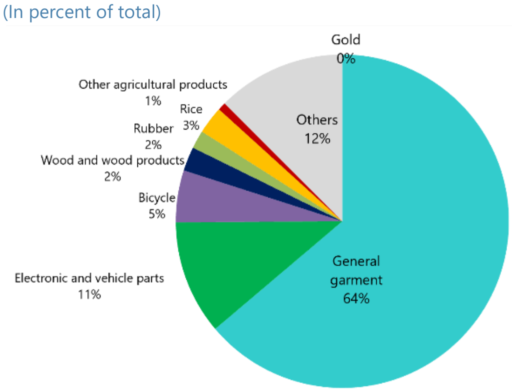
Source: IMF staff calculations based on NBC data.

7. The current account deficit has widened significantly and the external position at end-2021 remains substantially weaker than the level implied by medium-term fundamentals and desirable policies. The external sector assessment is complicated by data issues (Box 1), idiosyncratic and highly volatile flows of gold, uncertainty about the recovery, and the difficulty of assessing the appropriate level of imports to sustain growth convergence at this stage of the country's development.

- In 2021, the current account deficit widened substantially, to an estimated 48 percent of GDP. This was driven in part because of subdued tourism and rebound in imports, but unexpected imports of gold accounted for half of the deficit.[5] The reasons for the inflows of gold—and hence the assessment of whether the flows are temporary or permanent—are debatable: gold imports increased substantially from the end of 2020 through 2021 following the increase in the price of gold, suggesting perhaps purchases in expectation of future increases, but the size of the inflows is much larger (relative to nominal GDP) than would be expected on the basis of hedging flows observed in other countries.

Export in September 2022

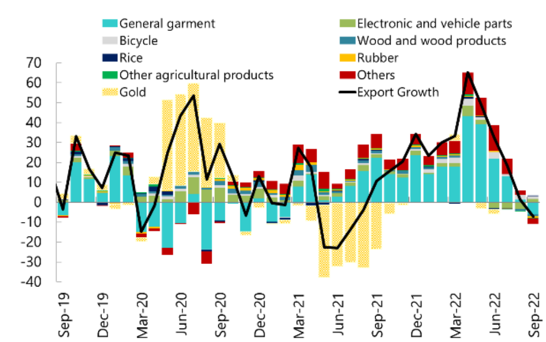
(In percent of total)



Sources: Cambodia authorities.

Contribution to Export Growth

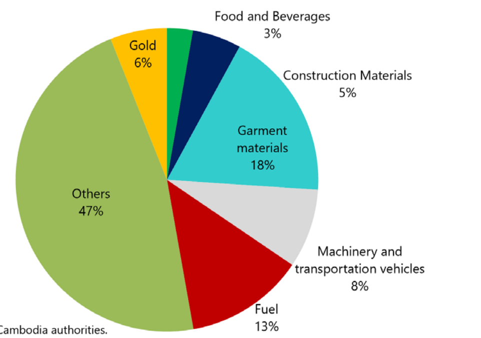
(In percent, y/y)



Sources: Cambodia authorities.

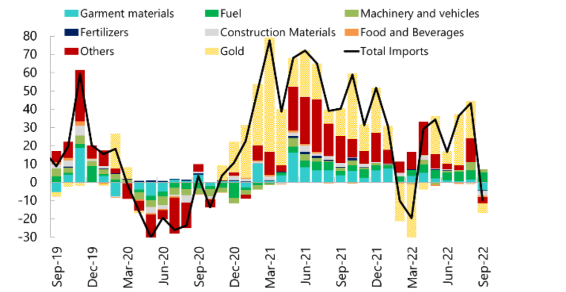
[5] Note that the current account balance actually *improved* in 2020, despite the collapse in tourism revenues and remittances, as a result of exports of non-monetary gold and import compression. Gold imports have often been large—as much as 5 percent of imports—but those for 2021 were exceptional.

Import in September 2022
(In percent of total)



Sources: Cambodia authorities.

Contribution to Import Growth
(In percent, y/y)



Sources: Cambodia authorities.

- The current account (CA) remains substantially weaker than implied by fundamentals and policies based on 2021 data (Annex I. External Sector Assessment), notwithstanding a gradual reduction in fiscal deficits. This conclusion is supported by both CA and REER models used, though there is uncertainty surrounding the underlying BoP data. The application of the CA model includes an adjustor for the impact of the pandemic on tourism, for the sharp increase in imports for emergency healthcare spending in 2021, and to discount half of the gold imports as temporary. The assessment would remain the same even with gold flows completely removed from the CA data, and would leave a substantial amount to be explained away by other factors. The gap may also be partly due to overstated savings needs, since the model does not take into account Cambodia's young population.[6]

- Financial inflows have been steady, which has been crucial for the stability of the exchange rate and FX reserves, and has been associated with continued growth in dollar deposits at banks. However, a large part is accounted for by a surge in short-term unidentified inflows.

- FX reserves declined by two percent in 2021 from levels in 2020, but, at US$ 21 billion, covers around 8 months of projected imports. The exchange rate has remained steady, with some intervention in late 2021, but none in 2022 to September.

8. The authorities' have largely continued with crisis policy responses and have pressed on with important reforms.

- Support measures include loans and guarantees; tax breaks; wage subsidies and retraining, and cash transfers. The Covid-19 Intervention Package, including public health, social and other economic interventions, is planned to reach US$ 882 million in 2022 (about 3 percent of GDP), providing a similar support than in 2020, although less than in 2021 (when it reached 5 percent of GDP) owing to withdrawal of emergency Covid-19-related healthcare spending. The National Bank of Cambodia (NBC) has maintained reserve requirements and the capital conservation buffer at current levels, has ended forbearance on new restructurings from July this year.

[6] See also IMF CR/21/260.

- The authorities have sought opportunities for structural reform, including establishing new free trade agreements and introducing a "One-Stop" mechanism for investors (e.g., online business registration, a national single window).

Box 1. Balance of Payments Data[1]

Recent noticeable improvements in data collection have resulted in improved coverage of trade data, especially in precious metals and in agricultural products. However, large and persistent discrepancies between the trade data from national sources and the mirror data from trade partner countries complicate the assessment of external balances, as does the large amount of short-term financial inflows labelled "Other". Improvements in data on remittances, foreign direct investment, and foreign assets and liabilities are also needed.

Trade: Discrepancies are the major contributor to inconsistency between national accounts and balance of payments—over the period from 2015 to 2020, discrepancies between the current account and saving/investment balances averaged around 11 percent of GDP. It is expected that these discrepancies will be smaller following the introduction of newly-rebased GDP data in the next year.

Short-term financial inflows: Current estimates are to be replaced with data sources that would cover cross-border financial transactions of non-financial sectors.

Remittances. Proposed changes to the models used to estimate remittances model rest on fastidious research of recent studies and economic indicators in hosting countries, but the potential for significant overvaluation remains. Better data on the number of workers abroad (especially in Thailand) and the work duration per contract will affect the estimation of earnings and, hence, the value of remittances.

Foreign assets and liabilities. Better source data are needed to measure foreign assets and liabilities of non-financial corporations and households. The priority is collecting and processing administrative data, most importantly financial statements of enterprises with foreign capital and data on the execution of large infrastructure projects, including under private-public partnership, where foreign capital is utilized.

The IMF continues to provide technical assistance to improve external sector statistics.

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[1] This box was written by Natalia Ivanyk from the IMF's Capacity Development Office in Thailand.

COVID-19 Intervention Package: Public Health and Social Intervention

(Percent of GDP)

Interventions	Description	2020	2021		2022
		Disb.	Plan	Disb.	Proj.
Health, Outbreak Prevention and Treatment	Scaling up health response by increasing prevention and detection facilities, clinical management, treatment and coordination and supporting system	0.1	0.1	2.6	0.3
Wage subsidy and skill training	Providing partial wage subsidies of $40 per month and technical/soft skills training for furloughed workers in the tourism and garment industries	0.2	0.2	0.1	0.2
Cash for work	Providing jobs in rural areas through construction, upgrade, and maintenance of rural roads, drainage and small-scale irrigation	0.4	0.6	0.6	0.3
Cash Transfer	Providing monthly cash grants to poor and vulnerable individuals that are registered in the government's IDPoor database	1.2	0.8	1.1	1.3

Authorities' Views

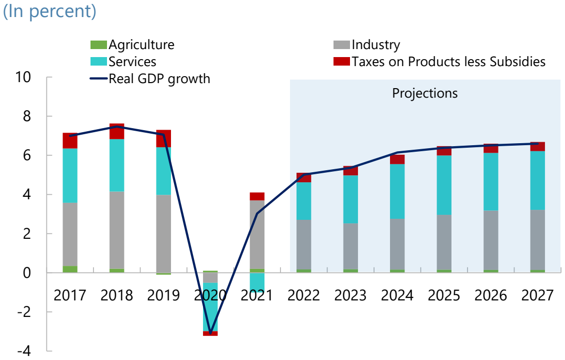
9. The authorities agreed that external stresses were severe, but were less conservative about credit levels. The authorities noted that the economy had maintained high credit growth for many years without problem, and that credit was evenly distributed across productive sectors; moreover, with rebased GDP, the private debt ratio would look more benign. They considered that estimates of current account imbalances should also account for high prices of imported intermediates and fuel, and falling tourism revenues and lower remittances during the pandemic.[7] Gold imports were driven by wealthy individuals seeking a store of value in uncertain times.

OUTLOOK AND RISKS

10. Despite the new pressures, the recovery is projected to continue. Real GDP growth is forecast to be 5 percent in 2022, after the strong export performance earlier in the year, and nearly 5½ percent in 2023, supported by the continued recovery of tourism and ongoing policy support, although dampened by external pressures and the impact of rising prices on real disposal income. Growth is assumed to gradually converge to a potential rate of about 6½ percent. The trend growth rate assumption is somewhat below pre-Covid-19 rates of 7 to 7½ percent, but comparable with those seen in neighboring countries at similar stages of development, and reflects a judgment that, although the Covid-19 crisis will have some lingering effects, the authorities' ongoing reforms (e.g. the investment law that creates a single contact point for investors) and new trade agreements (RCEP, an FTA with China) will support growth over the medium term. Inflation is expected to peak this year, be lower in 2023, and decline further thereafter, assuming it remains mostly confined to imported goods.

Real GDP Growth Contributions

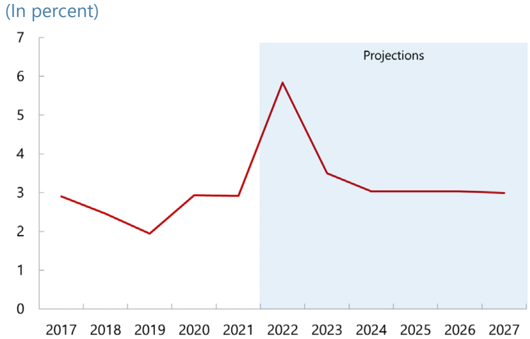
(In percent)



Sources: Cambodia authorities and IMF staff projections

Headline CPI

(In percent)



Sources: Cambodia authorities and IMF staff projections

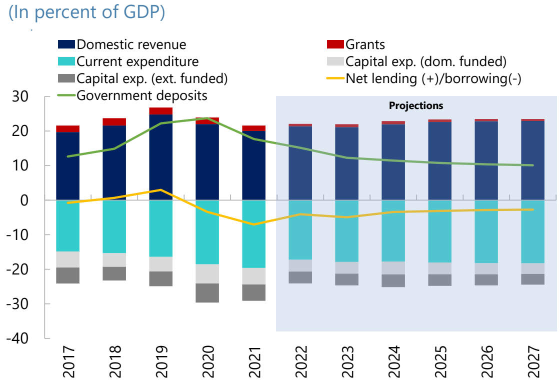
[7] That said, the authorities' own estimates of real exchange rate disequilibrium were quantitatively in the range consistent with staff's characterization of "substantially weaker than implied by fundamentals and policies".

11. The public finances are expected to gradually improve. Staff expects the fiscal deficit to narrow to 4.1 percent of GDP in 2022 and increase to 5.0 in 2023, before falling thereafter to 3 percent of GDP in the long-run, consistent with public debt at 40 percent of GDP. Debt-carrying capacity remains vulnerable to further shocks to exports and growth, but risks of external and overall debt distress remain low so long as debt is constrained in the future.

- Staff projects the fiscal deficit to narrow from 7.1 percent of GDP in 2021 to 4.1 percent of GDP in 2022, on the back of broad-based tax revenue rebound (Figure 2) and lower spending, increase somewhat in 2023, and decline steadily thereafter. Staff expects that fiscal support will be contained in 2022 because of winding back emergency Covid-19 healthcare spending. In 2023, current spending is expected to increase slightly, reflecting planned wage increases and some decompression of government operations (e.g. traveling), while social protection and capital spending levels are to be maintained. The projections assume a reduction in the level of government deposits at the central bank, from around 24 percent in 2020 to around 10 percent of GDP over the medium term.

Medium-Term Fiscal Outlook

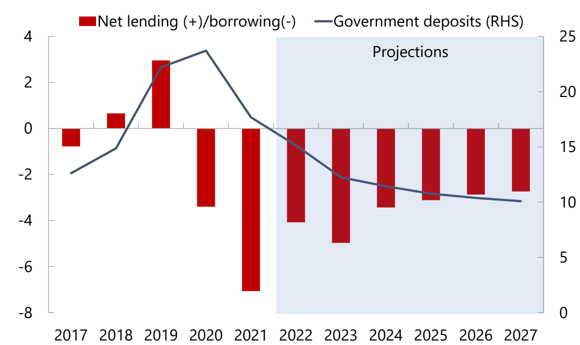
(In percent of GDP)



Sources: Cambodia authorities; and IMF staff calculations.

Fiscal Balance

(In percent of GDP)

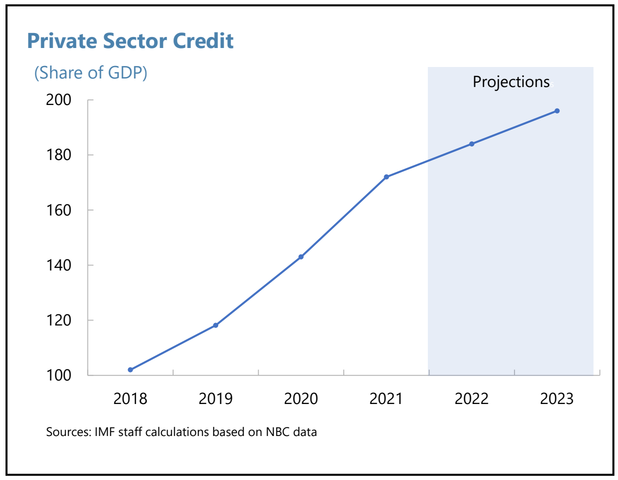


Sources: Cambodia authorities; and IMF staff calculations.

- Debt carrying capacity remains vulnerable to further shocks to exports and growth. A test for financial market contingent liabilities reveals an increase in debt servicing to revenues. Overall, however, the increase in the ratio of total public and publicly guaranteed (PPG) debt to GDP is relatively modest, implying that Cambodia remains at low risk of external and overall debt distress (Debt Sustainability Analysis).

12. The current account deficit gradually falls. The balance is projected to be -30 percent of GDP in 2022, narrowing as the services balance recovers thanks to the expected growth in tourism and other exports, and on the assumption that gold imports are temporary. The deficit remains mostly financed in the baseline. As a result, reserves are expected to remain high and stable, at about 8 months of imports throughout the projection period.

13. Credit growth would moderate, but private sector debt would continue to increase. Forces acting to slow credit growth include: revised prudential rules; further competition for funding among commercial banks (mainly deposits, but also higher wholesale costs for some banks); a reduced pace of drawing down deposits at the central bank, and, potentially, declining collateral values and rising shares of non-performing loans. However, credit growth would still outstrip nominal GDP growth.



14. Uncertainty around the outlook is particularly high, but risks are tilted to the downside (Annex II). The most pressing risks are

- *Credit growth:* The level of private debt raises concerns about the drag on the economy if borrowers struggle to meet repayments and large amounts of non-interest-paying assets accumulate in banks' balance sheets.

- *Conditions in key large economies:* Further lockdowns in China could lead Cambodian manufacturers to suspend production for want of supplies, while a further slowdown could slow inward investment. Demand in advanced countries is vulnerable to tightening financial conditions; vulnerabilities in Europe are accentuated by energy supply risks.

- *Inflation:* Global food and fuel price inflation could prove to be more persistent, and inflation expectations could de-anchor in advanced countries, incurring further and more rapid tightening of monetary conditions and borrowing costs, and lower growth in advanced economies. Imported food and fuel price increases could generate second-round effects in domestic inflation that would damage aggregate demand, which would be accentuated if the currency depreciated, given extensive dollarization.

Over the medium term, the economy faces ongoing risks from a resurgence of Covid-19 or other epidemics, and the country is especially vulnerable to natural disasters arising from drought, floods, and tropical storms.

Authorities' Views

15. The authorities agreed on risks from the external environment, but expected somewhat stronger growth. They expected positive momentum for exports into 2023, but slowing compared to early 2022. They agreed that the slowdown in China might slow inward investment, but nonetheless expected that construction and real estate would continue to grow, albeit at a slower pace and below pre-pandemic levels. They expressed particular concern about fallout from the war on Ukraine and from monetary policy tightening on demand in major export markets. They also stressed that fiscal support planned for 2023 would prop up domestic demand. The authorities expected inflationary pressures to slightly moderate in 2023, as international food and energy prices are expected to subside significantly, and did not see risks of significant second-round effects on domestic inflation. The authorities did not perceive the risks from private debt were as severe as those posed by the external environment.

POLICY DISCUSSIONS

16. The policy discussions focused on near-term challenges and medium-term policy frameworks. The immediate issue facing the authorities is the level and composition of policy support, given the challenges posed to growth from the external environment on the one hand and the high levels of private indebtedness on the other. The next pressing issue is policy frameworks to guide Cambodia over the medium term. Both items are relevant for thinking about safeguards against imbalances:

- *Credit and debt*: Escalating private debt combined with the risk of further pressures on real incomes raise the question of potential stresses on borrowers and the resilience of lending institutions, and emphasize the importance of frameworks for resolving insolvencies and restructurings.

- *Fiscal*: The Debt Sustainability Analysis indicates that Cambodia has fiscal space to cope with further adverse shocks, but nonetheless fiscal resources are not limitless, especially as sovereign access is only nascent, emphasizing the need for careful targeting of fiscal support and frameworks to ensure fiscal credibility is maintained.

- *External:* Due to extensive dollarization, nominal depreciation alone would not significantly address external imbalances. The burden of external adjustment therefore falls onto gradual fiscal consolidation, on measures to contain credit growth, and on reforms to improve long-run productivity.

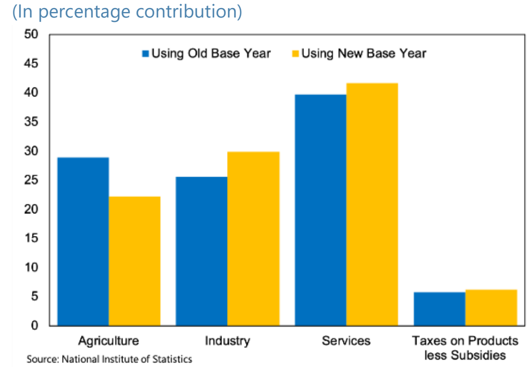
17. Prospective changes to GDP data complicate policy recommendations. Preliminary results suggest that the level of nominal GDP could increase by close to 30 percent when national accounts are rebased in early 2023, substantially changing indicators such as public debt to GDP ratios (Box 2).

Box 2. GDP Rebasing

The National Institute of Statistics has prepared new national accounts data, rebased to 2014. The level of Nominal GDP is expected to be revised up by just over 30 percent, and manufacturing and services (agriculture) will account for slightly larger (smaller) shares of production GDP. A Technical Review by the IMF's Statistics Department has confirmed that the rebasing exercise follows international statistical conventions.

Cambodia 2014 Gross Domestic Product

(In percentage contribution)



While a more comprehensive assessment of the implications of GDP rebasing will only be possible upon final data release, expected in early 2023, it is anticipated that the ratio of public and private debt to GDP will decline but so will the revenue-to-GDP ratio. The ratio of private debt to GDP would likely remain high, in comparison with peer countries in the region. Cambodia would retain lower-middle income status.

A. Policies to Manage Near-Term Challenges

18. Policy support will need to be nimble in the face of considerable uncertainties, balancing the need to support demand if downside scenarios to growth materialize, or temper inflation if second-round effects onto domestic inflation emerge, or potentially tighten macro-financial policies.

Fiscal Policy

19. Current fiscal plans are appropriately balanced under the baseline scenario, with (i) the Covid-19 fiscal package cut back and expected fiscal consolidation in 2022, (ii) some continued stimulus in 2023 providing support against new shocks to aggregate demand that hit the economy in 2022 and will continue to unfold in 2023, and (iii) steady reductions in the deficit over the medium term. In terms of composition, the current plans adequately maintain the same heightened capital investment and cash transfer stimulus, while allowing for some needed current spending decompression. However, given high inflation, wide external imbalances, strong credit growth, and weak monetary transmission, fiscal support needs to be well targeted. Support to households should gradually move from the Covid-19 Cash Transfer Program for the Poor and Vulnerable to a system that better targets the most vulnerable household members and their needs, as planned[8]. Support to business should be targeted based on viability and the long-term growth potential of different sectors.

[8] The government is currently planning to integrate four existing programs, namely (i) cash transfers to pregnant women and children under 2, (ii) scholarships for primary and secondary school students, (iii) cash transfers to people with disabilities, and (iv) cash transfers to the elderly, into a social assistance system that intends to respond to the needs of the poor families and their vulnerable members from conception to death (Annex V).

20. Fiscal plans may need to be recalibrated if risks materialize. If inflation risks materialize and there are signs of significant second-round effects on domestic inflation, fiscal support should be wound back. There is fiscal space to provide targeted support in case of downside risks to growth. The authorities should avoid permanent spending increases that would make a medium-term fiscal deficit reduction challenging.

21. Social protection measures should continue to be used to protect the poor against the effects of inflation, but with some offsetting cuts elsewhere. Fiscal measures to protect the vulnerable from inflation are preferable to subsidies, but costs could escalate rapidly. The government has indicated that it will expand the range of overall social protection (Annex V) and use the system of cash transfers introduced in 2020 to compensate poorer households for increases in fuel and food costs. This approach is better than subsidies, but could add as much as 0.8 percentage points of GDP in spending under plausible scenarios for fuel prices alone (Selected Issues Papers). Making these transfers compatible with preserving fiscal space will require some offsetting cuts—in particular rolling back some Covid-19 support measures no longer needed. Some offsetting fiscal measures already taken, include discontinuing wage subsidies (while maintaining skill training), lowering emergency healthcare spending, and partially rolling back tax exemptions[9].

Monetary and Exchange Rate Policy

22. The exchange rate regime and extensive dollarization limit the ability of monetary policy to respond to inflation. The exchange rate follows a managed peg; moreover, the economy is highly dollarized, with a considerable degree of dollar invoicing in the manufacturing sector[10].

23. Nonetheless, to help rein in credit growth, the NBC should gradually restore monetary conditions to pre-crisis levels. Minimum reserve requirements on financial institutions should be increased, with the priority to raise the minimum reserve ratio for foreign currency above that for local currency, which would also mitigate the higher liquidity risks in FX than in local currency and assist in de-dollarization (Annex VI).[11]

24. Rectifying real exchange rate imbalances falls to gradual fiscal consolidation, measures to contain credit growth, and reforms to improve productivity. Priorities for the latter include improving transport and communications infrastructure and raising human capital.

[9] One exception is that hotels and guesthouses, restaurants, and travel agencies in tourist regions remain tax exempt through to the end of 2022, except for VAT.

[10] Since 2016, the NBC has required at least 10 percent of bank lending to be in riel, as part of its policies to reduce dollarization. Nonetheless, nearly 90 percent of lending has been in dollars. As yet, there are no signs of currency mismatches. A new regulation revising the computation of and limits on net open positions is in preparation.

[11] Interest rates were cut early in 2020 to facilitate lending, and required reserve ratios were cut, from 12.5 percent for dollars and 8 percent for riel to 7 percent for both currencies, to ease liquidity conditions.

Because improvements are likely to be slow, the adjustment should be supported in the near-term by maintaining the steady reduction in fiscal deficits.

Financial System Policies

25. The supervisor has ceased forbearance on newly-restructured loans, but has continued supportive policies for borrowers and banks. In May 2020, the NBC introduced a policy to facilitate restructuring of loans; since December 2021, it has taken the welcome step of reintroducing provisioning requirements on restructured loans. However, prudential practices are yet to revert to pre-pandemic standards: only 10 percent of total restructured loans were classified as non-performing as of June 2022, whereas under pre-pandemic requirements, restructured loans would have been mostly classified as NPLs. The capital conservation buffer has remained at 1.25 percent, after having been halved in May 2020. In addition, capitalization levels, while high, may be overstated as regulators have been lenient in allowing accrued receipts to be included in profits and reserve accounts as capital resources.

26. The ongoing support and previous experience with private debt imply a more conservative approach to supervision is warranted.

- Current rates of credit growth are likely driven by lenient prudential requirements—should a small proportion of restructured loans be written off, losses would likely be large and concentrated across banks. Past experience suggests that supervisors should be prepared for increasing levels of NPLs, which, if not addressed, would act as a drag on growth[12].
- While all banks comply with mandatory liquidity coverage ratios, current regulations allow them to include holdings of central bank instruments in local currency, whereas potential liquidity needs are in foreign currency, given the high share of dollar deposits.

27. On this basis, the NBC needs to continue to normalize prudential conditions to pre-pandemic settings, so that the financial system is able to withstand future shocks[13].

- The authorities should continue the gradual calibrated withdrawal of forbearance on (all) restructured loans, including returning to pre-pandemic prudential practices on restructured loans. At the same time, it should instruct lenders with the largest share of restructured loans to proactively increase capital.
- The NBC should intensify supervision, continuing rigorous onsite inspections and including extensive reviews of loan portfolios. It is particularly important to understand to what extent covid-related forbearance policies may have been supporting unviable businesses. Supervisors could also consider collecting and centralizing financial information on the

[12] Ari, Anil, Sophia Chen, and Lev Ratnovski (2019), "The Dynamics of Non-Performing Loans During Crises: A New Database", IMF Working Paper WP/19/272.

[13] For a general framework, see also Kongsamut, Piyabha, Dermot Monaghan, and Luc Riedwig (2021), "Unwinding COVID-19 Policy Interventions for Banking Systems," IMF Special Series on COVID-19.

largest borrowers, to facilitating debt restructuring policies and avoid uncoordinated evergreening practices.

- The NBC should be vigilant of any sudden liquidity needs. The authorities should proactively address emerging weaknesses under established safeguards to avoid potential distress from spreading across institutions.

- The authorities could consider increasing minimum paid in capital amounts and further review "fit and proper" requirements to ensure the financial system remains sound and stable. In particular, the establishment of nine new banks during the pandemic is difficult to square with the economic cycle.

B. Policy Frameworks for a Resilient Economy

28. The recovery is the right moment to advance frameworks for a robust and resilient economy. The authorities announced their economic recovery strategic framework in late 2021, introducing programs to revive key sectors, address structural challenges for diversification and competitiveness, and strengthen preparedness and responsiveness to future crisis[14]. At this juncture, three sets of issues are particularly important: first, the medium-term fiscal strategy, second, securing a safe and inclusive financial system, and improving the framework for governance and anti-corruption.

Fiscal Strategy and Frameworks

29. Demands on public spending increased during the pandemic and will likely increase further.

- Previous exercises identified spending needs to reach SDG targets of at least 7½ percent of 2030 GDP, with the largest needs in education and health[15]. The authorities had incorporated those needs in a national plan, but the emergency spending related to the Covid-19 crisis required a reprioritization[16].

- The crisis also highlighted healthcare spending needs, which is below the average of peers. The crisis has also evidently seen damage to educational attainment: the World Bank

[14] Policy issues discussed during the 2021 Article IV Consultation remain relevant, such as the importance of further diversification and reducing labor informality—see IMF CR/21/260. So too do past recommendations on data quality and transparency—see Annex III.

[15] Education and health account for about two thirds. Universal access to electricity and road would require an additional annual spending of about 2½ percent of 2030 GDP.

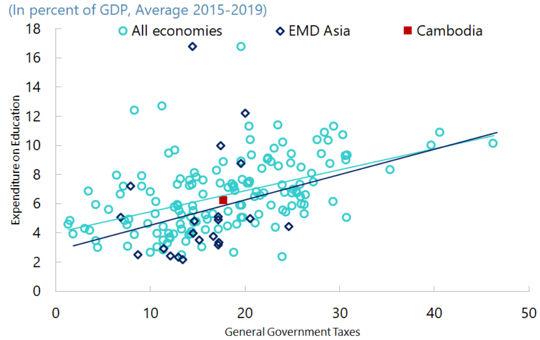
[16] See the National Strategic Development Plan (NSDP) for 2019–23.

estimates that Cambodia's current cohort of students stands to lose 1.5 learning-adjusted years of schooling—15 percent of pre-pandemic expectations[17].

- Going forward, demands on both educational and healthcare spending are likely to increase as the country attains middle income status, the authorities have indicated plans to expand social protection (Annex V), and climate adaptation needs will increase with climate change (Annex VII).

Government Expenditure on Health

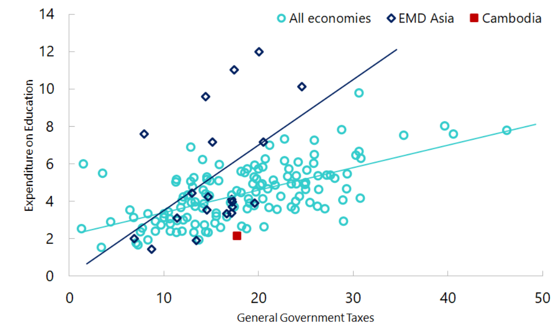
(In percent of GDP, Average 2015-2019)



Sources: World Bank and IMF staff calculations

Government Expenditure on Education

(In percent of GDP, Average 2015-2019)



Sources: World Bank and IMF staff calculations

30. The increased demands on public spending call for the introduction of a comprehensive fiscal framework. This would include an operational fiscal rule, with numerical target, to provide guidance on spending and revenue strategy and hence provide a credible framework as Cambodia develops access to market financing. Currently, the Public Debt Management Strategy (PDMS) 2019-23 lays out a total debt ceiling of 55 percent of GDP in NPV terms. Staff recommends a debt anchor in nominal terms, combined with an overall deficit ceiling, over other rules (e.g. expenditure rules), for simplicity, transparency, and direct link to fiscal balances. An anchor of 40 percent of nominal GDP should provide adequate buffers against the risk of debt increases, given the structural vulnerabilities (e.g. narrow revenue base, volatility of revenues and social protection demands, dollarization and fixed exchange rate) and the need to demonstrate policy continuity as the government seeks to establish market access.

31. A strategy for revenue mobilization should consider not only revenue needs but incentives (Selected Issues Papers)**.**

- On the basis of *current* GDP data, tax revenues are not low in comparison to peers. But given the likely increase in spending needs, tax revenues will need to increase. In addition, as

[17] See World Bank, *Cambodia Economic Update: The Impact of the COVID-19 Pandemic on Learning and Earning in Cambodia*, December 2021.

Cambodia graduates from least developed country status, grant revenue will continue to decline and will need to be replaced.

- The structure of taxes should be diversified. Revenue reliance on imported goods is significant, and consequently tax revenue is heavily procyclical. The ability to increase labor and corporate income taxes is limited by the desire to encourage workers and firms to register formally. Instead, more reliance on inelastic taxes (property, "sin" taxes) should be considered.

- Tax deferrals and exemptions should be minimized. Tax incentives to the tourism industry have been partially rolled back, but exemptions from customs duties and VAT remain significant, and the long-standing corporate income tax holiday is either not effective or potentially harmful.

32. The government should continue to develop a sovereign bond market, as access to concessional finance and grants will likely subside with continued increases in national income. Long-term government securities will also facilitate the development of the nascent Cambodian insurance and private pensions industries. The successful first issuance in September 2022 is a welcome step[18].

Authorities' Views

33. The authorities considered ongoing fiscal stimulus important, but with an eye to debt sustainability. The authorities considered that the fiscal stimulus should continue into 2023 to help support the recovery and counter the impact of inflation shocks. The authorities project the fiscal deficit to be slightly lower in 2023 compared to that in the 2022 budget law. The authorities agreed with the need to resume savings over the medium term in line with the new draft Public Finance System Law.[19] The authorities affirmed they are committed to maintain debt sustainability, and to develop the government bond market in a sustainable manner. They will consider a nominal debt target (which would embed a safety margin from the current debt ceiling) but highlighted that the upcoming GDP rebasing would affect several indicators, including not only the debt-to-GDP ratio but also tax revenues to GDP. To help mobilize domestic resources, the authorities will investigate how to rationalize tax exemptions.

Financial and Monetary Frameworks

34. Deeper policy frameworks are needed to safeguard the financial system and protect borrowers:

[18] A fixed coupon bond was issued domestically in September 2022, totaling KHR 41.7 billion (around US$10 million), with a 2 percent coupon rate and one year maturity. Further small issuances are planned.

[19] The new draft Public Finance System Law mandates that, in addition to any annual budget surpluses, 2 to 4 percent of current annual revenue at the national level from the previous year is to be accumulated in a Financial Reserve Fund.

- The authorities should complete the bank restructuring and the deposit insurance legal frameworks and enabling regulations, as the post-pandemic environment might request rapid action on distressed institutions. The authorities should also update the capital regulations in line with recent TA recommendations.

- Similarly, improvements of the corporate insolvency regimes and debt restructuring procedures are needed, both to ensure zombie enterprises are not dragging down growth and to support banks' management of distressed assets.

- The growing importance of residential real estate suggests that the NBC needs better oversight of households' financial burdens. An important first step has been the introduction of a residential real estate price index, following IMF technical assistance (Annex IV). The authorities should begin collecting data on income and collateral of borrowers and macroprudential tools such as debt-service-to-income, debt- to-income, and loan-to-value limits should be developed.

35. Cambodia has made progress in improving its anti-money laundering and combating the financing of terrorism (AML/CFT) framework. Cambodia has been under increased monitoring by the Financial Action Task Force (FATF), which assesses that Cambodia has taken steps towards improving its AML/CFT regime, including by improving the quality and quantity of disseminations by the Cambodian Financial Intelligence Unit and an increase in money laundering investigations. The FATF is now considering the authorities' submission with respect to the freezing and confiscation of criminal proceeds, instrumentalities, and property of equivalent value, to fulfil the last of the items requested by the FATF.

36. A modernized monetary policy framework together with de-dollarization (Annex VI) would improve monetary transmission, and give the NBC more policy options to respond to future economic cycles. Although a more flexible exchange rate regime would offer the potential for more independent monetary policy, more progress on de-dollarization would be needed.[20] Developing market-based monetary policy tools, including an Interest Rate Corridor (IRC), would support the NBC's policy agenda to modernize monetary policy framework and enhance the use of the national currency.[21] Stabilizing short-term money market rates would more easily preserve an interest rate spread that supports the demand for local currency. An improved liquidity management framework would also facilitate de-dollarization.[22]

[20] See the 2021 Article IV Staff Report and annex VI.

[21] The NBC has in place a partial Interest Rate Corridor, having introduced an overnight Marginal Lending Facility (MLF) in September 2021. The MLF increases liquidity of coming government bonds.

[22] The NBC has in place a partial Interest Rate Corridor (IRC), after introducing an overnight Marginal Lending Facility (MLF) in September 2021. By stabilizing short-term money market rates, the central bank with a tightly managed exchange rate can more easily preserve an interest rate spread that supports the demand for local currency vis-à-vis the anchor currency. In addition, an improved liquidity management framework would strengthen local currency usage (de-dollarization) by contributing to a reduction of local currency lending-deposit rates spread.

Authorities' Views

37. The authorities viewed the financial system to be sound and resilient. Banks remained well capitalized and profitable, with low liquidity risks. The authorities noted that they have conducted extensive onsite inspections in many systemic and non-systemic banks and were confident that loans had been classified correctly and that provisioning was adequate. Nevertheless, the authorities agreed that it is important to monitor developments closely and to have a granular approach on monitoring specific entities. The authorities considered that accommodative monetary policy is needed to support growth, as Cambodia is still in the process of recovery, but would closely monitor the financial sector developments, and agreed with the need to gradually return to pre-pandemic policy settings in terms of reserve and capital requirements in the medium term—in particular, the authorities would raise reserve requirements, starting with those in foreign currency.

Governance and Anti-Corruption Frameworks

38. The authorities are taking welcome steps to tackle corruption and strengthen the rule of law, yet vulnerabilities remain (Annex VIII)**.**

- In recent years, Cambodia has adopted a renewed anti-corruption action plan (2020-2025), created an Anti-Corruption Institution (ACI), and has taken steps to improve its legal anti-corruption framework. It has adopted measures toward the preparation of a National Risk Assessment (NRA). Additionally, it has taken measures to improve procurement procedures, and to enhance access to judicial and fiscal information.

- Nonetheless, perceptions remain of substantial weaknesses in rule of law, fair and equal access to the administration of justice, and of corruption (although indicators on the last show some progress). For example, transparency about concessions agreements remains limited, asset declarations are verified when public officials are under investigation rather than being monitored on a permanent basis, and Cambodia does not currently have whistleblower protection and access-to-information laws. Securing sufficient human and technological resources for investigative and monitoring agencies has been challenging.

39. Further improvements to the governance and anti-corruption frameworks would support private investment and national development. To that end, the authorities should, inter alia, adopt measures and tools to increase transparency and access to information (e.g. by improvement and digitization of the asset declaration system and declarations of beneficial ownership of public contracts) and to protect whistleblowers. The authorities should provide more resources and training, and reinforce inter-agency cooperation.

Authorities' Views

40. The authorities considered that much progress had been made in terms of the overall framework, but acknowledged implementation challenges. The appropriate institutions were in place, backed by legislation and rules. However, they acknowledged the challenges of securing human resources, and sought IMF technical assistance on aspects such as government financial systems. Security concerns meant that full digitalization of the asset declaration system would not be appropriate for the Cambodian environment at this stage.

STAFF APPRAISAL

41. The Cambodian economy had been recovering from the pandemic, but has been hit by new challenges in 2022: higher inflation following significant increases in fuel and fertilizer costs; the slowdowns in the economies of the US, Europe, and China; and tighter global financial conditions. There are some signs of scarring from the pandemic, and Cambodia's current account remains substantially weaker than implied by fundamentals and policies, based on 2021 data. The authorities have largely continued with crisis policy responses and have carried on with reforms to strengthen the economy.

42. The recovery is expected to continue but is vulnerable to downside risks. Despite the recent pressures, the baseline projections are for solid growth rates, especially in comparison to other countries. But the recovery remains highly susceptible to a worsening external environment. In addition, some domestic vulnerabilities have increased—although the risks from public debt are low, the level of private debt is very high, raising concerns about the drag on the economy if borrowers struggle to meet repayments.

43. To mitigate the risks from both the external environment and credit risks, the authorities should continue with targeted fiscal support, balanced by normalizing prudential and monetary conditions. Social protection should continue to be used to shield the most vulnerable from inflation and adverse demand shocks. The NBC has taken the welcome step of reintroducing provisioning requirements; it should take a very conservative approach to supervision, and be prepared to raise provisioning and capital requirements for those lenders facing solvency problems.

44. Improvements in policy frameworks can bolster prospects over the medium term. A debt anchor in nominal terms, combined with an overall deficit ceiling, would provide a credible framework, especially important as Cambodia seeks to develop a market for sovereign debt. The potential for high debt levels to persist emphasizes the importance of implementing corporate insolvency, debt and bank restructuring, and deposit protection frameworks.

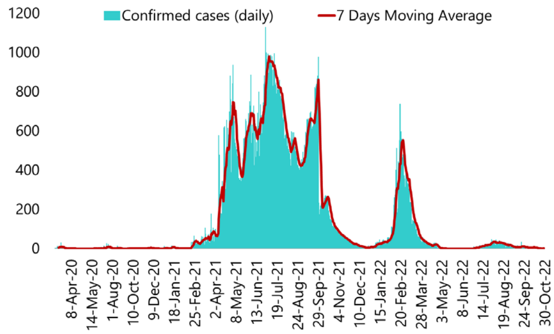
45. The investment environment would benefit from continued efforts on governance. Notable efforts have been made to improve governance frameworks. However, vulnerabilities remain, which would be ameliorated by passage of key legislation, digitization of reporting and monitoring processes, and securing sufficient human and technological resources for investigative and monitoring agencies.

46. It is proposed that the next Article IV consultation with Cambodia be held on the standard 12-month cycle.

Figure 1. Gradual Recovery of the Cambodian Economy

In Q2 2022, Covid-19 cases have plummeted…

Daily Number of COVID-19 Cases in Cambodia



Sources: Cambodia authorities

…as the country fully reopens.

Google mobility tracker

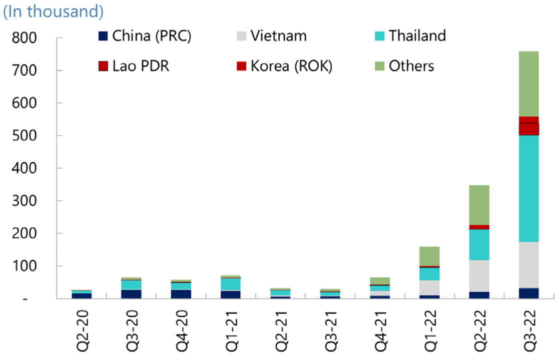
(Percent change from baseline)

Sources: IMF staff calculations based on Google Mobility data.

International arrivals are picking up…

International Tourist Arrival

(In thousand)

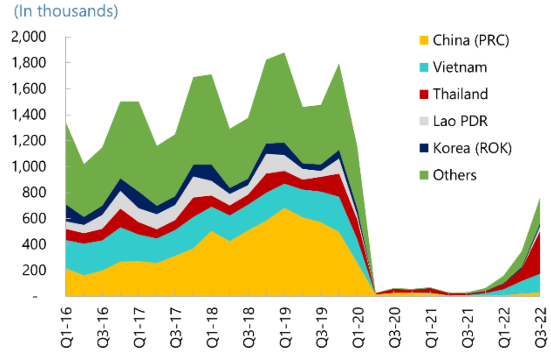


Sources: Cambodia authorities

…while tourism has room to recover further.

International Tourist Arrival

(In thousands)

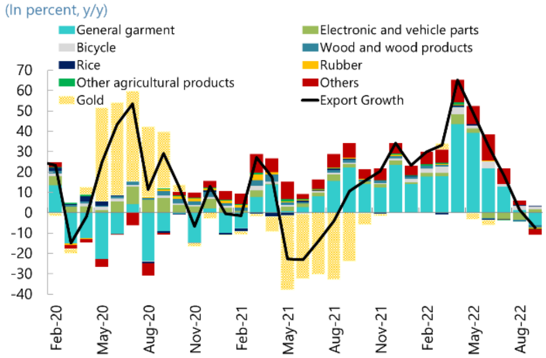


Sources: Cambodia authorities

Garment exports have largely recovered…

Contribution to Export Growth

(In percent, y/y)

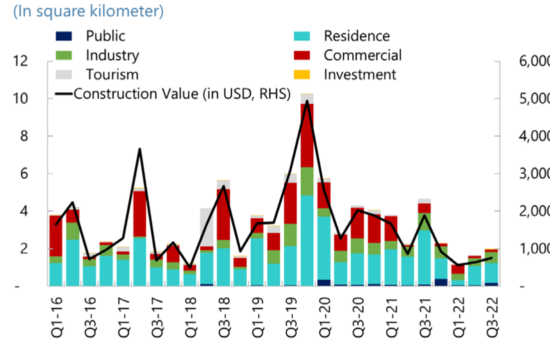


Sources: Cambodia authorities.

…while construction activity remains subdued.

Approved Construction Projects by Area

(In square kilometer)

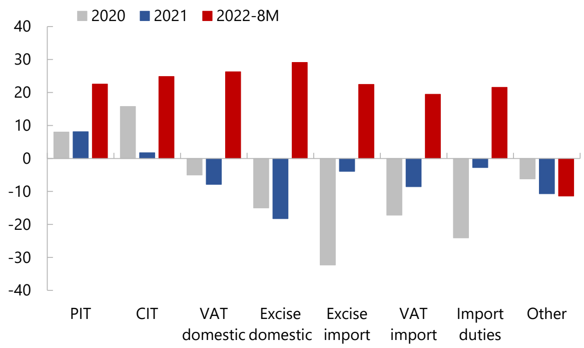


Sources: Cambodia authorities

Figure 2. The Public Finances

A broad-based recovery in tax revenues began in 2022, after a weak performance in 2021

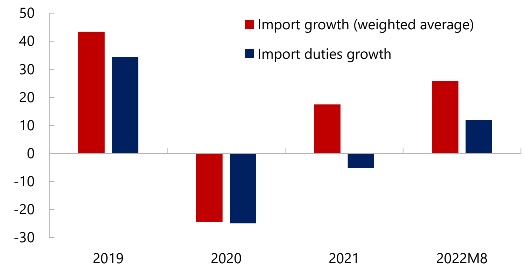
Tax Revenue Growth
(In percent y/y)



Sources: Cambodia authorities; and IMF staff calculations.

and some disconnect in import growth and revenues from imported goods in 2021.

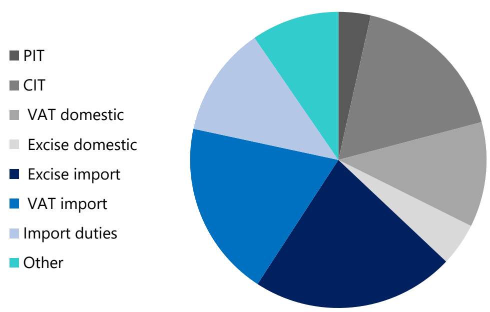
Import Duties vis-a-vis Imports
(In percent)



Sources: Cambodia authorities; and IMF staff calculations.
Note: Import growth is the weighted average import of vehicles, fuel, food and construction materials using 2019 import duties revenue weights of vehicles, fuel, food and construction materials as proxy weights.

Revenue reliance on imported goods is significant, with VAT and excises on imports almost threefold compared to domestic goods.

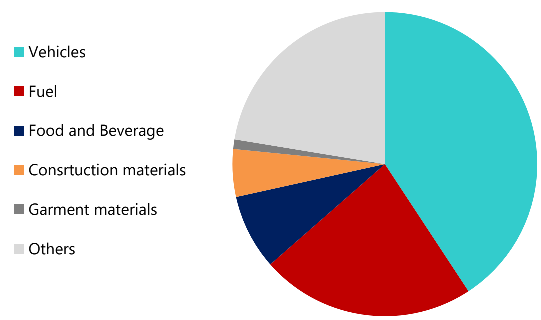
Pre-Pandemic Tax Revenue Composition, 2019
(Share of total)



Sources: Cambodia authorities; and IMF staff calculations.

Furthermore, import duties are concentrated on a few goods, including vehicles and fuel.

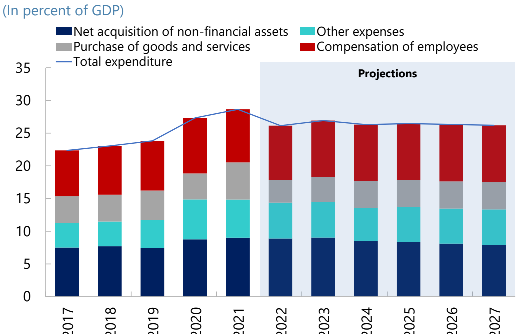
Pre-pandemic Import Duties Composition, 2019
(In percent of total)



Sources: Cambodia authorities; and IMF staff calculations.
Note: Import duties includes VAT, Excises and Tariffs.

Meanwhile spending pressures continued in 2021, but with higher healthcare measures.

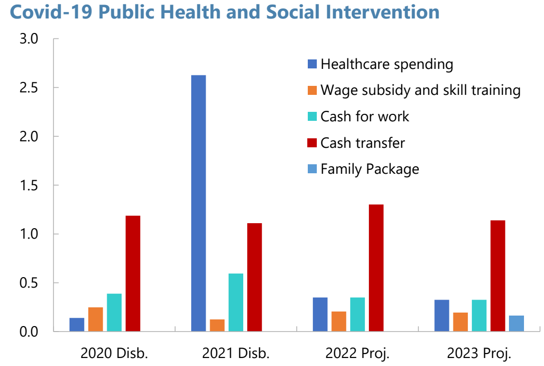
Government Spending
(In percent of GDP)



Sources: Cambodia authorities; and IMF staff calculations.

Going forward, Covid-19 intervention measures are being slowly waned, but with planned interventions in 2022 still larger than in 2020.

Covid-19 Public Health and Social Intervention

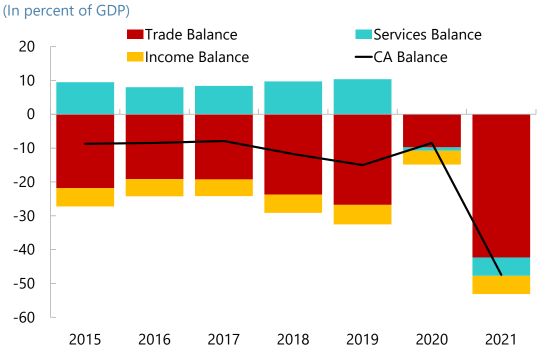


Sources: Cambodia authorities and IMF staff calculations.

Figure 3. External Balances

Current account deficit widened significantly in 2021, reflecting subdued tourism receipts,

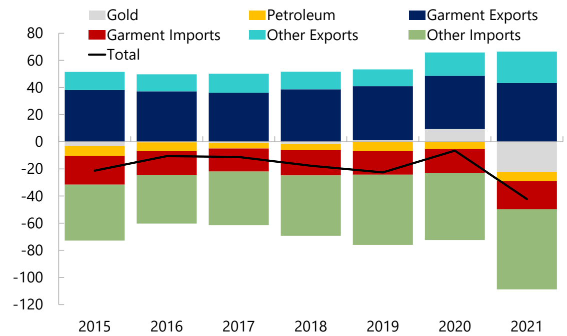
Current Account Balance
(In percent of GDP)



Sources: Cambodia authorities
Note: Income balance includes official transfers.

... and to a larger extent surging gold imports.

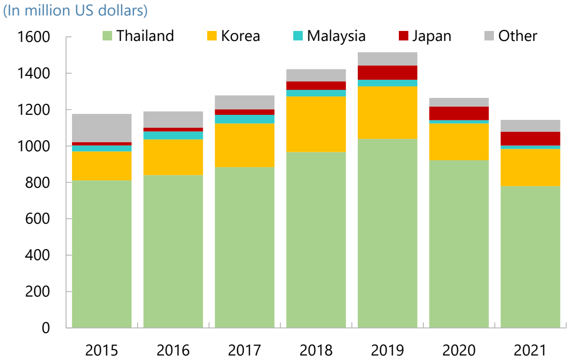
Trade Balance and Main Items
(in percent of GDP; exports (+), imports (-))



Sources: Cambodia authorities

Remittance income also remained relatively low.

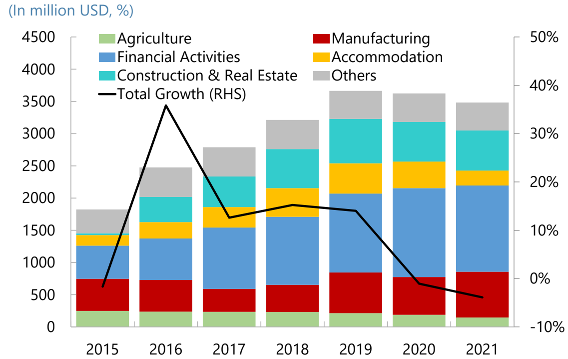
Remittances by Country
(In million US dollars)



Sources: Cambodia authorities

FDI inflows to manufacturing industries recovered somewhat, but inflows to service sectors slowed.

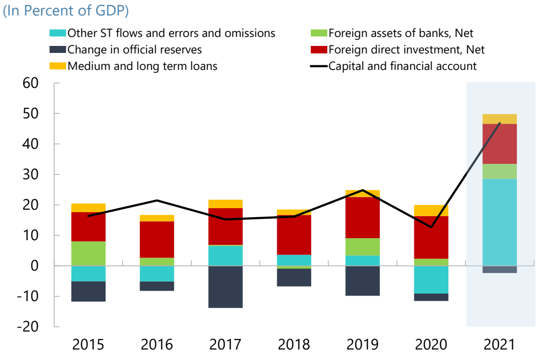
FDI Inflows by Sector
(In million USD, %)



Sources: Cambodia authorities

Short term capital inflows, on the other hand, skyrocketed,

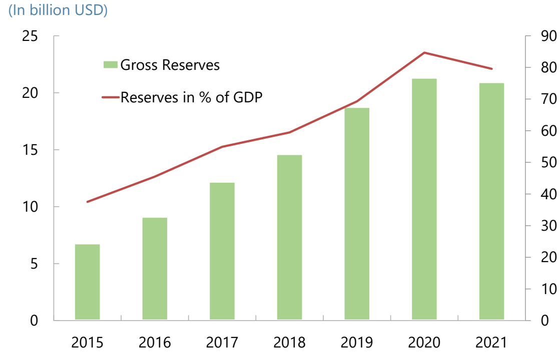
Current Account Financing
(In Percent of GDP)



Sources: Cambodian authorities; and IMF staff calculations.

...which partially offset the large current account deficit, resulting in a modest decline in reserve coverage.

International Reserves
(In billion USD)



Sources: Cambodia authorities

Table 1. Cambodia: Selected Economic Indicators, 2019 – 23

Per capita GDP (2021, US$) : 1,648 | Life expectancy (2019, years) : 75.5
Population (2021, million) : 16.3 | Literacy rate (2019, percent) : 87.7

	2019	2020	2021	2022	2023
			Est.	Proj.	
Output and prices (annual percent change)					
GDP in constant prices	7.1	-3.1	3.0	5.0	5.4
Inflation (end-year)	3.1	2.9	3.7	5.8	3.5
(Annual average)	1.9	2.9	2.9	5.8	3.5
Saving and investment balance (in percent of GDP)					
Gross national saving	9.2	16.4	-22.0	-5.0	10.9
Government saving	8.4	3.4	0.4	3.1	4.1
Private saving	0.8	13.0	-22.3	-8.1	6.9
Gross fixed investment	24.2	24.9	25.5	25.0	25.0
Government investment	7.4	8.8	9.0	8.9	9.0
Private investment	16.8	16.1	16.5	16.1	16.0
Money and credit (annual percent change, unless otherwise indicated)					
Broad money	18.2	15.3	16.3	18.5	12.6
Private sector credit	28.0	17.2	23.4	18.0	15.0
Velocity of money 1/	0.9	0.8	0.7	0.6	0.6
Public finance (in percent of GDP)					
Revenue	26.8	23.9	21.6	22.1	22.0
Domestic revenue	24.8	22.0	20.0	21.4	21.1
Of which: Tax revenue	21.7	19.7	18.0	19.4	19.1
Grants	2.0	1.9	1.6	0.7	0.8
Expenditure	23.8	27.3	28.6	26.1	26.9
Expense	16.4	18.6	19.6	17.3	17.9
Net acquisition of nonfinancial assets	7.4	8.8	9.0	8.9	9.0
Net lending (+)/borrowing(-)	3.0	-3.4	-7.1	-4.1	-5.0
Net lending (+)/borrowing(-) excluding grants	1.0	-5.3	-8.6	-4.8	-5.8
Net acquisition of financial assets	8.8	0.6	-4.0	-1.1	-1.7
Net incurrence of liabilities 2/	5.8	4.0	3.0	3.0	3.3
Balance of payments (in millions of dollars, unless otherwise indicated)					
Exports, f.o.b.	14,998	18,470	19,469	22,062	24,061
(Annual percent change)	15.6	23.2	5.4	13.3	9.1
Imports, f.o.b.	-22,251	-20,993	-30,726	-29,340	-28,220
(Annual percent change)	18.3	-5.7	46.4	-4.5	-3.8
Current account (including official transfers)	-4,067	-2,182	-12,624	-8,587	-4,318
(In percent of GDP)	-15.0	-8.5	-47.5	-30.0	-14.1
Gross official reserves 3/	18,763	21,334	20,941	20,747	22,304
(In months of prospective imports)	9.8	7.8	7.8	8.0	8.1
External debt (in millions of dollars, unless otherwise indicated)					
Public external debt	7,596	8,810	9,493	10,284	11,086
(In percent of GDP)	28.2	34.4	35.9	36.1	36.3
Public debt service	309	360	384	408	426
(In percent of exports of goods and services)	1.5	1.8	1.9	1.7	1.6
Memorandum items:					
Nominal GDP (in billions of Riels)	110,014	105,892	110,506	120,315	130,477
(In millions of U.S. dollars)	27,087	25,771	26,601	28,647	30,729
Exchange rate (Riels per dollar; period average)	4,062	4,109	4,154	..	..

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

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

2/ Includes statistical discrepancy.

3/ Includes unrestricted foreign currency deposits held at the National Bank of Cambodia.

Table 2. Cambodia: Medium-Term Macroeconomics Framework, 2019–27

	2019	2020	2021	2022	2023	2024	2025	2026	2027
			Est.			Proj.			
Output and prices (percent change)									
GDP at constant prices	7.1	-3.1	3.0	5.0	5.4	6.1	6.4	6.5	6.6
GDP deflator	3.2	-0.7	1.3	3.7	2.9	2.4	2.6	2.7	2.6
Consumer prices (end-year)	3.1	2.9	3.7	5.8	3.5	3.0	3.0	3.0	3.0
Consumer prices (average)	1.9	2.9	2.9	5.8	3.5	3.0	3.0	3.0	3.0
Saving and investment balance (in percent of GDP)									
Gross national saving	9.2	16.4	-22.0	-5.0	9.1	13.1	17.0	18.4	19.5
Government saving	8.4	3.4	0.4	4.1	3.2	4.2	4.5	4.6	4.6
Private saving	0.8	13.0	-22.3	-9.1	5.9	8.9	12.5	13.8	14.8
Gross fixed investment	24.2	24.9	25.5	25.0	23.2	23.0	24.0	25.0	26.0
Government investment	7.4	8.8	9.0	8.9	9.0	8.5	8.4	8.1	7.9
Private investment 1/	16.8	16.1	16.5	16.1	14.2	14.5	15.6	16.9	18.1
Private credit growth (percent change)	28.0	17.2	23.4	18.0	15.0	13.0	13.5	13.5	13.5
Public finance (in percent of GDP)									
Revenue	26.8	23.9	21.6	22.1	22.0	22.9	23.4	23.5	23.5
Of which: Tax revenue	21.7	19.7	18.0	19.4	19.1	19.9	20.6	20.8	20.9
Grants	2.0	1.9	1.6	0.7	0.8	0.9	0.7	0.6	0.6
Total expenditure	23.8	27.3	28.6	26.1	26.9	26.3	26.5	26.3	26.2
Expense	16.4	18.6	19.6	17.3	17.9	17.8	18.1	18.2	18.3
Net acquisition of nonfinancial assets	7.4	8.8	9.0	8.9	9.0	8.5	8.4	8.1	7.9
Net lending (+)/borrowing(-)	3.0	-3.4	-7.1	-4.1	-5.0	-3.4	-3.1	-2.9	-2.7
Net lending (+)/borrowing(-) excluding grants	1.0	-5.3	-8.6	-4.8	-5.8	-4.3	-3.9	-3.5	-3.3
Net acquisition of financial assets	8.8	0.6	-4.0	-1.1	-1.7	0.2	0.3	0.5	0.6
Net incurrence of liabilities	5.8	4.0	3.0	3.0	3.3	3.6	3.4	3.4	3.3
Government deposits	22.2	23.7	17.7	15.1	12.3	11.4	10.8	10.4	10.1
Balance of payments (in percent of GDP, unless otherwise indicated)									
Exports (percent change) 2/	15.6	23.2	5.4	13.3	9.1	9.2	9.1	8.5	8.5
Imports (percent change) 3/	18.3	-5.7	46.4	-4.5	-3.8	6.5	7.2	8.8	8.6
Current account balance (including transfers)	-15.0	-8.5	-47.5	-30.0	-14.1	-9.9	-7.0	-6.6	-6.5
(Excluding transfers)	-17.0	-10.2	-49.5	-32.0	-16.0	-11.8	-8.8	-8.3	-8.3
Foreign direct investment	13.5	14.0	13.1	12.8	12.5	12.2	11.9	11.5	11.2
Other flows	11.4	-3.1	33.6	14.4	6.6	3.1	0.9	0.9	1.0
Overall balance	9.9	2.5	-0.8	-2.8	5.0	5.4	5.8	5.9	5.6
Gross official reserves (in millions of U.S. dollars) 4/	18,763	21,334	20,941	20,747	22,304	24,096	26,171	28,463	30,829
(In months of next year's imports)	9.8	7.8	7.8	8.0	8.1	8.1	8.1	8.1	8.1
Public external debt (in millions of U.S. dollars)	7,596	8,810	9,493	10,284	11,086	12,021	12,963	13,983	15,054
(In percent of GDP)	28.2	34.4	35.9	36.1	36.3	36.6	36.5	36.4	36.3
Public external debt service (in millions of U.S. dollar	309	360	384	408	426	445	464	481	503
(In percent of exports of goods and services)	1.5	1.8	1.9	1.7	1.6	1.5	1.4	1.3	1.3

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/ Includes unrestricted foreign currency deposits held at the National Bank of Cambodia.

Table 3a. Cambodia: Balance of Payments, 2019–27 (BPM5)

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

	2019	2020	2021	2022	2023	2024	2025	2026	2027
			Est.			Proj.			
Current account (including official transfers)	-4,067	-2,182	-12,624	-8,587	-4,318	-3,268	-2,483	-2,537	-2,720
(Excluding official transfers)	-4,598	-2,629	-13,175	-9,166	-4,924	-3,903	-3,150	-3,221	-3,460
Trade balance	-7,253	-2,522	-11,257	-7,279	-4,159	-3,781	-3,561	-3,960	-4,332
Exports, f.o.b.	14,998	18,470	19,469	22,062	24,061	26,263	28,654	31,090	33,733
Of which: Garments	10,800	9,839	11,390	12,554	13,552	14,622	15,782	16,962	18,231
Imports, f.o.b. 1/	-22,251	-20,993	-30,726	-29,340	-28,220	-30,044	-32,215	-35,050	-38,064
Of which: Garments-related	-4,282	-4,020	-5,049	-6,905	-8,063	-8,992	-9,706	-10,431	-11,212
Petroleum	-2,426	-2,057	-2,930	-4,847	-4,674	-4,648	-4,740	-4,941	-5,255
Services and income (net)	1,244	-1,308	-2,874	-2,892	-1,719	-1,124	-641	-366	-288
Services (net)	2,808	-261	-1,447	-1,441	-213	452	1,013	1,374	1,547
Of which: Tourism (credit)	4,770	1,015	184	497	1,242	2,236	2,907	3,431	3,774
Income (net)	-1,564	-1,047	-1,428	-1,450	-1,505	-1,576	-1,654	-1,740	-1,834
Private transfers (net)	1,411	1,201	957	1,005	954	1,002	1,052	1,105	1,160
Official transfers (net)	531	447	551	579	606	635	668	684	739
Capital and financial account	6,727	3,258	12,462	7,779	5,859	5,045	4,542	4,813	5,069
Medium- and long-term loans (net)	613	939	857	789	798	932	938	1,017	1,067
Disbursements	831	1,213	1,154	1,120	1,142	1,282	1,294	1,376	1,433
Amortization	-224	-275	-297	-331	-344	-350	-356	-359	-365
Foreign direct investment 2/	3,663	3,612	3,484	3,659	3,842	4,034	4,235	4,447	4,669
Net foreign assets of deposit money banks	1,530	596	1,309	1,000	500	50	-100	-100	-100
Other short-term flows	566	-2,148	6,568	2,100	500	-180	-720	-720	-720
Errors and omissions	17	-441	-47	0	0	0	0	0	0
Overall balance	2,676	636	-210	-808	1,542	1,777	2,059	2,276	2,349
Financing	-5,360	-4,731	406	808	-1,542	-1,777	-2,059	-2,276	-2,349
Change in gross official reserves 3/	-2,676	-635	-636	372	-1,556	-1,793	-2,075	-2,292	-2,366
Memorandum items:									
Current account balance (in percent of GDP)									
Excluding official transfers	-17.0	-10.2	-49.5	-32.0	-16.0	-11.8	-8.8	-8.3	-8.3
Including official transfers	-15.0	-8.5	-47.5	-30.0	-14.1	-9.9	-7.0	-6.6	-6.5
Trade balance (in percent of GDP)	-26.8	-9.8	-42.3	-25.4	-13.5	-11.4	-10.0	-10.3	-10.4
Gross official reserves 4/	18,763	21,334	20,941	20,747	22,304	24,096	26,171	28,463	30,829
(In months of next year's imports)	9.8	7.8	7.8	8.0	8.1	8.1	8.1	8.1	8.1

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

4/ Includes unrestricted FCDs held at the NBC.

Table 3b. Cambodia: Balance of Payments, 2019–27 (BPM5)

(In percent of GDP, unless otherwise indicated)

	2019	2020	2021	2022	2023	2024	2025	2026	2027
			Est.			Proj.			
Current account (including official transfers)	-15.0	-8.5	-47.5	-30.0	-14.1	-9.9	-7.0	-6.6	-6.5
(Excluding official transfers)	-17.0	-10.2	-49.5	-32.0	-16.0	-11.8	-8.8	-8.3	-8.3
Trade balance	-26.8	-9.8	-42.3	-25.4	-13.5	-11.4	-10.0	-10.3	-10.4
Exports, f.o.b.	55.4	71.7	73.2	77.0	78.3	79.5	80.3	80.6	80.8
Of which: Garments	39.9	38.2	42.8	43.8	44.1	44.2	44.2	44.0	43.7
Imports, f.o.b. 1/	-82.1	-81.5	-115.5	-102.4	-91.8	-90.9	-90.3	-90.8	-91.2
Of which: Garments-related	-15.8	-15.6	-19.0	-24.1	-26.2	-27.2	-27.2	-27.0	-26.9
Petroleum	-9.0	-8.0	-11.0	-16.9	-15.2	-14.1	-13.3	-12.8	-12.6
Services and income (net)	4.6	-5.1	-10.8	-10.1	-5.6	-3.4	-1.8	-0.9	-0.7
Services (net)	10.4	-1.0	-5.4	-5.0	-0.7	1.4	2.8	3.6	3.7
Of which: Tourism (credit)	17.6	3.9	0.7	1.7	4.0	6.8	8.2	8.9	9.0
Income (net)	-5.8	-4.1	-5.4	-5.1	-4.9	-4.8	-4.6	-4.5	-4.4
Private transfers (net)	5.2	4.7	3.6	3.5	3.1	3.0	2.9	2.9	2.8
Official transfers (net)	2.0	1.7	2.1	2.0	2.0	1.9	1.9	1.8	1.8
Capital and financial account	24.8	12.6	46.8	27.2	19.1	15.3	12.7	12.5	12.1
Medium- and long-term loans (net)	2.3	3.6	3.2	2.8	2.6	2.8	2.6	2.6	2.6
Disbursements	3.1	4.7	4.3	3.9	3.7	3.9	3.6	3.6	3.4
Amortization	-0.8	-1.1	-1.1	-1.2	-1.1	-1.1	-1.0	-0.9	-0.9
Foreign direct investment 2/	13.5	14.0	13.1	12.8	12.5	12.2	11.9	11.5	11.2
Net foreign assets of deposit money banks	5.6	2.3	4.9	3.5	1.6	0.2	-0.3	-0.3	-0.2
Other short-term flows	2.1	-8.3	24.7	7.3	1.6	-0.5	-2.0	-1.9	-1.7
Errors and omissions	0.1	-1.7	-0.2	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	9.9	2.5	-0.8	-2.8	5.0	5.4	5.8	5.9	5.6
Financing	-19.8	-18.4	1.5	2.8	-5.0	-5.4	-5.8	-5.9	-5.6
Change in gross official reserves 3/	-9.9	-2.5	-2.4	1.3	-5.1	-5.4	-5.8	-5.9	-5.7
Memorandum items:									
Current account balance (in percent of GDP)									
Excluding official transfers	-17.0	-10.2	-49.5	-32.0	-16.0	-11.8	-8.8	-8.3	-8.3
Including official transfers	-15.0	-8.5	-47.5	-30.0	-14.1	-9.9	-7.0	-6.6	-6.5
Trade balance (in percent of GDP)	-26.8	-9.8	-42.3	-25.4	-13.5	-11.4	-10.0	-10.3	-10.4
Gross official reserves 4/	69.3	82.8	78.7	72.4	72.6	72.9	73.4	73.8	73.9
(In months of next year's imports)	9.8	7.8	7.8	8.0	8.1	8.1	8.1	8.1	8.1

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

4/ Includes unrestricted FCDs held at the NBC.

Table 4. Cambodia: General Government Operations, 2019 – 2027 (GFSM 2014)

	2019	2020	2021	2022		2023	2024	2025	2026	2027
			Est.	Budget	Est.			Proj.		
Revenue	29,461	25,335	23,842	24,785	26,552	28,645	32,458	36,157	39,728	43,442
Of which: Nongrant	27,251	23,291	22,112	23,769	25,729	27,575	31,173	35,001	38,688	42,401
Tax	23,822	20,882	19,875	21,493	23,293	24,931	28,298	31,863	35,256	38,649
Income, profits, and capital gains	5,467	6,110	6,219	5,763	7,836	8,498	9,240	10,386	11,360	12,296
Good and services	15,280	12,399	11,343	13,173	12,931	14,023	16,467	18,650	20,806	22,976
International trade and transactions	2,897	2,198	2,131	2,394	2,344	2,389	2,572	2,807	3,070	3,356
Grants	2,210	2,044	1,730	1,016	823	1,070	1,284	1,156	1,040	1,040
Other revenues	3,430	2,409	2,237	2,276	2,436	2,644	2,875	3,138	3,432	3,752
Total expenditure	26,202	28,935	31,649	31,515	31,459	35,128	37,326	40,977	44,588	48,506
Expense	18,040	19,659	21,680	19,882	20,756	23,335	25,212	28,015	30,857	33,814
Compensation of employees	8,355	8,992	8,967	9,957	9,957	11,252	12,234	13,351	14,748	16,125
Purchase of goods and services	4,984	4,199	6,266	4,207	4,207	5,019	5,894	6,432	7,035	7,692
Interest	367	381	403	646	321	363	467	588	713	856
Expense not elsewhere classified	4,335	6,087	6,044	5,071	6,271	6,701	6,617	7,644	8,360	9,141
Net acquisition of nonfinancial assets	8,161	9,277	9,969	11,633	10,703	11,793	12,114	12,962	13,731	14,692
Of which: Externally financed	4,667	5,857	5,250	…	4,099	4,422	5,243	5,184	5,454	5,724
Net lending (+)/borrowing(-)	3,260	-3,601	-7,807	-6,730	-4,907	-6,483	-4,868	-4,820	-4,860	-5,064
Net acquisition of financial assets	9,638	672	-4,461	-212	-1,331	-2,218	225	447	908	1,101
Net incurrence of liabilities	6,378	4,273	3,345	5,947	3,576	4,265	5,093	5,267	5,768	6,165
Of which: External	4,667	5,857	3,520	4,728	3,276	3,352	3,958	4,028	4,413	4,684
Revenue	26.8	23.9	21.6	20.6	22.1	22.0	22.9	23.4	23.5	23.5
Nongrant	24.8	22.0	20.0	19.8	21.4	21.1	22.0	22.6	22.8	22.9
Tax	21.7	19.7	18.0	17.9	19.4	19.1	19.9	20.6	20.8	20.9
Income, profits, and capital gains tax	5.0	5.8	5.6	4.8	6.5	6.5	6.5	6.7	6.7	6.6
Good and services tax	13.9	11.7	10.3	10.9	10.7	10.7	11.6	12.0	12.3	12.4
International trade and transactions tax	2.6	2.1	1.9	2.0	1.9	1.8	1.8	1.8	1.8	1.8
Grants	2.0	1.9	1.6	0.8	0.7	0.8	0.9	0.7	0.6	0.6
Other revenues	3.1	2.3	2.0	1.9	2.0	2.0	2.0	2.0	2.0	2.0
Total expenditure	23.8	27.3	28.6	26.2	26.1	26.9	26.3	26.5	26.3	26.2
Expense	16.4	18.6	19.6	16.5	17.3	17.9	17.8	18.1	18.2	18.3
Compensation of employees	7.6	8.5	8.1	8.3	8.3	8.6	8.6	8.6	8.7	8.7
Purchase of goods and services	4.5	4.0	5.7	3.5	3.5	3.8	4.2	4.2	4.2	4.2
Interest	0.3	0.4	0.4	0.5	0.3	0.3	0.3	0.4	0.4	0.5
Expense not elsewhere classified	3.9	5.7	5.5	4.2	5.2	5.1	4.7	4.9	4.9	4.9
Net acquisition of nonfinancial assets	7.4	8.8	9.0	9.7	8.9	9.0	8.5	8.4	8.1	7.9
Of which: Externally-financed	4.2	5.5	4.8	…	3.4	3.4	3.7	3.3	3.2	3.1
Net lending (+)/borrowing(-)	3.0	-3.4	-7.1	-5.6	-4.1	-5.0	-3.4	-3.1	-2.9	-2.7
Net acquisition of financial assets	8.8	0.6	-4.0	-0.2	-1.1	-1.7	0.2	0.3	0.5	0.6
Net incurrence of liabilities	5.8	4.0	3.0	4.9	3.0	3.3	3.6	3.4	3.4	3.3
Of which: External	4.2	5.5	3.2	3.9	2.7	2.6	2.8	2.6	2.6	2.5
Memorandum items:										
Net lending (+)/borrowing(-) excluding grant	1.0	-5.3	-8.6	-6.4	-4.8	-5.8	-4.3	-3.9	-3.5	-3.3
Government deposits	22.2	23.7	17.7	…	15.1	12.3	11.4	10.8	10.4	10.1
GDP (in billions of riels)	110,014	105,892	110,506	…	120,315	130,477	141,863	154,819	169,331	185,140

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

Table 5. Cambodia: Monetary Survey, 2019–23

	2019	2020	2021	2022	2023
				Proj.	
			(In billions of Riels)		
Net foreign assets	60,182	67,364	57,006	61,678	74,407
National Bank of Cambodia	76,931	86,782	83,989	90,399	104,766
Foreign assets	76,457	86,292	82,553	88,963	103,330
Foreign liabilities	-474	-490	-1,436	-1,436	-1,436
Deposit money banks	-15,801	-18,439	-24,111	-25,849	-27,487
Foreign assets	15,339	16,662	17,511	15,479	13,759
Foreign liabilities	-31,140	-35,100	-41,622	-41,328	-41,247
Net domestic assets	58,254	69,178	101,733	126,451	137,390
Domestic credit	106,133	127,353	168,496	203,764	238,102
Government (net)	-23,884	-24,995	-19,540	-18,066	-17,003
Private sector	130,017	152,347	188,035	221,830	255,104
Other items (net)	-47,879	-58,175	-66,763	-77,313	-100,712
Broad money	118,436	136,542	158,739	188,128	211,797
Narrow money	13,513	15,091	16,918	20,863	23,487
Currency in circulation	11,906	13,474	14,596	18,158	20,442
Demand deposits	1,607	1,617	2,322	2,705	3,045
Quasi-money	104,923	121,451	141,821	167,266	188,310
Time deposits	5,301	6,902	10,133	12,982	14,616
Foreign currency deposits	99,622	114,549	131,688	154,283	173,694
			(12-month percentage change)		
Net foreign assets	23.1	11.9	-15.4	8.2	20.6
Private sector credit	28.0	17.2	23.4	18.0	15.0
Broad money	18.2	15.3	16.3	18.5	12.6
Of which: Currency in circulation	32.1	13.2	8.3	24.4	12.6
Foreign currency deposits	16.1	15.0	15.0	17.2	12.6
			(Contribution to year-on-year growth of broad money, in percentage points)		
Net foreign assets	11.3	6.1	-7.6	2.9	6.8
Net domestic assets	6.9	9.2	23.8	15.6	5.8
Domestic credit 1/	20.7	17.9	30.1	22.2	18.3
Government (net)	-7.6	-0.9	4.0	0.9	0.6
Private sector	28.4	18.9	26.1	21.3	17.7
Other items (net)	-13.9	-8.7	-6.3	-6.6	-12.4
Memorandum items:					
Foreign currency deposits (in millions of U.S. dollars)	24,378	27,726	31,528	36,535	40,685
(In percent of broad money)	84.1	83.9	83.0	82.0	82.0
Riel component of broad money	18,814	21,993	27,051	33,845	38,103
(In percent of broad money)	15.9	16.1	17.0	18.0	18.0
Credit to the private sector (in millions of U.S. dollars)	31,816	36,875	45,018	52,531	59,753
(In percent of GDP)	118.2	143.9	170.2	184.4	195.5
Foreign currency loans-to-total loans (in percent)	87.9	87.4	87.8	87.8	87.8
Loan-to-deposit ratio (in percent) 2/	114.7	116.2	125.4	126.3	129.0
Velocity 3/	0.9	0.8	0.7	0.6	0.6
Money multiplier (broad money/reserve money)	2.7	3.2	3.3	3.2	3.2
Reserve money (12-month percent change)	0.3	0.0	0.1	0.2	0.1

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

1/ Excludes banks' credits to nonresident.

2/ Foreign currency loans and deposits only.

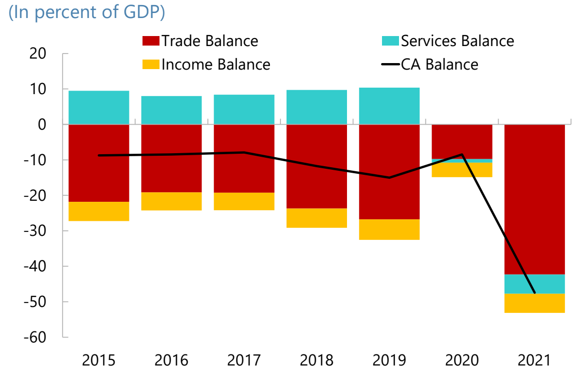
3/ The ratio of nominal GDP to the year-to-date average stock of broad money.

Annex I. External Sector Assessment

Staff assesses that Cambodia's external position in 2021 remains substantially weaker than the level implied by medium-term fundamentals and desirable policies after adjusting for temporary factors; a surge in gold imports while tourism receipts and remittance income remained sluggish. Short-term capital inflows soared, bringing the financial balance to historic highs. As a result, reserves coverage declined only modestly despite the sizable current account deficit.

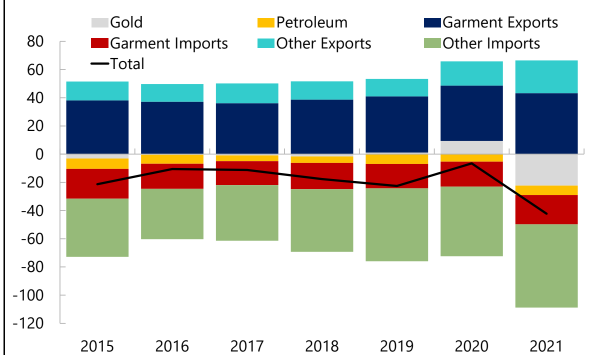
1. The current account deficit widened substantially in 2021, largely reflecting a surge in gold imports. The current account deficit was 48 percent GDP at the end of 2021, over five times of the deficit in 2020. Gold imports accounted for almost half of the total current account deficit. The increase in energy prices also contributed to the deficit, with a large increase in the value of petroleum imports. Trade—both exports and imports—of major manufacturing goods (e.g. textiles, electronics) saw a solid recovery. As a result, the trade balance excluding gold declined only modestly. Service trade remained sluggish because of weak tourism, and remittances and other private transfers continued to decline.

Current Account Balance
(In percent of GDP)



Sources: Cambodia authorities
Note: Income balance includes official transfers.

Trade Balance and Main Items
(In percent of GDP; exports (+), import (-))

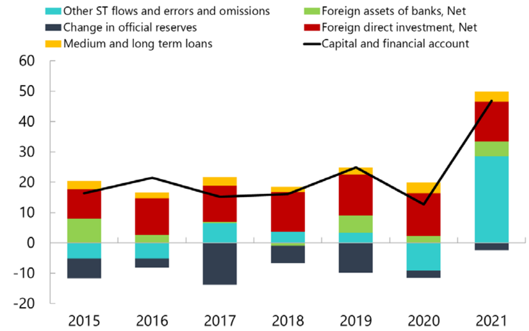


Sources: Cambodia authorities

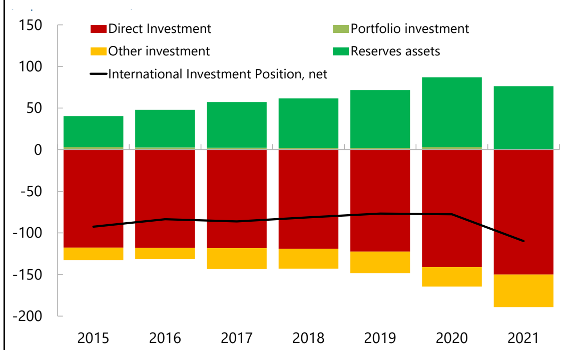
2. The financial account increased significantly (to 47 percent of GDP) in 2021, largely reflecting bank financing and other short-term capital inflows. Short-term capital increased to a net inflow of 25 percent of GDP in 2021 from a net outflow of -8 percent of GDP in 2020. Medium-to-long term loans remained broadly stable. Favorable external financing conditions partly contributed to rising financial inflows through bank borrowings, but a large part of the short-term capital inflows was recorded as other investment, hence the source and nature of the inflows are not clearly identified. Despite some recovery of FDI in manufacturing industries, service sectors (especially hotels and restaurants) continued to see declines in inward foreign investment. The net foreign asset (NFA) position decreased from -77 percent of GDP in 2020 to -111 percent of GDP by end-2021, reflecting increasing FDI liabilities and bank and other short-term liabilities. Over the medium term, Cambodia's NFA position is projected to trend downward, in line with recovery of FDI inflows partly offset by reserves accumulation.

Current Account Financing

Net Foreign Assets



Sources: Cambodia authorities



Sources: Cambodia authorities

3. The external position is assessed to be substantially weaker than implied by fundamentals and desirable policies. The current account deficit widened to -48 percent of GDP in 2021, of which 22 percent of GDP was driven by gold imports. Rising fuel prices also contributed to the higher deficit. Recent data suggests that gold imports in the first three months of 2022 are about 50 percent less than the same period last year. On this basis, gold imports are assessed to be partially temporary, and the current account deficit is adjusted by half of total gold imports, lowering the deficit by 11 percentage points. Along with cyclical adjustments to account for weaker terms of trade, the larger output gap, Covid-19-related tourism losses and medical imports, and natural disasters, the current account deficit in 2021 is adjusted to -25 percent. Comparing to the current norm of -7.6 percent of GDP, the current account gap is -17.3 percent of GDP, equivalent to a real exchange rate overvaluation of about 29 percent. The real exchange rate model also points to the same conclusion, with an estimated gap of -16 percent of GDP.

Cambodia: EBA-lite Model Results, 2021

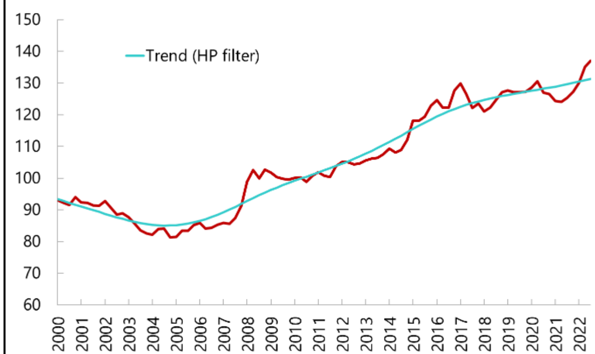
	CA model 1/	**REER model** 1/
	(in percent of GDP)	
CA-Actual	**-47.5**	
Cyclical contributions (from model) (-)	-3.3	
COVID-19 adjustor (-) 2/	-6.7	
Additional temporary/statistical factors (-)	-11.1	
Natural disasters and conflicts (-)	-1.3	
Adjusted CA	**-24.9**	
CA Norm (from model) 3/	**-7.6**	
Adjustments to the norm (-)	0.0	
Adjusted CA Norm	**-7.6**	
CA Gap	**-17.3**	**-16.2**
o/w Relative policy gap	1.3	
Elasticity	-0.60	
REER Gap (in percent)	**28.8**	**27.0**

1/ Based on the EBA-lite 3.0 methodology
2/ Additional cyclical adjustment to account for the temporary impact of the tourism (4.9 percent of GDP) and medical goods (1.8 percernt of GDP). The latter accounts for the large temporary increase in medical goods imports (medical goods exports are assessed to be negligible).
3/ Cyclically adjusted, including multilateral consistency adjustments.

4. The external sector assessment faces large uncertainties. Gold trade has been highly volatile during the pandemic: Cambodian exported gold in 2020, and then switched to importing gold in 2021. The gold imports have continued, albeit at a slower pace in early 2022, despite increases in the price of gold. Hence the estimated current account gap is subject to large uncertainties. The estimated gap can range from -8.4 to -31 percent of GDP assuming gold imports are entirely temporary or permanent respectively. However, the assumptions do not change the qualitative assessment that Cambodia's external position is substantially weaker than the implied fundamentals and desirable policies—that is, the same assessment would be reached based on the current account balance in 2021 completely excluding gold flows.

5. The trend appreciation in the real effective exchange rate has slowed down. The real exchange rate had appreciated by 4 percent annually over the decade before the pandemic. The appreciation trend was temporary disrupted by the (nominal) depreciation of the US dollar in 2020. In 2021, the real exchange rate appreciated again, by about 4 precent. The appreciation has resumed 2022 until its third quarter, reflecting capital inflows.

Real Effective Exchange Rate, 2000Q1—2022Q3 (2010=100)

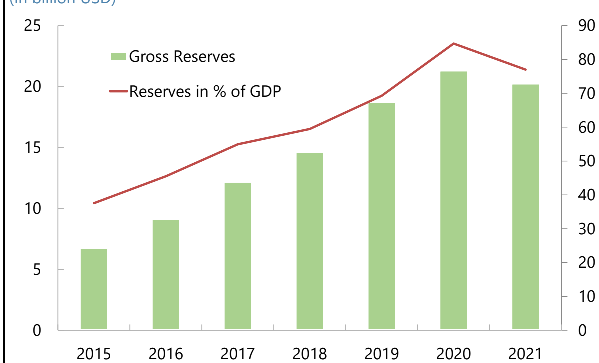


Sources: INS; and IMF staff calculations.

6. International reserves are broadly adequate. The current account deficit in 2021 was mostly, but not fully, offset by similar magnitude of capital inflows along with valuation effects stemming from non-US$-denominated assets. Gross reserves therefore decreased slightly, by US$0.4 billion. Reserves were 80 percent of estimated 2021 GDP. This corresponds to close to 8 months of prospective imports, which is higher than the optimal level of 4 month of imports as implied by the ARA tool for credit-constrained economies. Although the current level of reserves is adequate, a high level of international reserves remains advisable, as Cambodia is a highly export-dependent economy, operating in a fixed-exchange rate regime with a high degree of dollarization.

International Reserves

(In billion USD)



Sources: Cambodia authorities

Annex II. Risk Assessment Matrix[1]

Nature/source of the shock	Likelihood	Impact	Policies to minimize impact
		Conjunctural risks and scenarios	
Corporate and/or household debt distress	Medium-High	Rising private debt questions sustainability and may be causing large amounts of non-interest-bearing assets in banks' balance sheets. Loan books might be less healthy than indicated by statistics, raising concerns about the potential for corporate debt distress and lenders to fall under severe stress.	More intrusive financial supervision to have early warning of debt distress; active steps to force resolution and write-downs, and advancement of corporate insolvency and bank resolution laws.
Abrupt global slowdown or recession	Medium-High	Reduced external demand, especially from Europe, the US, and China, would have a substantial impact on the economy.	Monetary policy responses are constrained by maintaining the exchange rate peg. Therefore, supporting the economy would fall to fiscal policy.
Commodity price shocks + de-anchoring of inflation expectations and stagflation +	Medium	Cambodia is a net oil importer and stands to lose from rising oil and energy prices. It depends on raw materials imports for much of its manufacturing production. Rising commodity prices could reduce households' purchasing power and increase relative poverty.	Policies to counteract inflation are limited, in the short run. The monetary policy objective is currency stability; subject to that, there is some limited ability to withdraw liquidity. Fiscal policy should address distributional consequences while avoiding fueling domestic inflation pressures.
Local Covid-19 outbreaks	Medium	The high rate of vaccination and low rates of infection shown through 2022 so far suggest low risk, but the impact would be large—additional outbreaks could necessitate lockdowns and/or closure of borders, and the health system has relatively low capacity.	Continue with testing and tracing, and distribute boosters for new variants as available.
		Structural risks	
Deepening geo-economic fragmentation and geo-political tensions	High	An increase in geopolitical tensions in the region could disrupt trade and damage confidence, possibly affecting export markets and/or FDI.	Continue to promote export market diversification, relying on the growing importance of the regional markets.
Cyber attacks	Medium	Government and private sector information systems are vulnerable to security breaches.	Enhance guidelines for security in the government and private sector information systems.
Natural disasters related to climate change	Medium	Cambodia is extremely vulnerable to extreme weather events. Floods, droughts and changing monsoon patterns pose a severe threat to agricultural production, a crucial source of income for the most vulnerable segments of the population as well as an important source of exports. Urban areas located close to riverbanks have experienced flooding, which threaten industrial production and housing. Forced migration of large segments of the population may pose social and fiscal challenges.	The National Adaptation Plan (NAP) enacted in 2020 and the Green Recovery Action Plan (2021-2023) signal intention to take action to address climate challenges. Important to keep focusing on adaptation, through investment in climate-resilient infrastructure, reforestation and focus on securing agricultural production/food security. In the long run, it is crucial to budget for support to households and firms affected by extreme weather events.

[1] 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.

Annex III. Implementation of Past Advice

Policies	2021 Article IV Recommendations	Actions since 2021 Article IV Consultations (As of June 2022)
Fiscal Policy	As the economy recovers, policy can focus on further targeting of support measures, restoring revenues, increasing financing options, and supporting SDG goals.	**Targeting of support measures**: the authorities have introduced 10 rounds of Covid-19 policy measures and launched the "Strategic Framework and Programs for Economic Recovery in the Context of Living with Covid-19 in a New Normal 2021-2023" in December 2021. • On the support to households, the cash transfer system, introduced in 2020, continues to be utilized for the poor and vulnerable households until September 2022. The authorities are currently discussing whether to extend cash transfers to those affected by rising fuel and food prices. • On the support to businesses, the current range of interventions includes employment support, tax and fee exemptions, and credit guarantees and subsidies. In February 2022, the Ministry of Economy and Finance (MEF) announced additional funding of US$ 100 million to the SME Bank and the Agriculture and Rural Development Bank (ARDB) to support SMEs in pandemic affected sectors (e.g., tourism, garments). In May 2022, the MEF announced the implementation of the Tourism Recovery Co-Financing Scheme (TRCS) through the SME bank, with another US$ 75 million from the government budget. **Fiscal revenues**: the authorities have implemented measures to restore revenues to allow more spending on development needs: • Strong implementation of the authorities' Revenue Mobilization Strategy (RMS) 2019-23 has helped to mitigate the damage to tax revenues. There were further gains from VAT, customs, and excise tax collection, through strengthened administration such as E-registration, E-filling, E-payment, and E-customs. • With respect to the goal of more stable tax revenues and more progressive taxation, there has been progress on property tax (especially on transfers) and digital taxation (VAT on e-commerce). The introduction of capital gains tax has been postponed until 2024. The authorities have also focused on revenue diversification policies, especially from telecommunication, mine, and oil sources. • The authorities have attempted to cost numerous tax policies and fee exemptions as well as assess the progress of tax administration's modernization, with support from World Bank technical assistance, for proper evaluation the current tax system. The findings from this "Tax System Reform Study" will be inputs for preparing a new RMS 2024-28. **Financing options**: The government intends to issue, for the first time, local-currency government bonds in 2022, while building market infrastructure to manage issuance, registration, and trading.
	The extensive range of measures (e.g., social assistance, below-the-line	The authorities have made progress in improving fiscal governance with the introduction of, medium-term budget framework (MTBF), and PFM reform including drafting the new law on Public Finance System (PFS). There are

<table>
<tr><td></td><td>support) necessitates attention to safeguards.</td><td>ongoing efforts to modernize and harmonize public financial systems and practices, including the Financial Management Information System (FMIS) roll out, public procurement system reform 2019-25, budget system reform strategy for sub-national administration 2019-25, and public investment management system reform 2019-25. Some specific safeguarding measures include:
The authorities have been closely monitoring the new cash transfer system, the results of which suggest that reassessing ID Poor cardholders' financial situations could ensure that monies are allocated more in line with needs.
Regarding concerns about the authorities' capacity to quantify risks from government guarantees and other contingent liabilities, the authorities are working with private financial institutions to assess applicants' credit risks. The authorities intend that support is extended only to viable business in the most affected sectors.
To further monitor fiscal risks, especially from public sector entities (including Public Administration Entities (PAEs) and Public Enterprises (Pes)), the government is currently drafting a law on public enterprise management. Law on Public-Private Partnership (PPP) was introduced in 2021. This will be followed by the introduction of three volumes of operating procedures for PPPs. Deficiencies and recommendations set out by the 2021 PEFA (Public Expenditure and Financial Accountability) assessment are expected to be addressed in the next Consolidated Action Plan (CAP) (phase 4) platform of PFM reform.</td></tr>
<tr><td></td><td>Framing Interventions within a well-defined medium-term fiscal framework (MTFF) would help ensure confidence in the public finances over medium term.</td><td>Plans are already underway to develop an MTFF. The 2023 budget will set expenditure ceilings for key sectors. The draft MTFF 2023-2025 is expected to be completed in 2022, with on-going TA support from the IMF to calibrate fiscal rules and targets. (Currently, the Public Debt Management Strategy 2019-23 outlines a debt rule on medium-term debt levels as a fiscal anchor.)</td></tr>
<tr><td>Macro-Financial and Monetary Policy</td><td>Prudential requirements should be gradually normalized.</td><td>The NBC has taken steps to reduce risks from restructured loans and has been monitoring risks in the banking sector. Exit from regulatory forbearance is planned:
The NBC issued a circular at the end of 2021 extending the forbearance period for new restructured loans until the end of June 2022, and requiring banks to classify and provision for restructured loans. Banks are also required to conduct stress testing on their restructured loan portfolios and report results to the NBC.
Meanwhile, the NBC is considering gradually increasing reserve requirement ratios to pre-Covid-19 levels, starting from the second half of 2022.</td></tr>
<tr><td></td><td>Reforms should continue to close supervisory gaps and bolster financial safety net.</td><td>The NBC has been working to reducing supervisory gaps and strengthen the financial safety net.
The NBC has been working on new capital adequacy/solvency framework (CAR) in line with Basel III, taking into account local banking conditions. The framework consists of five Prakas, on Regulatory Capital, the Capital Adequacy Ratio (CAR), Credit Risk for CAR Purposes, Market Risk for CAR Purposes, and Operational Risk for CAR</td></tr>
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<tr><td></td><td></td><td>Purposes. The new framework has been drafted and is expected to be released in the second half of 2022.
Once the new CAR framework is completed, the NBC will review the Prompt Corrective Action (PCA) framework.
The Deposit Protection and Bank Resolution Unit at the NBC has been tasked with drafting law and/or regulation and conducting a feasibility study toward the establishment of a deposit protection scheme (DPS) in Cambodia, as well as assist in drafting legislation for bank resolution. The deposit protection law has been drafted and is to be reviewed by NBC management, while the legislation for Special Bank Resolution has been under drafting by NBC working team.
The Non-Bank Financial Services Authority (NBFSA), established in July 2021, is responsible for coordinating the formulation and implementation of policies and strategies for the development of the non-banking sector, including financial technology.
Six regulators have been introduced, for Insurance, Securities, Social Security, Trusts, Accounting and Audit, and Real Estate and Pawnshop Businesses. The next step for the authority is to secure full staffing and establish a reporting structure and implementation of roles according to the law on the NBFSA.
The NBFSA's first annual report outlining the outcomes in 2021 and targets in 2022 has been drafted. The NBFSA has also been working closely with the Digital Economy and Business Committee to draft Cambodia's FinTech Development Policy.</td></tr>
<tr><td></td><td>Advances in digital payments could increase efficiency and financial inclusion.</td><td>The NBC continues to encourage cashless payments.
The use of digital or e-payments has continued to grow, as evidenced by the increasing number of digital deposit accounts, e-wallets, virtual cards, number of online transactions, as well as the modernization of payment infrastructure.
Together with digital payment services provided by banks and payment service providers, the NBC's Bakong payment system using block-chain technology (officially launched in 2020), and with more than 8 million users as of April 2022) facilitates cashless payments and cross-border remittances, reduces risks and costs of transactions, and enables the rural population to access financial services.
Cambodia's FinTech Development Policy is also expected to play an important part in building the country's fintech infrastructure including the payment system.</td></tr>
<tr><td></td><td>Increasing exchange rate flexibility would boost monetary policy credibility but is contingent on reducing dollarization.</td><td>Prerequisites for reducing dollarization include development of financial markets, namely interbank and money markets.
The government is expected to issue sovereign debt in 2022Q3.
The NBC, with the support from IMF TA, has continued to work on improving banking liquidity management and forecasting and modernizing monetary policy tools to help reduce exchange rate risk and allow more flexibility. A Marginal Lending Facility (in riel) has been introduced and a Marginal Deposit Facility is in preparation. A</td></tr>
</table>

		feasibility study is being conducted to include interbank transactions in NBC's online trading platform (NBC Platform).
	Addressing deficiencies in the AML/CFT regime	Cambodia has taken steps to address the recommendations of the Financial Action Task Force (FATF), especially for key remaining deficiencies identified in the mutual evaluation report (MER). • An ad hoc sub-committee was established in January 2022 to implement an action plan laid out by FATF with the four remaining deficiencies identified in the AML-CFT mutual assessment. The sub-committee involves officials from the Ministry of Justice, Cambodia Financial Intelligence Unit (CAFIU), Ministry of Foreign Affairs and International Cooperation (MOFAIC), Ministry of Commerce, Non-Bank Financial Services Authority (NBFSA), Commercial Gambling Control Commission, and the National Police's Central Security Department. • The authorities have made some progress in the four deficiencies by (i) improving the dissemination of financial intelligence to law enforcement authorities (Immediate Outcome (IO)-6); (ii) the provision of trainings to strengthen the skills of competent authorities to implement Targeted Financial Sanctions (TFS) related to proliferation financing (PF) (IO-11); iii) an increase in money laundering investigations & prosecutions (IO-7) and; (iv) freezing and confiscation of criminal proceeds, instrumentalities, and property (IO-8). • A progress report is being prepared and will be submitted to FATF by June 2022 for re-evaluation—the result will be available in November 2022.
Structural policies	Addressing lack of diversification and low value added.	Trade and investment liberalization has helped Cambodia to move from dependence on agriculture toward light manufacturing. A new Investment Law (adopted in October 2021) and the Garment, Footwear and Travel Goods (GFT) Sector Development Strategy 2022-27 (adopted in March 2022) aim to enable a move to a higher value-added economy. The authorities have recently introduced several measures, including additional funding to the SME Bank and ARDB in February 2022, to support domestic manufacturing and agriculture. In the long-run, Cambodia also aims to capture the opportunities and benefits of the digital economy by introducing the Cambodia Digital Economy and Society Policy Framework 2021-35 (adopted in May 2021, English version available in August 2021).
	Addressing labor informality.	The authorities continue to take policy measures for addressing labor informality including: i) tax breaks for encouraging firms, especially small and medium-sized businesses, to formally register their business; and ii) expansion of the Health Equity Fund (HEF) to cover informal workers. Nonetheless, the effectiveness of interventions remain limited as workers can still be employed informally within firms.
	Addressing corruption.	To lower transportation cost, improve trade facilitation, and reduce "informal customs charges", the authorities dissolved CAMCONTROL (Cambodia Import-Export Inspection and Fraud Repression Directorate-General of the Ministry of Commerce) and KAMSAB (Kampuchea Shipping Agency and Brokers) from all border checkpoints and ports. The authorities also simplified the process for setting up a business, including the launch of the Cambodia Data Exchange Platform (CamDX) and the online business registration platform.

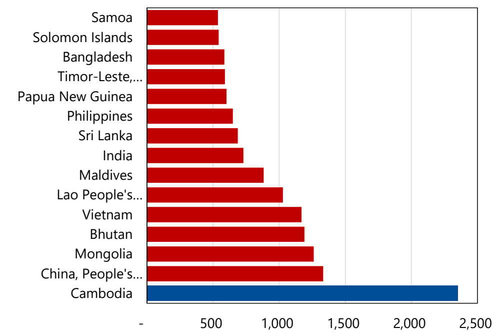
		The Anti-Corruption Unit (ACU) has been focusing on raising awareness, managing assets and liabilities declarations, and investigating corruption cases. Draft legislation on whistleblower protection has been submitted to the Ministry of Justice for review.
	Addressing climate change vulnerabilities	The government has implemented a national Climate Change Strategic Plan 2014-23 and ratified the 2015 Paris Accord. The government has also provided first National Determined Contribution (NDC) report to the UNFCCC in 2015 and updated report in 2020. The authorities also launched the Long-Term Strategy for Carbon Neutrality (LTS4CN) in December 2021. The importance of a green recovery and climate adaptation was further emphasized in the Economic Recovery Strategy with the introduction of "3Rs" in December 2021. The authorities published the Cambodia Climate Public Expenditure Review 2020 in March 2022 on the website of National Council for Sustainable Development (https://ncsd.moe.gov.kh/node/12800). The authorities plan to keep monitoring climate change expenditure with next round of the Climate Public Expenditure Review. On mainstreaming climate adaptation measures, line ministries have been preparing for their own sectoral Climate Change Action Plans (CCAPs) linked to Budget Strategic Plan (BSP). At this point, 14 line ministries have prepared their CCAPs.
	Data quality and transparency	Cambodia participates in the e-GDDS linked to the IMF's Dissemination Standards Bulleting Board (DSBB). The National Summary Data Page (NSDP) hosted on the Central Bank website aims to provide access to the national economic statistics. Recent developments include the official launch of a Residential Property Price Index in June 2022, with technical support from IMF. There is also an ongoing effort to rebase GDP, with technical review from IMF. On Government Finance Statistics (GFS), there has been some progress on: i) full consolidation of general government (including Public Administration Entities (PAEs) and National Social Security Fund (NSSF)) covering 2015-2020; ii) compilation of expenditure in line with COFOG (classification of functions of government) on environmental, health, education, and social protection; iii) and reconciliation of 3 indicators (net incurrence of liabilities, interest to nonresidents, and liabilities stock position) against External Sector Statistics (ESS).

Annex IV. Capacity Development Strategy

1. Cambodia has been an extensive user of the Fund capacity development (CD). Within the Asia and Pacific region, Cambodia was the largest recipient of CD resources in FY2022 (text figure), as the Fund has responded to Cambodia's significant needs for building institutions toward market economy.

2. While Cambodia had robust economic performance prior to the Covid-19 pandemic, significant challenges remain. Ranked as one of the world's fastest-growing economies over the two decades prior to the pandemic, Cambodia has made important progress towards SDGs. Amid the pandemic during 2020-21, Cambodia faced many challenges in maintaining macroeconomic stability and further advancing sustainable and inclusive growth. As the economy recovers from the pandemic, the authorities are wrestling with daunting tasks to make the economy more resilient. For instance, the financial sector has grown rapidly over the past decade and vulnerabilities were elevated even during the pandemic; large infrastructure gaps and mounting development spending needs pose challenges for fiscal management; and structural constraints to sustained strong and inclusive growth reflect a narrow economic base, inadequate competitiveness, and underdeveloped business climate.

IMF TA Delivery by APD Country, FY 2022
(In thousands USD)



(Source) IMF CDMAP data

A. Recent CD Activities

3. The large volume of CD has been well integrated with Fund surveillance. High-quality CD remains central in strengthening the effective implementation of Fund policy advice and bolstering our engagement with the authorities**.** Reflecting key economic challenges, the main surveillance priorities identified by the 2021 Article IV consultations were: i) fiscal policies including on safeguarding fiscal sustainability; ii) macro-financial and monetary policies including on addressing macro-financial risks; and iii) structural policies including on promoting further diversification. CD is also focused on strengthening institutions, policy frameworks, and technical skills to address these issues.

4. Recent CD activities are consistent with surveillance priorities and cover Covid-19-related issues. The priorities include: (i) safeguarding fiscal sustainability, and (ii) addressing macro-financial risks. At the same time, recent CD activities also responded to the increased demand for Covid-19-related issues.

- **Safeguarding fiscal sustainability (Table 1).** Regular TA on public financial management (PFM) and treasury management coordinated through CDOT regional advisors has helped improve spending efficiency, and fiscal reporting and governance. CD to develop an operational Macroframework helped the authorities assess the impact of fiscal policies. The MEF has also been supported by a resident MTBF (Medium-Term Budget Framework) advisor. Macro-fiscal semi-structure model has been developed by MEF with the support from IMF/CD experts to support work on a MTFF (Medium-Term Fiscal Framework). Reflecting the need to increase revenues under the authorities' revenue mobilization strategy (RMS), the authorities have received TA on strengthening customs administrations.

Table 1. Cambodia: Recent Surveillance and TA Integration in the Fiscal Sector

Surveillance Focus: Safeguarding Fiscal Sustainability

Issue	Recent TA Focus	Results
• **PFM - Improve fiscal reporting and governance**	• PFM (FMIS*1, COFOG*2, IPSAS*3, and treasury management); • MTFF (Medium Term Fiscal Framework)	• Supported rolling out Phase II and III of the FMIS • Improved fiscal reporting, fiscal management and budgeting, treasury, and accounting issues.
• **Macro-fiscal Capacity**	• Capacity building in macro-fiscal areas	• Improved MEF's macroeconomic and revenue models, developed tools to monitor and update macro projections in-year and a MTFF. • Developed an operational Macroframework to assess the impact on the economy.
• **Ensure sustained revenue improvement**	• Customs administration • Tax administration diagnostic for RMS (2019-–23)	• Supported GDCE in developing enforcement strategy, the ICT strategy, and strategic and operational planning functions. • Priority areas identified in the tax policy review and tax administration diagnostic are included in the new RMS (2019–23).

*1 FMIS (Financial Management Information System), *2 COFOG (Classification of the Functions of Government), *3 IPSAS (International Public Sector Accounting Standard)

- **Addressing macro-financial risks (Table 2).** Supporting efforts to address elevated macro-financial risks, TA has focused on strengthening banking supervision and regulation, including through the presence of a long-standing resident advisor in banking supervision and regulation. This follows up on the pilot exercise for enhanced macro-financial surveillance. This TA covers the issue of regulatory forbearance to soften the impact of the Covid-19 shocks on the financial sectors as well as prepares for the exit from regulatory forbearance. Other TA has included financial stability analysis; stress testing and macroprudential policy; preparations to establish a bank resolution regime framework and a deposit protection scheme; improving liquidity forecasting/management and interbank market development as well as strategy to promote the use of local currency (with regular support from the regional advisor from Capacity Development Office in Thailand (CDOT) on monetary and foreign exchange operations).

Table 2. Cambodia: Recent Surveillance and TA Integration in the Monetary and Financial Sector

Surveillance Focus: Addressing Macro-Financial Risks		
Issue	**Recent TA Focus**	**Key Results**
• **Upgrade regulation and supervision; build liquidity and capital buffers**	• Upgrading regulation framework of the banking sector	• Upgraded regulations and supervisory processes for credit risk, provisioning, and reporting requirements; minimum capital requirement; capital buffer; liquidity coverage ratio (LCR) and solvency framework in line with Basel III (including the new Prakas on CAR), prepared a new framework for prompt corrective action (PCA) and Deposit Protection Scheme (DPS).
• **Improve monetary policy framework and support gradual shift to market-based monetary and FX Operations**	• Improving liquidity forecasting and monetary operations and developing interbank and FX markets	• Improved liquidity management and forecasting; interbank market development, introduced local currency instruments including NCD*1, LPCO*2, MLF*3 and established online trading platform. • Working to establish a fully-fledged Interest Rate Corridor, streamlining of open market operations (OMOs) and KHR reserve requirement, as well as adjusting the monetary policy decision making process.
• **Promote local currency use**	• Strategy for promoting the use of local currency	• A market based, gradual strategy for promoting the use of local currency is prepared.
• **Systematic financial stability analysis**	• Strengthening systemic financial stability analysis at the NBC	• Established a fully dedicated division to systemic financial stability analysis; and published the first-ever Financial Stability Report (FSR).
• **Analysis of macro-financial linkages in a Macroframework**	• Impact of financial policies on macro economy	• Build a microframework with linkages from the financial to real, fiscal, and external sectors that shows the impact of financial shocks.

*1 NCD (Negotiable Certificate of Deposit), *2 LPCO (Liquidity-Providing Collateralized Operation),
*3 MLF (Marginal Lending Facility)

- **Statistics.** Recent TA on statistics has focused on improving data quality and availability in external (ESS), government (GFS), and monetary and financial sector statistics (MFS). Fund CD has also supported development of a residential property price index (RPPI) (officially launched in June 2022), while CDOT/STA organized regional webinar on workshop on International Trade in Services Statistics and Webinar on Digital Economy and its Measurement. Consistent with the need for broad improvements in data provision for surveillance, TA on statistics helps compile and disseminate data to support policy analysis and detect economic risks and vulnerabilities. TA to support Cambodia's participation in the e-GDDS and the launch of a National Summary Data page (NSDP) have improved data transparency.

- **Training.** Macro-financial training (resumed face-to-face in April 2022 after being conducted virtually during the Covid-19 outbreak) It was delivered by CDOT, STI and ICD, and supported the general macroeconomic capacity development needs of Cambodian officials. It involved regional ICD courses for Cambodia, Laos and Vietnam, tailored to their needs, and included courses on Macroeconomic Diagnostics, Exchange Rate Policy, and Public Sector Debt Dynamics. This training supported TA provided to an "Interagency Economic Core Group (ECG)" to develop a Macro-framework and strengthen macroeconomic analysis and forecasting. It has also supported TA to the MEF on macro-fiscal modeling as an input into MTFF. Cambodia has benefitted from several regional and country-specific training aimed at enhancing the quality of statistics (e.g., external sector statistics, government financial statistics) to support decision making.

B. Forward Looking CD Priorities

5. **Looking ahead, IMF CD can play a pivotal role in Cambodia's transitions to the next phase of its development.** Fund CD can contribute to enhancing institutional capacity to effectively design, implement, and monitor policies in securing macroeconomic stability and sustaining strong and inclusive growth. Some new CD programs are being initiated, including to the NBC to strengthen forecasting for monetary policy Forward looking CD priorities are informed by an evolving multi-year surveillance strategy and CD matrix (Table 3). The multi-year strategy covers traditional macroeconomic issues, enhanced focus on macro-financial issues, topics that fall under Fund key commitments to support countries in achieving their Sustainable Development Goals (SDGs) as well as emerging Fund issues.

Table 3. Cambodia: Multi-Year Strategic Surveillance and CD Matrix

	Macro-Critical	Traction	2019	2021	2022	2023	CD
Traditional macroeconomic issues	HIGH	HIGH	✓	✓	✓	✓	✓
1. Macro-financial Issues, 1/							
Capital Inflows and Spillovers	HIGH	HIGH	✓	→			✓
Financial Stability, Deepening and Inclusion	MEDIUM	MEDIUM	✓	→			✓
Financial Cycle and Macro-implications	HIGH	HIGH	✓	→	→	✓	✓
Balance Sheet Analysis	N/A	N/A			✓	→	
Macroprudential Policy	HIGH	MEDIUM	✓	→	→	→	✓
Financial Supervision and Regulation	HIGH	HIGH	✓	→	→	✓	✓
Macroeconomic Shocks and Financial Stress	HIGH	HIGH	✓	→	→	→	✓
2. SDGs/FfD Commitments							
Domestic Revenue Mobilization	HIGH	HIGH	→	→	✓	✓	
Infrastructure Investment 2/	HIGH	HIGH	✓	→	→	→	✓
Building Policy Space/Economic Resilience	MEDIUM-HIGH	MEDIUM		✓	→	→	✓
Environmental Sustainability, Equity/inclusion	MEDIUM	MEDIUM	✓	→			
Fragile and Conflict-Affected States	N/A	N/A					
Domestic Financial Market Promotion	HIGH	HIGH	✓	→			✓
Data enhancement	HIGH	MEDIUM	✓	→	→	→	✓
3. Emerging Issues							
Gender	LOW	LOW			✓	✓	✓
Income Inequality, 3/	MEDIUM-HIGH	MEDIUM	✓	→			
Climate Change	MEDIUM	LOW			✓	✓	
Governance	HIGH	MEDIUM	✓	→	→	→	✓
Social Spending	MEDIUM	MEDIUM		✓	✓	→	

Key: ✓= focus; → = follow up on previous year(s)

Notes:

1/ Pilot for enhanced macro-financial surveillance (2016) and mainstreaming macro-financial surveillance (2017).

2/ Pilot for infrastructure investment (2016, 2017).

3/ Pilot for inequality (2018).

6. CD priorities:

- **Safeguarding fiscal sustainability.** Spending pressures should be well-managed, and priority given to growth-enhancing infrastructure and development spending. Sustaining revenues will require modernizing revenue administration and policies to improve efficiency and equity. Debt management will face new challenges with the increase in potential contingent liabilities from Public Private Partnerships (PPPs) and introduction of a domestic debt market. Introduction of a medium-term fiscal and budget framework (MTFF/MTBF) will help safeguard fiscal sustainability via improved budget planning and fiscal risk management. Improvements in multiple fronts are needed to strengthen fiscal governance. Against this backdrop, activities should focus on supporting revenue mobilization and debt management, improving fiscal governance and strengthening capacity.

- **Addressing macro-financial risks**. Building on progress made, further measures are needed to monitor elevated financial sector vulnerabilities especially in the real estate sector during the gradual exit from forbearances. This includes effective implementation of past measures, further targeted prudential measures, such as raising risk weights for real-estate lending, introducing a crisis management framework with a deposit protection scheme, and continued upgrading of regulation and supervision. Promoting further financial market development and encouraging local currency use would increase resilience. Further TA will be needed to address deficiencies in AML/CFT.

- **Structural reform issues.** Continued structural reforms are needed to increase competitiveness, encourage further diversification, and expand financial inclusion. There is also room for fiscal policies to better support inclusion, through shifting taxes towards progressive revenue sources and re-orienting expenditure towards priority infrastructure, and health and education spending.

- **Statistics.** While activities should continue to support broad-based improvements in data availability, quality, frequency, and transparency, management of macro financial risks, safeguarding fiscal sustainability and inclusive growth also requires expanded coverage of existing datasets as well as new datasets to address emerging needs. Data provision is broadly adequate for surveillance, but shortcomings in terms of coverage, accuracy and timeliness hamper analysis. For example, budget formulation and reporting are still based on the TOFE system (based on GFS 1986) as opposed to the GFS 2014 standard; national accounts statistics suffer from several weaknesses (including outdated base year, inadequate estimates of the GDP expenditure components, and limited quarterly national accounts data); gaps in real estate statistics prohibit more informed assessment of risks in the sector and to undertake respective policy options; and slow implementation of the national statistics strategy lead to segmented, unreliable, and inconsistent macroeconomic statistics that are not keeping pace with a fast growing economy.

- **Addressing governance vulnerabilities and corruption.** Fiscal governance should be further strengthened through reforms to revenue administration, public financial management and procurement focused on increasing spending efficiency, improving transparency and reducing opportunities for corruption. Additional efforts are also needed to improve the regulatory environment, strengthen the rule of law and push ahead with anti-corruption agenda.

C. CD Strategy

7. Going forward, several caveats would be warranted to make CD more effective. With further strengthening forward-looking integration of CD and surveillance as described above, enhancing TA design to instill a broad-based reform agenda, strong commitment from the authorities, overarching HR management to build lasting capacity, and flexibility of CD delivery are crucial for the success of CD:

- **Tailoring**. TA design needs to take full consideration of authorities starting point, absorption capacity and time required to instill a broad-based reform agenda. CD needs to recognize capacity constraints including often limited absorptive capacity and resources. CD also needs to follow up with past TA recommendations if any This should include a better tailoring of

CD, based on careful prioritization and sequencing, with proposing incremental reforms to ensure sustainability.

- **Ownership**. Strengthening country ownership at all stages of CD interventions (scoping, initiation, execution, and implementation) would further enhance traction. Country authorities play a leading role throughout the CD process, with due consideration to institutional and capacity constraints. Close ongoing dialogue between Cambodia authorities and the Fund strengthens the scoping of CD needs in line with country priorities, with tailoring the technical and policy advice to local conditions and institutional capacity, while allowing for mid-course corrections where needed, and ultimately results in improved traction and impact.

- **Human resource management**. Overarching human resource management in the counterparts are needed to build lasting capacity. It is important to modernize authorities' HR strategy to conduct (and update regularly) a mapping of all key functions and significant business processes in each agency, build staffing and identify most needed resources and urgent gaps in skills based on these outcomes, and to enhance the efficiency of staff allocation and associated CD management. If CD can also deliver some manuals to elaborate TA results like CAMFI (Cambodia Macro-Fiscal Model) prepared by ICD, that would help enhance institutional memories.

Annex V. Social Protection Reform in Cambodia[1]

The authorities plan to expand a new system of social protection across life cycles (e.g., family package) and vulnerable groups (e.g., universal health coverage). This annex takes stock of the progress and direction of social protection reform in Cambodia.

A. Overview: Social Protection Scheme in Cambodia

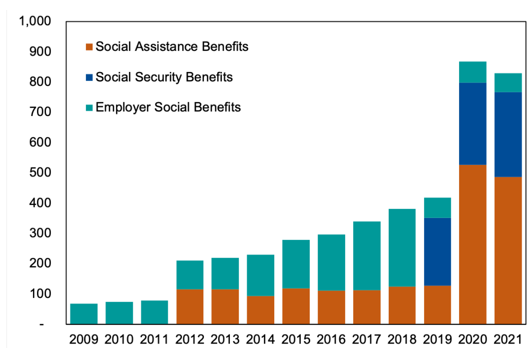
1. Following the National Social Protection Policy Framework (NSPPF), Cambodia has introduced several social protection schemes under the two pillars of: i) social assistance and ii) social security. The social assistance pillar covers emergency responses, human capital development, vocational training, and welfare for vulnerable people. The social security pillar covers pension, health insurance, employment injury insurance, the Health Equity Fund (HEF), and a baby bonus (see Figure 1 for an overview of the social protection schemes and Appendix Table for more details of different schemes.) Under the NSPPF, the authorities plan to introduce unemployment insurance and disability insurance in the future.

Figure 1. Overview

Social Protection Scheme in Cambodia	
I. Social Assistance	II. Social Security
1.Emergency Response	1.Pension
2.Human Capital Development	2.Health Insurance
3.Vocational Training	3.Employment Injury
4.Welfare for Vulenerable People	4. Health Equity Fund (HEF)
	5. Baby Bonus

2. Social protection was expanded significantly during the pandemic (Figure 2). The existing ID Poor system and digital payment method were deployed in 2020 to facilitate targeting and delivery of the Cash Transfer Program for the Poor and Vulnerable Households during the Covid-19 pandemic. From initiation in June 2020 to May 2022, the government has spent around US$ 684 million on the implementation of the cash transfer program for 687,372 families in both urban and rural areas across the country. On social security, there have been 3,018,798 payments provided for poor households and 73,164 payments provided for informal workers under the HEF in 2021.

Figure 2. Fiscal Spending on Social Benefit, 2009-2021
(In million US dollars)



Source: Ministry of Economy and Finance, Government Finance Statistics, 2022.

Note: Social security benefits only covers social security fund for civil servants and veterans.

3. The government will develop social protection further. The government will introduce the "Family Package (FP)" after a gradual phase-out of the Cash Transfer Program for the Poor and Vulnerable Households affected by Covid-19. In addition, the government will develop a roadmap for universal health coverage (UHC) and examine the feasibility of expanding

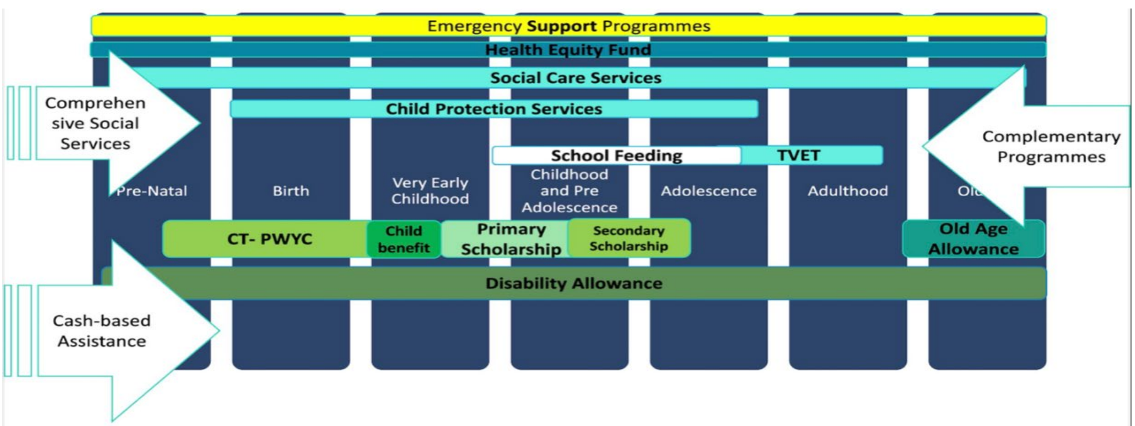
[1] Prepared by Yasuhisa Ojima and Pirun Chan (Resident Representative Office, IMF) and Erna Ribar (UNICEF).

HEF and social security schemes for healthcare for citizens living near the poverty line and working in the informal economy.

B. The Family Package (FP) Framework

4. The government plans to introduce the Family Package Framework in 2023 as a transition from the Covid-19 Cash Transfer Program for the Poor and Vulnerable. The FP will gradually integrate 4 programs, namely i) cash transfers to pregnant women and children under 2, ii) scholarships for primary and secondary school students, iii) cash transfers to people with disabilities, and iv) cash transfers to the elderly, into a social assistance system that intends to respond to the needs of the poor families and their vulnerable members from conception to death (Figure 3). The government intends to implement the FP starting in 2023, with gradual integration of four programs. in collaboration among key line ministries. The schemes under the FP are targeted at poverty at this point, and require continued strengthening of the ID Poor system to identify poor and at-risk households. The FP roll-out envisages streamlining of the delivery system, including enrollment, payments and grievance, and a monitoring and evaluation system managed by the National Social Assistance Fund (NSAF) in collaboration with line ministries responsible for the delivery of the components of the package.

Figure 3. Draft Family Package Program Design – Integrated Social Assistance Framework



Source: Ministry of Social Affairs, Veterans and Youth Rehabilitation and National Social Protection Council

5. The FP aims to establish a system of structured routine cash transfers delivered through a unified approach to support to the key vulnerable categories of the population: pregnant women, children, the elderly, persons with disability (PwD), and persons living with HIV. The FP generally follows a life-cycle approach, with identified gaps intended to be filled in based on the availability of fiscal space. The integrated social assistance framework (Figure 3) envisages linkages with existing complementary social protection programs, as well as with social services to meet the human development and other objectives of the individual cash transfer programs. The FP creates a space for a potential expansion of coverage to additional vulnerable populations, particularly within the context of the shock-responsive social protection.

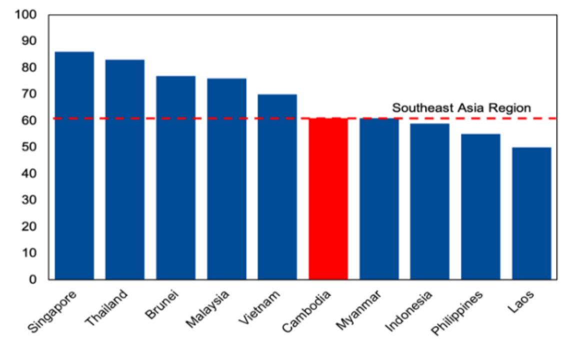
6. Integrating the fragmented social assistance programs into one framework remains the key challenge. Although the authorities have been working on program design, there would be some challenges (some of which are under discussion) including:

- Having clear institutional arrangement and strong coordination among relevant entities for integrating the core programs into a comprehensive FP;
- Ensuring full coverage of all age groups under the current model of poverty targeting of the key vulnerable population groups;
- Expanding coverage as appropriate to better cover certain vulnerable groups ((e.g., near poor or more expanded coverage of certain categories of population such as children, PwD or elderly), particularly in the context of the shock-responsive social protection;
- Strengthening digitalization of the payment system, with considerable investment in financial inclusion and financial literacy;
- Establishing an adequate value of benefits following the new poverty line and the in-depth analysis of additional needs of particular vulnerable groups, including PwD, children and elderly; and
- Developing financing strategy for the social assistance schemes.

C. Universal Health Coverage (UHC)

7. The government aims to achieve UHC in Cambodia by expanding the coverage of existing schemes, including HEF and national social security on healthcare. Cambodia's health service coverage is at the regional average (Figure 4). The existing health coverage schemes collectively cover about 4.7 million Cambodians, or 30 percent of the population (Figure 5), of which HEF covers about 2.6 million individuals and the national social security fund (NSSF)'s health insurance schemes for civil servants and formally employed workers cover 0.4 million and 1.7 million people, respectively (Kolesar et al., 2021).

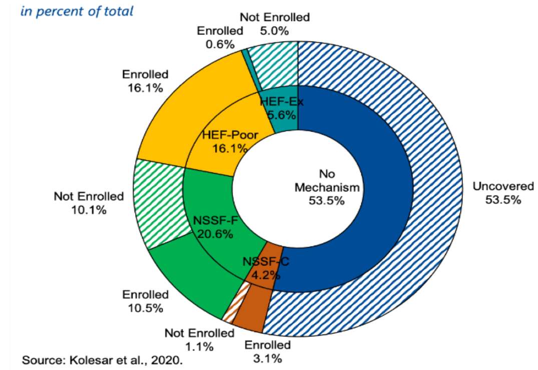
Figure 4. Universal Health Coverage: Service Coverage Index, 2019[1]



Source: WHO, 2022. *World Health Statistics*. Accessed in June 2022.

[1] The construction of the UHC service coverage index (SCI) is based on 14 indicators extracted from various sources and organized into four broad categories of service coverage, namely reproductive, maternal, newborn and child health (RMNCH), infectious diseases, noncommunicable diseases, and service capacity and access. These indicators are meant to be indicative of service coverage and should not be interpreted as a complete or exhaustive list of the health services or interventions that are required to achieve UHC.

Figure 5. Legal and Effective Coverage Estimates of Health Security Schemes



Source: Kolesar et al., 2020.
Note: Inner circle represents legal coverage, while outer circle represents effective coverage.

8. However, coverage issues, including exclusion and inclusion errors, remain. About 36 percent of people under the national poverty line do not hold an Equity card to access HEF benefits, while less than 50 percent of Equity card holders are under the national poverty line (Kolesar et al., 2019; Organization for Economic Cooperation and Development [OECD], 2017).

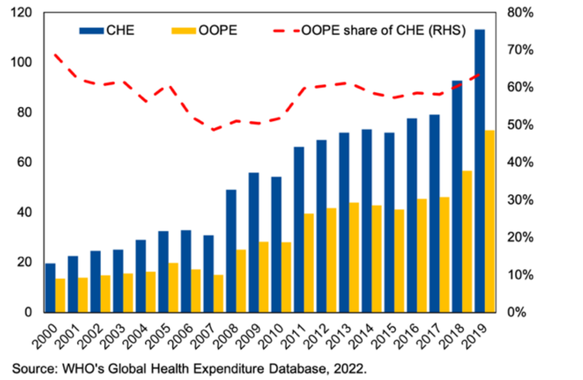
9. The health service provision system faces other additional challenges in addition to coverage:

- *Efficiency issues*. On technical efficiency (cost effectiveness), it has been estimated that Cambodia's public hospitals and health centers can achieve higher service output (e.g., outpatient/inpatient case, major/minor surgery, and maternity care) by 34 and 73 percent respectively with current level of resources (Kolesar et al., 2022). On allocative efficiency, resources are concentrated in urban areas, while rural areas with higher maternal mortality rates remain underfunded (Masaki et al., 2021).

- *Financing issues*. High out-of-pocket expenditure (OOPE) and reliance on external financing are challenges for sustainable financing for UHC (Figure 6). OOPE is estimated to account for approximately 60 percent of total health expenditure in Cambodia (WHO, 2019). For instance, some empirical studies (Kolesar et al., 2019) show that OOPE for rural areas would be estimated at US$ 18.01 and US$ 24.16 per individual per month for the second and third wealth quintiles respectively, while the average monthly OOPE among working-age adults seeking care is estimated at US$ 43.08 and US$ 46.68 (Kolesar et al., 2020). Cambodia's current health expenditure (CHE) appears to be low compared with regional peers (Figure 7).

Figure 6. Cambodia's Health Expenditure, 2000-2019

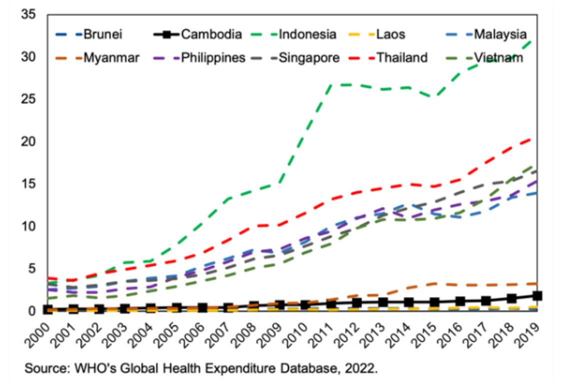
(In per capita USD)



Source: WHO, 2022. Global Health Expenditure Database. Accessed in June 2022. Note: CHE (Current Health Expenditure), and OOPE (Out-of-Pocket Expenditure).

Figure 7. ASEAN Countries' Current Health Expenditure, 2000-2019

(In billion current USD)



Source: WHO, 2022. Global Health Expenditure Database. Accessed in June 2022.

10. Moving forward, the challenge is to improve coverage with enrollment to vulnerable population including informal workers, while addressing the efficiency and financing challenges.

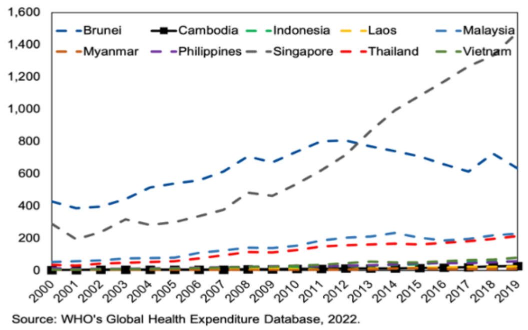
- On coverage, expansion to the lower three income quintiles would likely mitigate exclusion errors (Kolesar et al., 2019). About 8.7 million Cambodians (over 53 percent of the population), out of which nearly 5 million are considered as vulnerable, do not have a social health protection mechanism yet (Kolesar et al., 2020). Moreover, about 16 percent of the eligible population who have access to a mechanism are not yet enrolled (Figure 5). Current expansion efforts focus on the formal employee schemes which primarily benefiting individuals from higher income households.

- On efficiency issues, public health facilities' technical efficiency could be improved by increasing the use of the public health service, given the fact that current public health service is underutilized by healthcare seekers. For instance, less than 20 percent of rural patients first sought healthcare among public services, while 76 percent used private sector as their first point of contact (Kolesar et al., 2019). This would also lead to a decrease of unit costs, given health facilities' high fixed costs (Jacobs et al., 2019). Allocative efficiency should also be considered from a broader perspective of geographic distribution of resources, while acknowledging equity-efficiency trade-offs (WHO, 2022). Increasing health professionals/resources in rural areas may not be cost efficient, given low population density; however, the geographic location of health services has a direct impact on health outcomes within countries, by affecting how quickly patients can seek care when faced with illness and injuries.

- On financing issues, effective resource mobilization is crucial for meeting the growing health spending needs. Cambodia's public health expenditure per capita is the third lowest among regional peers in 2019 (Figure 8). The Cambodia's Health Strategic Plan target (i.e., government health expenditure as percentage of government total expenditure to reach 9 percent by 2020) has not yet been met (Figure 9).

Figure 8. ASEAN Countries' Public Health Expenditure, 2000-2019

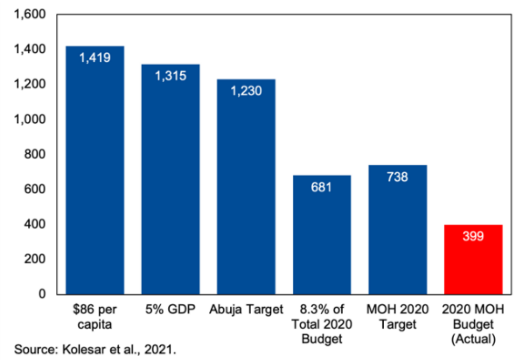
(In per capita USD)



Source: WHO, 2022. Global Health Expenditure Database. Accessed in June 2022.

Figure 9. Health Spending Benchmarks versus Cambodia's MOH Budget[1]

(In million USD)



Source: Kolesar et al., 2021.

[1] The per capita target of US$ 86 for low-income countries is based on an initial estimate of required level of public health expenditure prepared by the High-Level Taskforce on Innovative International Financing for Health Systems. 5 percent of GDP was first proposed in the 2010 World Health Report. The Abuja Declaration of 2001 recommended that governments allocate 15 percent of their budgets to the health sector. WHO data show that in 2016 the share of general government health expenditure as a percentage of general government expenditure for lower-middle income countries averaged 8.3 percent. Cambodia's Health Strategic Plan targets government health expenditure as percentage of government total expenditure to reach 9 percent by 2020.

Table 1. Cambodia: Overview of Social Protection Scheme in Cambodia			
No	Program	Current Progress	Future Direction
I. Social Assistance			
1	**Emergency Response**		
1.1	Food Reserve System	Established to provide food to poor households during catastrophic events or emergency.	
1.2	Cash Transfer for Poor and Vulnerable Households during Covid-19	Between June 2020 and May 2022, 687,372 households or 2.7 million people received the benefits with total budget spent at approximately US$683.6 mill.	Will be phased-out gradually depending on the development of Covid-19 and inflation (oil and food prices).
1.3	Post-Lockdown Cash Transfer in Phnom Penh, Takmao, and Preah Sihanouk	For those facing difficulties and living in the large lockdown area in Phnom Penh, Takmao, and Preah Sihanouk province.	One-off program.
2	**Human Capital Development**		
2.1	Cash Transfer for Pregnant Women and Children under 2	Launched in 2019, by March 22, 2022, 138,482 beneficiaries received the cash transfer of which 96,949 mother and 41,533 children.	Will be integrated into "Family Package Framework".
2.2	Home-Grown School Feeding Program	By 2022, cover 290 schools with 74,951 students located in 9 provinces (Battambang, Preah Vihear, Stung Treng, Banteay Meanchey, Siem Reap, Oddar Meanchey, Kampong Cham, Kampong Chhnang, and Pursat).	
2.3	Scholarship Program for Primary and Secondary Education	Around 261,974 students have received the scholarship.	Will be integrated into "Family Package Framework".
3.	**Vocational Training**		
3.1	TVET Program	Provide vocational training to youths from poor households, improving their skills to enable them to be able to find jobs and have good incomes.	
4	**Welfare for Vulnerable People**		
4.1	Cash Allowance for Poor Person with Disabilities	Around 16,807 beneficiaries received these benefits in 16 provinces.	Will be integrated into "Family Package Framework".

Table 1. Cambodia: Overview of Social Protection Scheme in Cambodia (Concluded)

No	Program	Current Progress	Future Direction
II. Social Security			
1	**Pension**		
1.1	Pension Scheme for the Civil Servants and Veterans	The government fully subsidies the pension expense.	
1.2	Pension Scheme for Workers and Employees	Expect to launch in 2022.	
2	**Health Insurance**		
2.1	Health Care Scheme for Civil Servants, Retired Civil Servants, and Veterans	Started in 2018, the government fully cover the contribution.	Will be expanded for "Universal Health Coverage".
2.2	Health Care Scheme for Workers and Employees	Started in 2016, the employers fully cover the contribution.	Will be expanded for "Universal Health Coverage".
3	**Employment Injury**		
3.1	Occupational Risks Scheme for Public Officials	Started in 2021, the government fully cover the contribution.	Will be expanded for "Universal Health Coverage".
3.2	Occupational Risks for Workers	Started in 2008, the employers fully cover the contribution.	Will be expanded for "Universal Health Coverage".
4	**Health Equity Fund**		
4.1	Health Equity Fund	In 2021, there are 1,331 public health facilities under HEF. There have been 3,018,798 cases provided to poor households which equal to US$2,225,882, and 73,164 cases provided to informal workers which equal to US$419,282.	Will be expanded for "Universal Health Coverage".
5	**Baby Bonus**		
5.1	Baby Bonus	From January 2018 to February 2022, the baby bonus provides benefits to 296,220 new mothers (298,242 children) with both formal and informal employment equivalent to US$29.8 mil.	

Source: Ministry of Social Affairs, Veterans and Youth Rehabilitation and General Secretariat of the National Social Protection Council (GS-NSPC).

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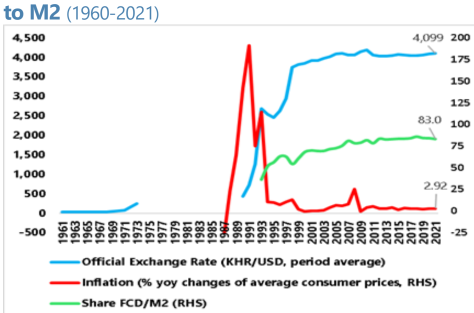
Annex VI. De-Dollarization Measures in Cambodia[1]

This annex analyzes recent developments in Cambodia's dollarization and take stock of measures taken by the authorities so far to promote the use of local currency (Khmer Riel or KHR), while listing some additional potential measures toward de-dollarization.

A. Dollarization in Cambodia

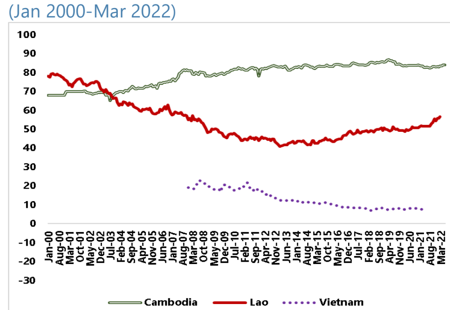
1. The most notable characteristic of Cambodian dollarization is that it had continued across the three dimensions of "*financial,*" "*payment,*" and "*real*" dollarization[2] in the process of rebuilding the financial system from scratch after its collapse by the Khmer Rouge. As there were essentially no financial assets after the Khmer Rouge regime, Cambodia had no options but to deploy the internationally accepted currency. The U.S. dollars (USD) played key roles in saving (as a store of value) and payment (as a measure of settlement). The widespread use of USD, including display of prices (as a unit of account), began during the United Nations Transitional Authority in Cambodia (UNTAC)'s period after the establishment of peace in 1991, with massive aid inflows of USD to revive its economy. The dollarization process was also reinforced through credit creation with web of USD lending and deposit. From other countries' experiences (see Garcia-Escribano, Mercedes and Sosa, Sebastian (2011) for the case of Latin America countries), dollarization tends to be reversed when the local currency is stabilized with moderate inflation rate under the process of "de-dollarization" efforts. However, despite price stability both in inflation rate and nominal exchange rate (see Figure 1), "financial dollarization" in Cambodia has continued to expand with growing foreign currency deposits (FCDs). This is exceptional situation compared with neighboring peers like Viet Nam and Laos (see Figure 2).

Figure 1. KHR/USD Exchange Rate, Inflation and Share of FCD to M2 (1960-2021)



Source: NBC, NIS, IMF and World Bank

Figure 2. Share of FCD to M2
(Jan 2000-Mar 2022)



Source: Country's Monetary Survey

[1] Prepared by Yasuhisa Ojima and Kuchsa Dy.

[2] In most emerging and developing economies where dollarization became prevalent, assets denominated in the local currency were substituted by ones denominated in foreign currencies, mainly in USD. This is "*financial dollarization*" as *a store of value* to protect assets, given limited confidence in the domestic currency on the back of political and economic instability. With further economic instability, the role of the domestic currencies in the economies was further constrained by "*payment dollarization*," where foreign currencies began to be used as *a measure of settlement*. With further deterioration in the economies, the domestic currencies to lose even their function of *unit of accounts*, leading up to "*real dollarization*" where foreign currencies were used to display prices (Nicolo et al., 2005).

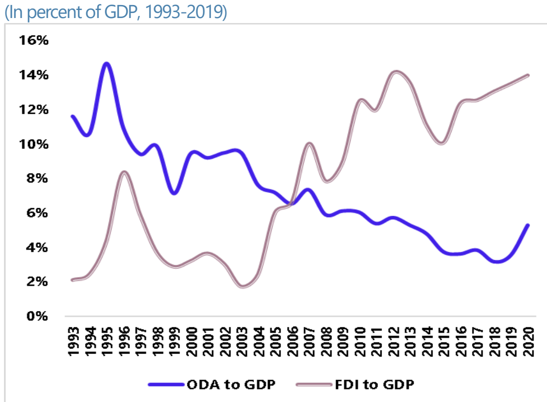
2. Dollarization in Cambodia remains persistent in part due to its external sector development with continued FX inflows, financial deepening with foreign currency credit creation, and the network externalities. The dollarization has been supported by its external sector development as well as the current pattern of financial sector development. At the same time, dollarization has been reinforced progressively over a long period as the various economic actors have reached a self-restraining Nash equilibrium that stabilizes the system (Greif, 2006).

- **External sector development**. The country continues to absorb foreign currency mainly through Foreign Direct Investment (FDI) to various sectors such as manufacturing (e.g., garment) and services (e.g., tourism, finance, and real estate), while official aid gradually decreases as the economy develops (Figure 3). Similarly, by looking at the country's balance of payment (Figure 4), Cambodia's rapid economic growth has been financed by the inflow of funds from abroad (i.e., FDI, foreign aids) over the last two decades: substantial current account deficits have been continuously offset by the country's surplus in financial account, leading to the accumulation of country's net foreign assets including NBC's international reserves.

- **Financial deepening**. Unlike its neighboring countries, the use of USD and financial development were integrated. As the economy stabilized and financial development accelerated mainly with external funding, the use of USD expanded from cash to deposit currency (financial dollarization). In Vietnam and Laos, the financial dollarization, measured by the share of FCDs in total broad money (M2), dropped to 10.8% and 44.4%, respectively, in the mid-2010s (Figure 2) as economic conditions improved and the authority tightened restrictions on the use of foreign currencies. In contrary, in Cambodia, financial dollarization increased from about 36.3% in 1993 to 85.6% as end of 2018 before slightly decreased to 83% as end of 2021. This suggests very high and persistent dollarization in Cambodia, although the country has generally experienced both macroeconomic and political stability over the last two decades.

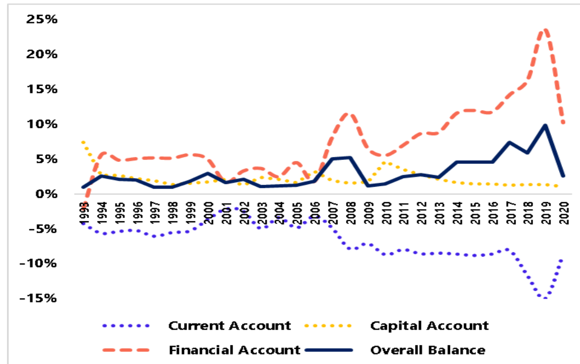
- **Network externalities**. Given the external development and financial deepening, the USD continue to be dominant for payment (medium of exchange), value measure (unit of account), and savings (store of value). Payment and real dollarization themselves would be served as preconditions for financial dollarization, leading to the situation of "network externality" where the larger number of currency users brings the higher value of its utility (Samreth 2011).

Figure 3. ODA and FDI in Cambodia
(In percent of GDP, 1993-2019)



Source: World Bank

Figure 4. Balance of Payments
(In percent of GDP, 1993-2020)



Source: IMF

3. **Dollarization is concentrated mainly in the urban area, while the degree of dollarization in the activities of an enterprise is not necessarily determined by its size.** Evidence from the NBC-JICA survey in 2017 on dollarization of households in Cambodia shows that the degree of dollarization is not homogeneous across the regions in Cambodia. Dollarization is concentrated mainly in urban areas, where economic activities are more dynamic and exposed to foreign currency flows, especially in Phnom Penh. In the rural areas, the KHR dominates in payments, price quotations, and even as a store of value. In general, the USDs are used for large payment transactions and imported goods or in modern markets, while the KHR is essentially used in small payment transactions such as those for foodstuffs or in traditional markets, and some large transactions in the agricultural sector. Moreover, the degree of dollarization in the activities of an enterprise is not necessarily determined by its size, but by other factors such as geographic distribution and sources of incomes and borrowings (NBC-JICA survey in 2017 on dollarization of Cambodia's enterprises).

B. Measures to Promote the Use of Local Currency

4. **The authorities have so far formulated and implemented certain measures towards de-dollarization.** The government, together with relevant authorities, have put in place several supportive and market-oriented policies and measures to gradually promote the use of local currency. The table below provides a summary of main policies and measures that have been implemented.

Table 1. Cambodia: Summary of De-Dollarization Measures Taken so Far

Policies	Description
• Enhancing confidence in the local currency through exchange rate stabilization	- In the short term, stabilizing the exchange rate of KHR and its purchasing power by moderating inflation to increase strong enough confidence in KHR. - In the medium to long term, migrating to a more flexible exchange rate under flexible inflation targeting, while more rigorous studies of the impact of flexible inflation targeting with confidence in KHR are warranted.

Table 1. Cambodia: Summary of De-Dollarization Measures Taken so Far (Concluded)	
• Promoting price quotations and payments for goods and services in KHR	- In the short term, encouraging firms and sellers to quote the price and payments of goods and services, and the payments of salaries and wages in KHR only or at least alongside USD. - In the medium to long term, requiring quoting only in KHR. More rigorous studies of the impact of price quotations and payments are needed.
• Promoting the opening of bank accounts in KHR	- Encouraging the use of bank accounts denominated in KHR. In the long run, gradually requiring all firms to open bank accounts for their employees in KHR is essential. Currently, government officials get their salaries through bank accounts in KHR. - Promoting price quotations and payments for goods and services and salaries and wages in KHR seems to also promote the opening of bank accounts in KHR. - In rural areas, where many households are unbanked and where the use of KHR is high, are a good place to promote the opening of bank accounts in KHR.
• Improving the payment system and financial instrument in KHR	- Having more availability of KHRs notes in ATMs across the countries. - Encouraging money transfers or remittances to be carried out within formal financial institutions or using agents to reduce the direct use of foreign currencies.
• Increase the cost of retaining foreign currency deposits	- The NBC introduced differentiated rates of required reserves for USD and KHR in 2008 (i.e., 16% for USD and 8% for KHR). However, the rates became reduced to same level of 7% both for USD and KHR in March 2020 to ease banking liquidity in response to the pandemic. The rates remain same as of June 2022 (Figure 5).
• Increase financial intermediation in KHR	- The NBC required banks and financial institutions (BFIs) to have at least 10% of their loan portfolio in KHR by end of 2019. However, so far, no strict measures are imposed on the non-compliant BFIs and no rigorous study is done yet to evaluate the impact of this requirement.
• Introduce mechanisms and tools to encourage interbank -market and provide liquidity in KHR to BFIs	- The NBC introduced NCD (in KHR and in USD) to absorb excess liquidity and at the same time for BFIs to use in interbank money market. The NCB also introduced LPCO, and more recently Marginal Lending Facility (MLF) to provide termed KHR liquidity to BFIs with NCD as collateral.
• Develop securities market for local currency	- It is already started by introducing securities market (CSX) with quotations in KHR to promote KHR although its current transactions are still limited. - The government started to issue government bonds from September 2022 by auctions.
• Requirement of tax payment in KHR	- Revenue collection through tax is conducted in KHR. However, there are still some revenues collected in foreign currency, such as electricity bill, entrance fees to tourism sites, airport taxes, visa fees, rents…etc.
• Promoting public awareness of the importance of using local currency	- Mainly done by the NBC through various program and campaign including annual Riel Day.

5. Moving forward, domestic financial markets need to be further strengthened towards de-dollarization, while ensuring macroeconomic stability as precondition. The development of domestic financial markets would help to reduce risk, increase availability of funds, decrease uncertainty and volatility of exchange rate, and enhance public confidence in local currency.

- **Foreign exchange market**. An effective and formal wholesale foreign exchange market is essential to absorb foreign currency inflows and provide foreign currency when the market needs. All money changers need to be formalized with having a bank account with commercial banks. With more accurate market information, the NBC could craft measures to promote the use of local currency in a timely fashion.

- **Money markets**. There is currently no active interbank money market in Cambodia. The money markets would allow BFIs to better manage local currency liquidities and use KHR in their operations. The introduction of a full-fledged interest rate corridor (IRC) at the disposable of NBC would support development of KHR interbank markets. An IRC allows banks to predictably place surplus liquidity and obtain short-term funding from each other or NBC at reasonably stable rates. In this connection, the introduction of an overnight Marginal Lending Facility (MLF) in Sep 2021 is a commendable step. A more systemic and timely market monitoring through NBC platform would also be warranted.

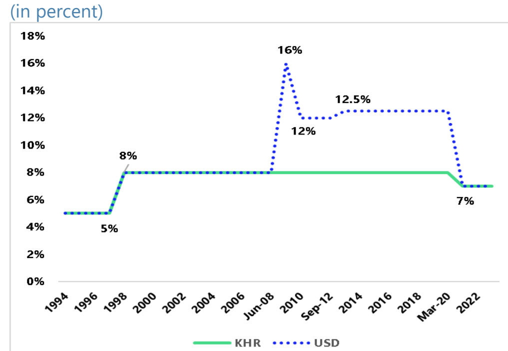
- **Securities markets**. Further development is needed to promote securities and bond markets given the limited volume of current transactions in the markets. More instruments need to be introduced in addition to the recent issuance of government bond in local currencies.

- **Payment systems**. The clearing house's policy on further lowering KHR transaction fee would make KHR more attractive for banks and then for the clients. In addition, further enhanced payment system (e.g., Bakong) would lead to lower KHR transaction costs.

6. Additional supporting measures for de-dollarization could be warranted.

- **Prudential measures**. The differentiated reserve requirement rates for USD and KHR need to be reintroduced with higher rates for USD, raising the cost of holding USD deposits for BFIs (Figure 5). Future deposit protection scheme would also take differentiated approach towards USD and KHR deposits (e.g., higher insurance coverage for KHR deposit), enhancing incentives for depositors to hold more KHR deposits.

Figure 5. Required Reserve Ratio for KHR and USD
(in percent)



Source: NBC

- **Public price quotation measures**. The authorities could consider gradual migration to all other current public revenues to be in KHR transaction including entrance fees to tourism sites, airport taxes, visa fees, and public building rents.

7. Evidence-based policy making. NBC introduced a strategy "Promoting the Use of Khmer Riel" in 2017. This strategy could be upgraded to national policy with robust empirical studies on the impact of de-dollarization measures. An evidence-based policy making would lead to stronger commitment by various stakeholders.

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Annex VII. Fighting Climate Change in Cambodia[1]

Cambodia remains one of the most vulnerable countries to climate risks, while its greenhouse gas emissions remain relatively low. This summarizes the authorities' climate targets and policy responses across both mitigation and adaptation, after setting out stylized facts about Cambodia's greenhouse gas emissions and vulnerability to climate risks.

A. Cambodia's Greenhouse Gas Emissions

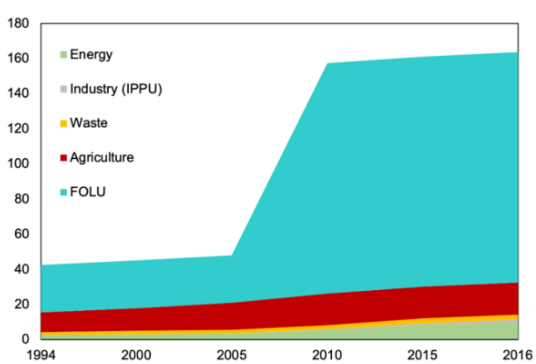
1. **Cambodia's Forest and Other Land Use (FOLU) sector has traditionally been the major contributor to greenhouse gas (GHG) emissions, driven primarily by deforestation.** GHG emissions have been steadily increasing over the last three decades, with a huge jump in GHG emissions by FOLU sector from 2010 onward (Figure 1). This was due to the differences in the observed loss of forest cover between 2010-2016 (579,280 ha/year in average) and 1994-2009 (132,733 ha/year in average) (National Council for Sustainable Development [NCSD], 2020).

2. **At same time, GHG emissions were also accelerated by the agriculture and energy sectors.** Agriculture is the second largest contributor, mainly through cultivation of rice. GHG emissions from agriculture increased at an annual average rate of about 2.5 percent between 1994 and 2016 (NCSD, 2020). Energy demand also increased significantly due to growth in the transport sector, due to urbanization and population growth (especially through migration to urban areas).

3. **Nonetheless, Cambodia's GHG emissions remain relatively low.** CO_2 emission per capita for Cambodia was 0.65 tons in 2018 compared to 4.42 for the world, Asia-Pacific's 3.89, and ASEAN's 2.27 (Figure 2). In terms of energy sources, oil accounted for 70 percent of CO_2 emissions in 2018, with coal accounting for the remaining in the same year (International Energy Agency [IEA], 2021).

Figure 1. GHG Emissions in Cambodia, by Sector

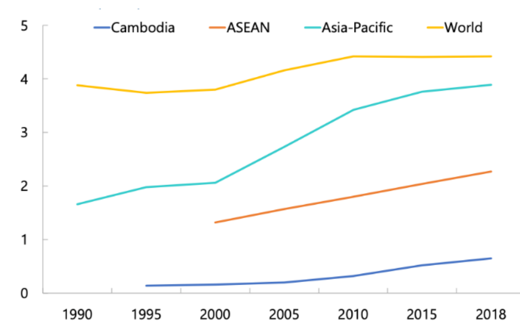
(In MtCO2e)



Source: Cambodia's First Biennial Update Report, 2020.

Figure 2. CO_2 emissions per capita 1990-2018

(Tons of CO2 per capita)

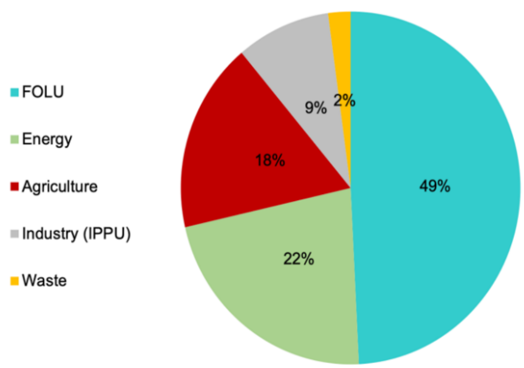


Source: International Energy Agency, 2021. [CO_2 emissions Data and Statistics](). Accessed in March 2021.

[1] Prepared by the IMF Resident Representative Office for Cambodia (Yasuhisa Ojima and Pirun Chan).

4. Overall GHG emissions are projected to increase. The updated Nationally Determined Contribution (NDC) indicates that overall GHG emissions are projected to increase to 155 million tons of CO_2 equivalent in 2030, growing from 2016 estimate by 24 percent (Royal Government of Cambodia [RGC], 2020). Emissions under all Business-As-Usual (BAU) scenarios indicate a steady increase by 2030, with the highest emissions contributor from FOLU sector (49 percent), followed by energy (22 percent) and agricultural sectors (18 percent) (Figure 3). The IMF projects emissions growth for Cambodia under its BAU scenario at more than 30 percent from 2017 to 2030, mainly driven by fast economic growth (Figure 4) (Dabla-Norris et al., 2021).

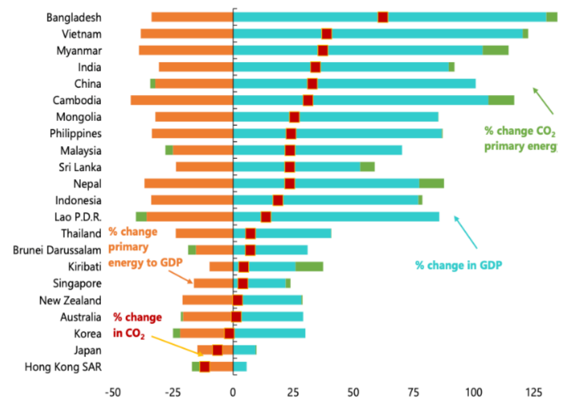
Figure 3. Sectoral Share of GHG Emissions in 2030



Source: Cambodia's Updated NDC, 2020.

Figure 4. Baseline CO2 Emission Change

(In percentage change from 2017 to 2030)



Source: Dabla-Norris et al., "Fiscal policies to address climate change in Asia and the Pacific", IMF Asia and Pacific and Fiscal Affairs Departments, 2021.

B. Cambodia's Mitigation

5. Cambodia has committed to achieving carbon neutrality by 2050. Cambodia submitted an updated NDC in 2020, with a commitment to reduce emissions by 42 percent by 2030 (RGC, 2020). In November 2021, at the UN Climate Change Conference (COP26), the Minister of Environment announced commitments to increase the share of clean energy without developing any new coal power plants and new hydropower dams along the Mekong River. In December 2021, the government submitted a Long-Term Strategy for Carbon Neutrality (LTS4CN), a pathway towards a country-wide carbon neutral economy by 2050, to the Secretariat of the United Nations Framework Convention on Climate Change (UNFCCC).

6. Cambodia's carbon neutrality is largely supported by the FOLU sector. This FOLU sector would provide a total carbon sink of 50 $MtCO_2e$ by 2050 (RGC, 2021), consistent with the updated NDC in which GHG emissions from FOLU sector could be halved by 2030. The LTS4CN sets out mitigation targets and actions as follows:

- *FOLU Sector:* During the first decade of the strategy, emission reductions are achieved through the implementation of investment plan on REDD+[2] .The FOLU sector is expected to be carbon neutral from 2031, and reforestation and afforestation efforts will ensure that the carbon sink from forests continues to grow.

- *Agriculture Sector:* Major emission reductions will be ensured through i) mitigating methane-intensive rice and livestock production, and ii) promoting the use of biogas in livestock management, organic fertilizer, and deep fertilizer technology.

- *Transportation Sector:* Urban public transportation will be further developed, and electric vehicle penetration will grow in the passenger vehicle fleet. Investments in rail development will start after 2030. Emissions will be further reduced by i) more moderate use of electric vehicles, ii) increased fuel efficiency for internal combustion engine vehicles, and iii) higher penetration of compressed natural gas (CNG) for interregional buses and for trucks. 70 percent of motorcycles and 40 percent of cars and urban buses are expected to be electric vehicles by 2050.

- *Energy Sector:* Emission reductions until 2030 come from energy efficiency and conservation through the implementation of the National Energy Efficiency Policy in buildings, industry, and public services. At the same time, demand side management will be enhanced, for instance, through switching to electricity for cooking and passenger vehicles and to coal alternatives in the industrial sector. After 2030, emission reductions in the energy sector will come from more stringent energy efficiency standards and continued fuel switching to low-carbon sources. Renewable energy in the generation mix is set to reach a share of 35 percent in 2050, of which 12 percent is assumed to come from solar.

- *Waste Sector:* The waste sector will achieve half of its emission reductions in the first decade through mitigation measures in solid waste disposal (e.g., reduced, reuse and recycle). In 2050, the waste sector is expected to realize nationwide waste collection coverage of 85 percent and will be almost fully decarbonized. The recycling rate will increase to 35 percent, and half of organic waste will be composted or treated.

- *IPPU (Industrial Processes and Product Use) Sector:* Key mitigation actions in the sector are using clinker[3] substitution and carbon capture and storage in cement production, recycling of aggregate concrete, increased use of refrigerants with low global warming potential and regular inspection of refrigeration and air-conditioning equipment as well as recovery of spent refrigerants.

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[2] REDD+ stands for "Reducing Emissions from Deforestation and forest Degradation, plus the sustainable management of forests, and the conservation and enhancement of forest carbon stocks".

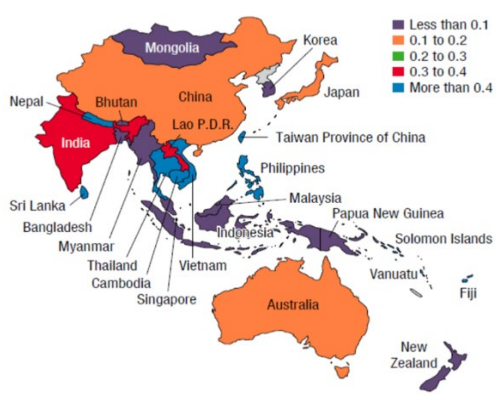
[3] Clinker is a material primarily used in cement production as the binder in cement products. Nonetheless, producing clinker is carbon intensive because of the carbon released by limestone (material used for producing clinker), and because of the energy required in the process.

C. Climate Change Risks for Cambodia

7. Cambodia remains vulnerable to climate risks, particularly floods, droughts, and storms (Figure 5). During 1993 and 2020, Cambodia has faced many climate-related disaster events including 20 floods, 5 droughts, 6 tropical storms and 1 famine, with at least US$1.5 billion of estimated damage from these events (Emergency-Events Database [EM-DAT], 2021). The drought and floods in 2020 highlighted that the large agricultural sector relies on regular monsoon seasons, while fluctuations in Mekong River flows affect traditional irrigation system, fishing, and transportation for industry and land tourism. Without actions, the population exposed to an extreme river flood could grow to around a quarter of total population (i.e., 4 million) by the 2040s, while the damming of the Mekong River as well as the large-scale dams built on its tributaries may alter future flood dynamics (World Bank [WB] and Asian Development Bank [ADB], 2021). Furthermore, Cambodia scores relatively low on "adaptive capacity[4]" (Figure 6).

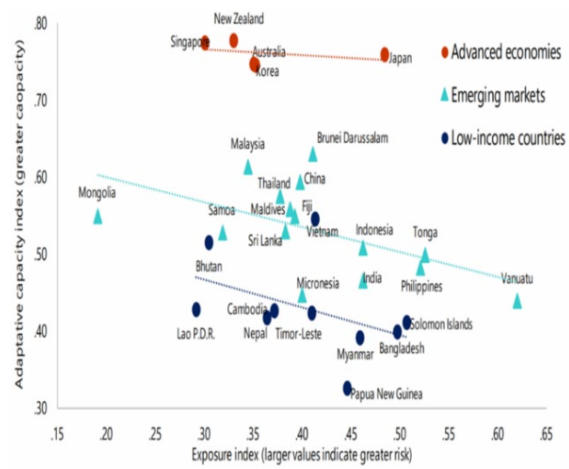
Figure 5. Damage from Climate-related Events, 2010-19

(Percent of GDP)



Source: Emergency-Events Database (EM-DAT), 2021.

Figure 6. Adaptive Capacity and Physical Exposure



Source : Dabla-Norris et al. (2021)

8. Projected climate change trends indicate more severe floods and droughts that are projected to reduce GDP by 9.8 percent in 2050 relative to its baseline (NCSD, 2019). Cambodia is also projected to experience warming in the future. Under the highest emissions pathway (Representative Concentration Pathways (RCP) 8.5), Cambodia would face the warming of 3.1°C by the 2090s against the baseline conditions over 1986-2005. In addition, increases in annual maximum and minimum temperatures are expected to be larger than the rise in average temperature, increasing pressures on human health, livelihoods, and ecosystems (WB and ADB, 2021).

[4] Adaptive capacity is defined as the ability of systems, institutions, humans, and other organisms to adjust to potential damage, to take advantage of opportunities, or to respond to consequences (IPCC, 2007).

D. Cambodia's Adaptation

9. Cambodia has made efforts to mainstream climate adaptation into policy framework. Climate change has been addressed at the National Strategic Development Plan (NSDP) since 2009 and at the Rectangular Strategy Phase IV (2019-2023). In 2013, Cambodia adopted the first national framework addressing climate change—Cambodia Climate Change Strategic Plan (CCCSP) 2014-2023. Under this framework, climate change has been integrated into sectoral planning as 14 ministries adopted respective action plans encompassing adaptation including sub-national planning (NCSD, 2021). The authorities have also mainstreamed adaptation into national budget process as the Ministry of Economy and Finance (MEF) prepared its 2020 Climate Public Expenditure Review (CPER) (MEF, 2022). The authorities recently reaffirmed its commitment to enhancing resilience to climate change in the Economic Recovery Plan 2021-2023.

10. Nonetheless, there remains substantial work to be done. A full National Adaptation Plan (NAP) has not yet been adopted, while the authorities adopted financing and implementation plan for 14 sectors partially (see NCSD (2017)). Achieving the full NAP will call for fiscal reform (e.g., domestic revenue mobilization, strategic budget planning) and a coordinated approach across government and private sector partners to ensure adequate financing for adaptation-related investments. The public adaptation costs for Cambodia are projected to be between 2-3 percent of GDP (Figures 7 and Figure 8). Moreover, the updated NDC highlighted that the total funding required for adaptation actions would be over US$2 billion (RGC, 2020). However, majority of the identified climate adaptation projects by the 14 ministries (NCSD, 2017) have not yet been funded.

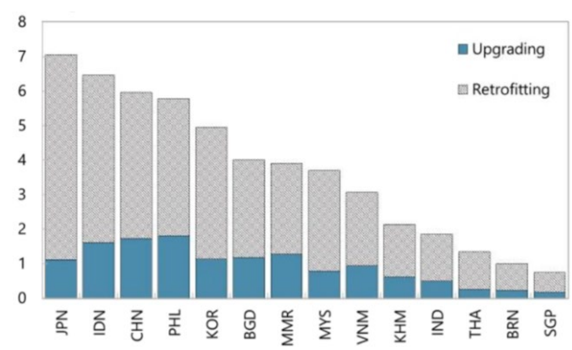
Figure 7. Adaptation Costs and Pre-Covid-19 Fiscal Space

	At least some fiscal space or moderate/low risk of debt distress	At-risk fiscal space or high risk of debt distress
Public adaptation costs above 1 percent of GDP	China, Bangladesh, Cambodia, Indonesia, Japan, Korea, Myanmar, Papua New Guinea, Philippines, Solomon Islands, Timor-Leste, Vanuatu, Vietnam	Fiji, Kiribati, Lao P.D.R., Malaysia, Maldives, Marshall Islands, Micronesia, Tonga, Tuvalu, Samoa
Public adaptation costs below 1 percent of GDP	Australia, Bhutan, Nepal, New Zealand, Singapore, Thailand	India

Sources : Hallegatte, Rentschler, and Rozenberg (2019) ; Nicholls and others (2019) ; Rozenberg and Fay (2019) ; and IMF Staff reports and staff calculations.
Dabla-Norris et al. (2021)
Note: Fiscal space assessments are estimated for advanced and emerging market economies and are based on the last published IMF Article IV debt sustainability assessment; risks of debt distress estimated for low-income countries and are taken from the last published debt-sustainability assessment. These assessments were performed pre-COVID and do not reflect the developments since the outset of the pandemic.

Figure 8. Annual Cost of Upgrading Investments and Retrofitting Existing Assets

(Percent of GDP)



Source : Dabla-Norris et al. (2021)

11. Moving forward, the government has called for further investment for climate adaptation and financial resources in partnership with the private and financial sectors.

- Green and resilient public investment is seen as important to facilitate a sustainable recovery, including the adaptation to climate change. In this context, the upcoming Climate-Public Investment Management Assessment (C-PIMA) will help the authorities identify potential improvements in public investment management institutions and processes to develop low-carbon and climate-resilient infrastructure.

- The government has emphasized the importance of sustainable finance, especially creating a favorable environment to mobilize additional resources to ensure the sustainability of climate actions. This includes the formulation and implementation of green financing mechanism and public-private partnership (PPP).

- The National Bank of Cambodia (NBC) has continued to call for banks and financial institutions (BFIs) to put policies in place to promote green finance and environment-friendly investments. On the regulatory side, NBC is promoting ESG (Environment, Social, and Governance) by applying lower risk weight/provision to ESG loans.

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Annex VIII. Governance and Anti-Corruption Frameworks[1]

Authorities are taking welcome steps to tackle corruption and strengthen the rule of law, yet key challenges remain. *In recent years, Cambodia has adopted a renewed anti-corruption action plan (2020-2025), created an Anti-Corruption Institution (ACI)[2], and has taken steps to improve its legal anti-corruption framework. Additionally, it has taken measures to improve procurement procedures, and to enhance access to judicial and fiscal information. Lastly, it has adopted measures toward the preparation of a National Risk Assessment (NRA), consistent with FATF recommendations. However, corruption vulnerabilities and rule of law weaknesses remain substantial in several areas. Whistleblower and transparency laws are still pending, improvement and digitization of the asset declaration system should be pursued, and securing sufficient human and technological resources for investigative and monitoring agencies has been challenging.*

1. **A special focus was made during the 2022 Article IV consultations on anti-corruption and rule of law.** This is consistent with the requirement for assessments in the context of a medium-term surveillance cycle, following the framework for enhanced Fund engagement on governance issues adopted by the IMF Board in 2018. The aim was to analyze key corruption vulnerabilities and rule of law weaknesses, to take stock of progress in related rule of law and anti-corruption policies and frameworks, and assess their implementation. To that end, the IMF team collected and reviewed relevant documents and met with representatives of the key governmental institutions involved in implementing Cambodia's governance and anti-corruption framework[3]. This Annex summarizes conclusions and provides actionable recommendations.

A. Anti-Corruption

Corruption Vulnerabilities

2. **Petty corruption remains a significant concern in Cambodia, although indicators show some progress, and corruption risks in different sectors remain challenging.** Additional preventive steps could be considered. According to the Global Corruption Barometer, a survey conducted by Transparency International, the percentage of respondents reporting having paid bribes lowered, from at least 50 percent in 2013 to 37 percent in 2020. The latter percentage, however, is well above regional and global averages[4]. Moreover, according to the

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[1] Prepared by Camilo Enciso (LEG).

[2] Composed by the National Council Against Corruption (NCAC) and the Anti-Corruption Unit (ACU).

[3] Staff met with the Financial Intelligence Unit (CAFIU), Ministry of Justice, National Audit Authority (NAA), Anti-Corruption Institution (ACI), and the General Department of Procurement at the Ministry of Economy and Finance. In addition, the IMF team met with civil society representatives.

[4] 2013_GlobalCorruptionBarometer_EN_200525_112757.pdf (transparencycdn.org) and 2020 Global Corruption Barometer - Asia 2020 - Transparency.org According to Transparency International: "The results are weighted to

(Continued)

ACI, some sectors face significant challenges for the prevention of corruption, including education, social, and covid-related spending. Challenges in the education sector are particularly sensitive, due to recent reforms that have granted enhanced autonomy to provinces to manage funds for education.

3. **Transparency in the extractive industry remains limited.** The extractive industry is one of the sectors with higher risks of corruption in most of the world. Nonetheless, Cambodia has not adopted enhanced risk prevention tools to prevent corruption in the sector. The National Risk Assessment would be expected to provide insights on specific vulnerabilities in the extractive industries and allow for the adoption of improved governance and administration reforms impacting the sector, in line with Articles 10.c. and 61 of the United Nations Convention Against Corruption (UNCAC).

4. **Access to information and monitoring of concessions agreements for the use of land and/or development of infrastructure projects, requires further attention**. Cambodia has seen significant development and foreign investment in land development-related projects. However, lack of access to information creates public distrust and corruption risks. Moreover, concerns for inadequate monitoring have been raised and investigations have been conducted by the Anticorruption Institution (ACI).

5. **The authorities have adopted steps to improve procurement regulation and transparency, yet access to information, statistics, and data remain challenging.** The lack of tools to facilitate "big data" management of procurement and public contracts, and insufficient publication of documents of all the phases of public procurement, increases the risk of corruption, conflicts of interest, and influence peddling. Further, lack of access to information increases vulnerabilities to favoritism, tenders with one single offeror, collusion, and manipulation of the tender process. Likewise, decentralization aims of a new draft procurement law generate additional risks for corruption which need to be addressed, particularly in consideration to the reduced oversight of public spending in said regions.

6. **Corruption risks in other sectors remain challenging. Additional preventive steps could be considered.** According to the ACI, some sectors face significant challenges for the prevention of corruption, including education, social, and Covid-19-related spending. Challenges in the education sector are particularly sensitive, due to recent reforms that have granted enhanced autonomy to provinces to manage funds for education.

Anti-Corruption Frameworks

7. **The ACI framework includes safeguards to its independence, which could be further strengthened.** The independence of the ACI has benefited from the creation and operation of

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be nationally representative according to available population data. They have a margin of error ranging from +/- 2.2 to +/- 3.1percentage points at a 95 per cent confidence level."

the National Council Against Anticorruption (NCAC) and from the introduction of Article 40 to the Anti-Corruption Law, which penalizes the threat, obstruction, or interference in the work of the ACI. Nonetheless, concerns for lack of independence remain, and improvements to the selection process of ACI directors and investigators should be adopted. For that purpose, authorities could consider adjusting the composition of the ACI and the NCAC ensuring adequate independence and autonomy, as required by UNCAC (Articles 2.2. and 11) and, by improving the selection process of commissioners, investigators, technical experts, and staff. Further, they should ensure the ACI provides adequate training to staff and has sufficient resources to adopt technological tools that may be needed[5] (e.g. Wiretapping, automated review of digital information of assets declarations, or adequate servers needed to save, protect, and analyze digital information in the context of corruption investigations).

8. The current asset disclosure regime for top officials should be improved. Asset declarations (AD) are submitted (according to authorities) by nearly all obligated subjects, amounting to nearly 70,000 per year. However, the ADs are only verified when public officials are under investigation by enforcement authorities, instead of being monitored on a permanent basis for accuracy and for detection of suspicious economic increase by using a risk-based approach. Also, asset declarations are not made public, nor cover information of children and spouses, except for general contact data. Furthermore, ADs are collected manually and stored in closed envelopes, and therefore do not facilitate massive digital assessment and risk detection. Thus, sanctions against obligated subjects are uncommon.

9. Efforts to investigate corruption and confiscate the proceeds generated should be further pursued. The authorities should make better use of AML/CFT tools to support such efforts. While the CAFIU has been disseminating financial intelligence on potential corruption cases, the number of investigations initiated remains low. To date there is no evidence of statistics that can help corroborate the effective collaboration between the Financial Intelligence Unit (CAFIU) and ACI in connection with the recuperation of assets lost to corruption. Further efforts to enhance cooperation should be made. Furthermore, the authorities should prioritize confiscation of the proceeds of corruption, including by continuing enhancing capacity in this area, to prevent the corrupt from enjoying their ill-gotten assets and to help disincentivize future corruption.

10. After its creation in 2002, with support of the Asian Development Bank, Cambodia has been strengthening its National Audit Authority (NAA[6]). The NAA is an independent authority, with a separate budget, that reports directly to the National Assembly, the Senate, and the government. It is tasked with conducting external audits over the government and to audit accounting records, financial reports, management system, operation controls, and programs of the governmental institutions. The head of the NAA is appointed by a two-thirds majority vote of

[5] Article 2 of UNCAC requires states to provide anticorruption bodies the necessary resources to carry out its functions, as follows: "(…) The necessary material resources and specialized staff, as well as training that such staff may require to carry out their functions, should be provided."

[6] Audit Profile: National Audit Authority of Cambodia - ProQuest

National Assembly members, at the recommendation of the government, and has the same level as senior minister. Some additional improvements are connected to the adoption of new accounting standards and regulations, and to the recruitment of specialized staff. Going forward, authorities are encouraged to ensure the NAA has adequate resources to undertake its mission and to deliver adequate training to NAA's officials.

11. Cambodia does not currently have whistleblower protection and access to information laws. More concerning, article 41 of the Anticorruption Law criminalizes individuals filing reports of corruption that may end up being considered groundless by the government, by imposing penalties for the crimes of *defamation* or *disinformation*. Such provision, added to the lack of a comprehensive whistleblower protection law, can severely undermine the likelihood of whistleblowers from coming forward, particularly given the apparent low confidence of citizens in judicial institutions in Cambodia. Further, the lack of existence of a law of access to information diminishes the ability of citizens, watchdogs, and the media to assess the effectiveness of government, and to hold public officials involved accountable for wrongdoing. Thus, the adoption of a whistleblower protection law and a transparency and access to information law would be advisable, and would help detect corruption cases, and facilitate public oversight and increased accountability. Doing so would also be consistent with UNCAC requirements under Articles 13.1, 13.2, and 33.

12. Finally, the country is in the process of passing a new procurement law, following the recent introduction of a new procurement platform[7]. However, some deficiencies need to be addressed. Access to information must be enhanced to ensure openness of data by default while protecting confidential information where needed. Further, information of beneficial owners of offerors in procurement processes and public contracts should be collected and managed by procurement authorities.

B. Rule of Law[8]

Rule of Law Weaknesses

13. Rule of law weaknesses are perceived to be substantial. The 2021 scores under the World Justice Project's (WJP) Rule of Law Index are particularly low, with a total score of 0.32 (over 1) in 2021[9]. In the same line, according to the latest assessment of the Transformation

[7] http://gdpp.gov.kh/

[8] This section covers weaknesses and frameworks in connection with the enforcement of contracts and property rights, and considering that the most important determinant with respect to the enforcement of economic rights is the quality of the judiciary—both in terms of its technical capacity and its independence from private influence and public interference.

[9] "The World Justice Project (WJP) Rule of Law Index measures the rule of law based on global surveys of more than 138,000 households and 4,200 legal practitioners and experts. It is the world's leading source for original, independent data on the rule of law. The Index presents a portrait of the rule of law in 139 countries and jurisdictions by providing scores and rankings based on eight factors: Constraints on Government Powers,

(Continued)

Index (BTI) Cambodia obtained an overall score of 1.8 over 5 in the rule of law component, comprised by measures on separation of powers (1 out of five), independent judiciary (2 out of five), prosecution of office abuse (2 out of five), and civil rights (2 out of five[10]).

14. Independence and fair and equal access to the administration of justice are perceived as lacking in the judicial sector thus jeopardizing contract enforcement and property rights protection. The judicial system is perceived as one that does not provide assuredness of even-handedness, equal access, efficiency, and fair play. (See, for example, the BTI assessment, in which Cambodia obtained a score of 1.8 out of 10 in 2022, decreasing from 2.0 in 2018 and 2.5 in 2014[11]). This implies that distrust in the court system to ensure contract enforcement and property rights is widespread.

Rule of Law Frameworks

15. Authorities have made positive reforms toward increased access to information on existing norms and judicial decisions. Legislation, decrees, and some judicial decisions are being published online in the portal of the Ministry of Justice[12]. However, not all judicial decisions are accessible, and some norms, particularly those adopted by local governments, are difficult to access.

16. Protection of land rights presents important challenges. According to different actors of the private sector and the BTI project[13], Cambodia has had low performance in connection to land administration, including the reliability of infrastructure, transparency of information, geographic coverage, land dispute resolution, and equal access to property rights. The cadastral system faces numerous shortcomings, particularly in connection with different land titles and state agencies involved[14]. The announcement of the government to adopt and implement a Master Plan for State Property Management is welcome.

17. The reliability of dispute resolution, contract enforcement, and dispute settlement mechanisms should be strengthened. According to rule of law assessments conducted by the World Bank, Cambodia's systems for dispute resolution, contract enforcement and dispute settlement are highly vulnerable. This was confirmed by different actors interviewed by staff

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Absence of Corruption, Open Government, Fundamental Rights, Order and Security, Regulatory Enforcement, Civil Justice, and Criminal Justice." On a methodological note: Use of these indicators should be considered carefully, as they are derived from perceptions-based data, and methodology can be found here: WJP-INDEX-21.pdf (worldjusticeproject.org) P. 181-187. Further the last survey for Cambodia, including 1000 individuals has been made in 2014.

[10] Transformation Atlas 2022 (bti-project.org) Further explanations on the methodology applied by BTI can be found here: BTI 2022 (bti-project.org) No specific confidence intervals are available.

[11] Transformation Atlas 2022 (bti-project.org)

[12] https://www.moj.gov.kh

[13] Transformation Atlas 2022 (bti-project.org)

[14] Transformation Atlas 2022 (bti-project.org)

during the mission, including development partners and civil society organizations. Overall, enhanced efforts are needed to upgrade the quality and trust in the court system[15].

Recommendations:

1) Amend the Anti-Corruption Law and the Assets Declaration regime to ensure:
   a) Public access to asset declarations of high-level officials,
   b) That the declaration form requires information on assets and interests of children and spouses of obligated subjects (instead of just general contact data),
   c) Independence of ACI commissioners, investigators, and staff

2) Adopt measures and tools to ensures effectiveness of the asset declarations regime, including:
   a) New technological tools that allow for the collection, management, and risk-based audits over assets declarations.
   b) A phased strategic plan to run risk-based audits over assets declarations.

3) Reinforce inter-agency cooperation to:
   a) Strengthen cooperation between ACI and CAFIU, by adopting a joint task force to identify and recuperate assets lost to corruption or illicit enrichment.
   b) Strengthen cooperation between ACI and the NAA, by adopting a joint task force to identify and recuperate assets lost to corruption or illicit enrichment.

4) Provide more resources and training for the NAA to:
   a) Provide additional resources to the NAA to improve human capacity and training centers, particularly—but not only—for conducting audits of financial management systems based on current international accounting standards, to help prevent and deter loss of public funds to corruption.
   b) Develop a strategic plan to ensure fiscal oversight over public spending in areas with corruption vulnerabilities, including—but not limited to—education, land concession agreements, and high-cost infrastructure projects.

5) Adopt measures to protect whistleblowers of acts of corruption, by:
   a) Enacting a comprehensive whistleblower protection law, consistent with international good practices, that ensures whistleblowers' protection from any form of retaliation.
   b) Derogating article 41 of the Anti Corruption Law, which deters individuals from reporting corruption cases, out of fear to being subject of criminal prosecution.

6) Adopt measures to increase transparency and access to information by:

[15] OECD Investment Policy Reviews: Cambodia 2018 | en | OECD

a) Adopting a law on transparency, that regulates the matter based in good international practice, including a definition of public information and documents, petition channels, and exceptions.
b) Adopting necessary tools to ensure access to big data and documents on public procurement, that may allow for enhanced oversight, accountability, and improved procurement-related policies.
c) Demanding disclosure of beneficial ownership in public contracts.
d) Ensuring publication of all legal norms, regulations, and judicial decisions, and considering adopting of legal tracking systems for the courts that may contribute to better court management and traceability of legal processes.

Annex IX. Fiscal Rules in Cambodia[1]

Despite a history of prudent fiscal policy, new challenges suggest Cambodia would benefit from establishing a well-designed fiscal rules framework to further ensure fiscal sustainability. While Cambodian authorities have recently adopted a debt rule, it does not provide sufficient guidance for medium-term fiscal policy. Staff recommends adopting a debt rule in percent of GDP in nominal terms, combined with an overall deficit ceiling to ensure sustainability and operational feasibility.

A. Context

1. **Despite a history of prudent fiscal policy, new challenges suggest Cambodia would benefit from establishing a well-designed fiscal rules framework to further ensure fiscal sustainability.** While debt-to-GDP ratios had been relatively low and stable in Cambodia for more than a decade prior to the COVID-19 pandemic, debt has increased due and in response to the pandemic. Going forward, heightened uncertainty and upward pressures on borrowing costs (due to income level graduation and domestic debt market development) increase the need for a careful assessment of fiscal space, to ensure that new ambitious policies (including for social protection or infrastructure) can be implemented while not impeding fiscal sustainability.

B. Guiding Principles and Common Practice

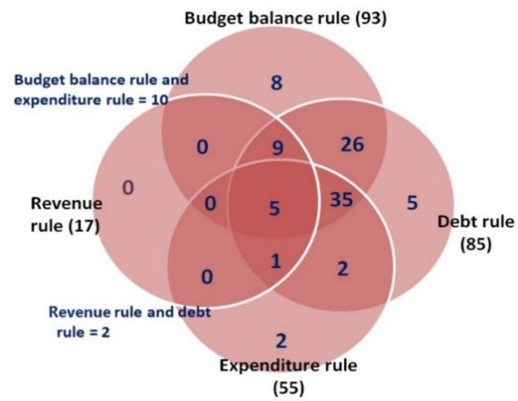
2. **Well-designed fiscal frameworks should specify operational limit(s) on fiscal aggregates and a medium-term fiscal anchor linked to the final objective of fiscal policy.** A natural medium-term anchor is the debt-to-GDP ratio, which provides a guide for both expectations and nearer term policies, and whose threshold can be calibrated to ensure the long-term fiscal sustainability of public finances. The fiscal rules framework should also include shorter-term operational rule(s), under the direct control of governments, that have close and predictable links to debt dynamics.

3. **Effective fiscal rules should display some key properties—simplicity, flexibility, and enforceability while ensuring sustainability and allowing stabilization.** These properties are difficult to achieve simultaneously and involve tradeoffs. Countries should find the right balance, according to their individual preferences and characteristics. Compliance with the rule should ensure long-term debt sustainability. Following the rule should not exacerbate economic cycles (stabilization). Simplicity requires the rule to be easily understood by decision makers and the public. Credible rules should be able to withstand negative shocks, highlighting the need to improve flexibility (for example through well-designed escape clauses to account for unexpected events). To be effective, rules should be monitored and enforced, and deviations from targets should have a cost for the government. They should also have a broad institutional and

[1] This note was prepared by Juliana Araujo based on the findings of the 2022 FAD Technical Assistance Report "Cambodia: Towards A Stronger Fiscal Framework" by Fabien Gonguet, Laura Doherty, William Gbohoui, Kentaro Katayama, Marie-Hélène Le Manchec, Delphine Moretti and Holger Van Eden

economic coverage as limitations in coverage can open loopholes that encourage circumventing the rule and undermine the credibility of the fiscal framework.

Figure 1. Common Adoption of Fiscal Rules: A Snapshot in 2021
(Number of countries)



Sources: IMF Fiscal Rules Dataset: 1985–2021; Davoodi et al. (2022), "Fiscal Rules and Fiscal Councils: Recent Trends and Performance during the Pandemic", IMF Working Paper No. 22/11.

4. **Fiscal rules could be categorized into four types: debt, budget balance, expenditure, and revenue rules (the last three are often called operational rules).** Debt rules and budget balance rules are by far the most frequent (Figure 1). Yet, expenditure rules are increasingly common, often set as a ceiling on annual expenditure growth. Revenue rules have been less used, partly reflecting the fact that governments have less control over yearly revenues. Countries typically combine debt rules with one or several operational rules: about 70 percent of countries with fiscal rules have a debt rule combined with operational limits on annual budget aggregates, most often a budget balance rule and/or an expenditure rule. The most common rules among EMDCs are a combination of a debt rule with a budget balance rule. However, expenditure rules are far more popular in AEs than EMDCs.

C. A Framework for Cambodia

5. **While Cambodian authorities have recently adopted a debt rule, it does not provide sufficient guidance for medium-term fiscal policy.** The government established several constraints on government debt in the Public Debt Management Strategy (PDMS) 2019-23. The debt ceiling (comprising public domestic debt, public external debt and publicly guaranteed debt) is set at 55 percent of GDP, of which the ceilings on the present values of external and domestic debt ratios are 40 percent and 15 percent of GDP, respectively. While this qualifies as a debt rule, it doesn't provide proper medium-term guidance, as the level of this ceiling is equivalent to the DSA threshold, which should not be targeted. Further, while an "implicit" deficit ceiling of 5 percent of GDP (MEF definition) is used as an internal reference during the budget process, no formal or explicit operational rule is currently implemented.

6. Staff recommends adopting a debt rule in percent of GDP in nominal terms, combined with an overall deficit ceiling to ensure sustainability and operational feasibility. A medium-term debt anchor in nominal terms, expressed in percent of GDP, is appropriate for Cambodia because it is simple to compute and monitor and easy to communicate to the public. Furthermore, a rule on debt is pertinent, given the recent increase in debt and the expected change in structure and composition of debt (e.g., expected decline in concessional financing, planned issuances of local-currency governments). The lack of experience with fiscal rules, combined with capacity constraints, make a overall deficit target an appropriate operational rule for Cambodia. Its direct link to debt dynamics also helps to ensure sustainability.

7. The debt anchor should be set in gross terms and continue to cover all public and publicly guaranteed debt. Gross debt constitutes the most appropriate fiscal anchor for several reasons. Net debt is complicated to measure and communicate because it is difficult to define which government assets are truly liquid. In addition, targeting net debt could also mask important below-the-line financing operations (like the recapitalization of a public bank or loans to state-owned enterprises) that would be accounted for under the gross debt concept, concealing the build-up of fiscal risks over time. In terms of coverage, the debt anchor should continue to include all public and publicly guaranteed debt. The fiscal rule should cover all entities that carry significant risks to the budget. All loans or projects guaranteed by the government as well as on-lending to SOEs should continue to be accounted for.

8. Further work is required to define the escape clause and the corrective mechanisms. Currently, Cambodia is considering an escape clause that suspends the fiscal rules for a number of unexpected events. These events are identified in the draft 2023-24 Medium-Term Fiscal Framework (MTFF) document i.e. "such as natural disasters, pandemics, national emergencies or urgent need for national interests, that trigger significant changes in macroeconomic assumptions". The first three events listed would benefit from further specification, with a specific trigger identified (i.e. the Prime Minister formally declaring a national emergency). However, the last event is too broadly defined, leaving the door open to wide interpretation and possible misuse. GDP should continue to review literature on the international experience with escape clauses to strengthen the concepts of trigger events, trigger and monitoring authority in Cambodia, and the requirements for government to inform Parliament when an escape clause is invoked and provide a specified pathway to return to the rules. In the first instance, these should be further defined as part of the MTFF document. Looking forward, these should be included in a fiscal responsibility law (FRL) when (and if) Cambodia decides to develop one.

9. A number of options could be considered to encourage compliance in Cambodia, once the government has committed to implement the new fiscal rules framework. Currently, there have been no proposals on how to ensure compliance with the fiscal rule, and monitoring arrangements are still to be determined. The PDMS includes a ceiling on the present value of total public debt of 55 percent of GDP and outlines a mechanism for regular monitoring and evaluating progress. The current MTFF document does not specify requirements for compliance with the envisaged fiscal rules, and there is no commitment to publish monitoring reports. In the first instance, responsibility for rule monitoring should be primarily assigned to GDP. GDP would be responsible for reporting quarterly to Cabinet on compliance with the rule and producing a half-year report to be submitted to Parliament that would be published alongside (or attached to) the MTFF. The report on expected compliance with fiscal rules during that fiscal year should flag any noncompliance risks and propose any necessary corrective measures to ensure fiscal rules are met. At this current juncture, in line with Cambodia's high-quality but small technical cadre, setting up an independent fiscal council would be difficult in the short to medium-term.

CAMBODIA

November 12, 2022

STAFF REPORT FOR THE 2022 ARTICLE IV CONSULTATION—DEBT SUSTAINABILITY ANALYSIS

Approved By
Anne-Marie Gulde Wolf and Andrea Schaechter (IMF), and Marcello Estevão and Hassan Zaman (IDA).

Prepared by Staff of the International Monetary Fund and the International Development Association

Cambodia: Joint Bank-Fund Debt Sustainability Analysis	
Risk of external debt distress	*Low*
Overall risk of debt distress	*Low*
Granularity in the risk rating	*Not applicable*
Application of judgment	*Yes: the breach of the export shock stress test is small and temporary.*

Cambodia remains at low risk of external and overall debt distress under the Low-Income Countries Debt Sustainability Framework (LIC-DSF).[1] The current debt-carrying capacity[2] remains consistent with a medium classification. The baseline scenario assumes steady economic recovery, largely driven by exports of tourism services and, to a lesser extent, manufacturing goods, notwithstanding pressures on external demand in the near term. The total PPG debt-to-GDP ratio is projected to rise by around 4 percentage points during the next decade. The present value of the external debt-to-GDP ratio breaches its threshold in the exports stress test, which would imply a moderate risk rating. However, the breaches are small, short-lived (only four periods, the last barely), and driven by the exceptional volatility of exports in 2020 that has increased the sample volatility for the standardized shock. Moreover, other debt burden indicators are projected to remain well below their thresholds under the baseline and the shock scenarios. Given the expectation

[1] This DSA follows the Guidance Note on the Bank-Fund Debt Sustainability Framework for Low Income Countries (imf.org), February 2018 (GN).

[2] Cambodia's Composite Indicator (CI) index, based on the April 2022 WEO update and the World Bank's 2020 CPIA, indicates that the country's debt-carrying capacity remains medium (2.968), the same as in the 2021 DSA (in which the CI index was 2.966).

of a steady and solid recovery, and because the breaches for one of the tests are small, temporary, and driven by the exceptional volatility of exports in 2020, judgment has been applied that the external risk of debt distress remains low. Nonetheless, the analysis shows that debt sustainability remains vulnerable to shocks in exports and growth. These findings reinforce the importance of implementing reforms to increase the economy's resilience to external shocks and to facilitate export and economic diversification. Efforts to mobilize fiscal revenue, strengthen the Public Investment Management Framework, and further enhance monitoring of Public-Private partnerships (PPP) and financial sector risks are needed to ensure debt sustainability over the medium term.

PUBLIC DEBT COVERAGE

1. **The DSA covers central government debt and debt guaranteed by the central government to state-owned enterprises (SOEs).** By law, state and local governments and the central bank do not engage in borrowing, and SOEs do not contract non-guaranteed loans. Currently, there are no extra-budgetary funds, and the National Social Security Fund is funded by deposits and does not constitute a liability for the general government (text table 1). Consistent with the previous DSA, external debt is defined on a currency basis.

Text Table 1. Public Sector Debt Coverage

Subsectors of the public sector	Sub-sectors covered
Central government	X
State and local government	
Other elements in the general government	
o/w: Social security fund	
o/w: Extra budgetary funds (EBFs)	
Guarantees (to other entities in the public and private sector, including to SOEs)	X
Central bank (borrowed on behalf of the government)	X
Non-guaranteed SOE debt	X

Text Table 2. Design of Contingent Liability Stress Test

The country's coverage of public debt	The central government, central bank, government-guaranteed debt, non-guaranteed SOE debt			
	Default		Used for the analysis	Reasons for deviations from the default settings
Other elements of the general government not captured in 1.	0	percent of GDP	0.0	
SoE's debt (guaranteed and not guaranteed by the government) 1/	2	percent of GDP	0.0	Not allowed by law
PPP	35	percent of PPP stock	5.8	Staff estimates
Financial market (the default value of 5 percent of GDP is the minimum value)	5	percent of GDP	10.0	Giving risks emerging from private external borrowing
Total (2+3+4+5) (in percent of GDP)			15.8	

1/ The default shock of 2% of GDP will be triggered for countries whose government-guaranteed debt is not fully captured under the country's public debt definition (1.). If it is already included in the government debt (1.) and risks associated with SoE's debt not guaranteed by the government is assessed to be negligible, a country team may reduce this to 0%.

2. **The DSA includes contingent liability stress tests for PPPs and a financial market shock** (text table 2).

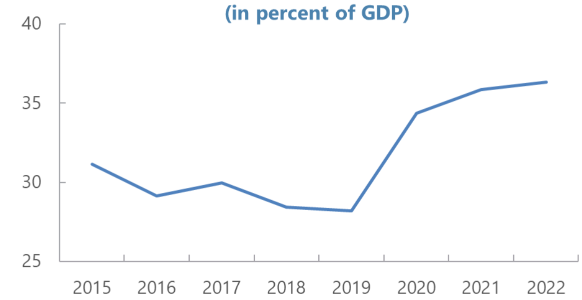
- The shock scenario for the SOE debt is set to 0 percent of GDP because, by law, SOEs do not engage in non-guaranteed external borrowing, and guarantees to SOEs are included in public debt. According to the IMF's Investment and Capital Stock Dataset and information provided by the authorities, the capital stock of PPPs is estimated at 16.5 percent of GDP as end of 2021, corresponding to a contingent liability of 5.8 percent of GDP.

- The standard financial market shock is intensified in this DSA. Specifically, the financial market shock assumes contingent liabilities from financial markets to be 10 percent of GDP, twice the default value of 5 percent of GDP. This change is included to account for the risks emerging from private sector debt that has grown steadily as a share of nominal GDP. Around 7 percent of the total stock of outstanding credit has been restructured (amounting to 13 percent of GDP; given the current stock of restructured loans, further losses may yet have to be recognized by banks.

BACKGROUND ON DEBT

3. Cambodia's external public debt amounted to around US$ 9.5 billion (36 percent of GDP) by end 2021. The external debt-to-GDP ratio increased slightly in 2021, by 1.5 percentage points, following a more sizable increase in 2020 and given slack in the economy and extended fiscal responses to the COVID-19 pandemic (text figure 1). Bilateral debt continues to account for around 70 percent of total external debt, with more than half owed to China (text table 3).[3] External debt has been accrued on concessional terms, with a present value of around 24 percent of GDP at end-2021. The debt stock includes legacy arrears to the Russian Federation and the United States of about 2.4 percent of GDP. As the status of negotiations of these arrears remains unchanged compared to the previous DSA, this analysis assumes no debt restructuring.[4] In addition, as the arrears reflect diplomatic disagreements, they do not trigger an "in debt distress" rating.

Text Figure 1. External Public Debt (in percent of GDP)



Sources: Cambodian authorities; and IMF estimates.

Text Table 3. External Public Debt (2021)

	In million of U.S. dollars	In percent of GDP	In percent of external debt
Total	9502.7	35.7	100.0
Multilateral	2892.2	10.9	30.4
Bilateral	6,610.5	24.9	69.6
of which: China	4,054.1	15.2	42.7

Sources: Cambodia authorities; and IMF estimates.

4. Public domestic debt remains negligible. Public domestic debt comprised only non-marketable bonds issued by SOEs, and the outstanding debt (about US$ 1.6 million by end 2019) had been fully repaid in early 2020. To support financial market development, the authorities started to issue local-currency government bonds in 2022,[5] while strengthening market infrastructure to manage issuance, registration, and trading of domestic securities.

5. PPPs are assumed to continue to play an important role in financing investment projects, in expectation of diminishing access to concessional financing and slow progress in

[3] According to Cambodia Public Debt Statistical Bulletin, (see Table 3 "Debt Stock"), the multilateral debt in the text table 3 is breakdown by the Asian Development Bank as US$ 1,943 million, the World Bank as US$ 730 million, and others. (Nothing is owed to the IMF.)

[4] See Cambodia Public Debt Statistical Bulletin, Table 13 ("Old Debt Under Negotiation"). The data reflect principal amounts, i.e. excluding any accumulated interest. The arrears relate to obligations made by the then-government in the early 1970s, which have been refuted by subsequent governments. There has been no progress at resolving this issue during Paris Club negotiations.

[5] The authorities drafted the preliminary "Policy Framework of Development on the Government Securities" in September 2021, which aimed at (i) the first securities issuance in 2022, (ii) setting principles for the usage of fund from government securities, and (iii) appointing the NBC as a fiscal agent and arranging the issuance operations. In September 2022, the authorities issued a local-currency bond for the first time, floating KHR 41.7 billion (around US$ 10 million) at a 2.2 percent yield with a tenor of 1 year. The authorities plan further issuances up to US$ 300 million during the rest of 2022, including at longer maturities.

developing domestic debt markets. The PPP stock more than doubled between 2010 and 2015, and was estimated at around 16.5 percent of GDP by end-2021. The authorities have been taking welcome steps to strengthen the PPP framework in line with past Fund recommendations, including a system for risk assessment and the necessary legal, regulatory, and institutional arrangement for PPP management.[6]

6. **Private external debts in Cambodia are excluded from this analysis.** Staff estimates private external debt at about 39 percent of GDP in 2021, broadly unchanged since last year.[7] Risks emerging from excessive external borrowing by the private sector could increase the government's exposure to contingent liabilities.

BACKGROUND ON MACRO FORECASTS

7. **The Cambodian economy was hit hard by the COVID-19 pandemic, but damage was mitigated by policy measures.** Cambodia was hit first by external shocks, such as the loss of tourism from early 2020 and a collapse in demand for manufactured goods, and then community spread of the virus in in 2021. However, large fiscal buffers provided room for increased spending on health care, employment support, and cash transfers to households; and substantial foreign exchange reserves kept the exchange rate from coming under significant pressure.

8. **From the second half of 2021, the Cambodian economy showed stronger signs of recovery from COVID-19 pandemic stresses.** Growth was driven mainly by exports of goods, while growth in construction and real estate—large contributors to growth before the crisis—was relatively weak.

9. **Credit growth has continued to be strong, and private sector indebtedness is now very high.**

- Credit growth averaged around 24 percent y/y from 2013 to 2019 and slowed only mildly during the pandemic. Private sector debt growth has consistently outstripped growth in nominal GDP; outstanding private sector credit reached 170 percent of GDP by end 2021, a ratio above those of other countries in the region, suggesting that the level cannot be safely dismissed as driven by financial deepening. Moreover, these numbers do not account for credit issued by unsupervised lenders (such as real estate developers and pawn shops), which could be sizeable. Restructured loans in June 2022 are estimated to be about 7 percent of lending (13 percent of GDP), and non-performing loans have risen to 2.8 percent of outstanding loans (nearly 4½ percent of GDP).

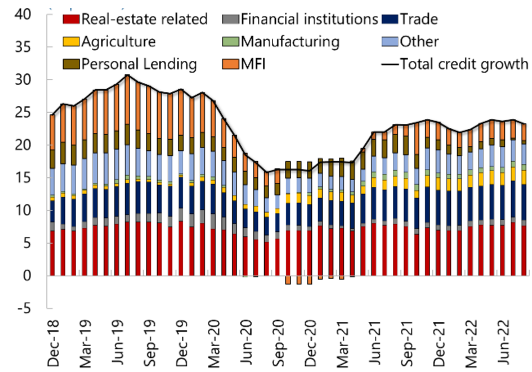
[6] For example, a central PPP unit had been established under the Ministry of Economy and Finance, and a new law on PPP was enacted in November 2021.

[7] According to CEIC data, the total external debt amounted to US$ 20 billion in 2021, and private debt can be estimated at about US$ 11 billion after deducting PPG external debt.

- Credit growth has not been driven by only one or two sectors of the economy (e.g. overheating in real estate and construction) but has been strong across all sectors, with retail and wholesale trade accounting for the largest share of total debt outstanding, followed by commercial real estate and construction.[8] Roughly two thirds of loans are corporate. A substantial portion of loans classified as to households might be personal borrowing for small businesses. The number of loans has increased but the number of borrowers has increased at a slower pace, suggesting that some borrowers are becoming more leveraged.

Text Figure 2. Contribution to Private Credit Growth

(In percent)



Source: Cambodia authorities

- Credit growth was associated in 2020 and 2021 with growth in broad money that, although lower than that in 2019, was still stronger than growth in nominal GDP, driven in part by the expansion in the central bank's balance sheet as the government drew down on deposits at the central bank to finance fiscal support during the pandemic. It was also supported by the steady inflow of FX deposits in commercial banks,[9] and a steady increase in the loan-to-deposit ratio.

10. There are signs of damage from the crisis. Lack of employment data make it difficult to assess scarring effects in the labor market. But test scores indicate that lost schooling hours during the COVID-19 pandemic has damaged human capital attainment. Approvals of large (foreign-financed) projects remain lower than before the crisis and falling lease yields indicate excess supply of commercial property; business registrations appear to be recovering, but liquidations are have been increasing.

11. 2022 has brought new stresses:

- China is a significant source of foreign investment, particularly in real estate, and the major supplier of textiles to the garments industry. The slowdown in China and further lockdowns therefore have the potential to slow the Cambodian economy. Continued restrictions on movement mean that a quick return to pre-crisis tourist numbers is unlikely, given the importance of Chinese tourists to Cambodia.

- Although Cambodia has limited export and financial exposure to Ukraine and Russia, Europe is a major market for its manufactures.

[8] The growth in credit is almost entirely to the private sector—that to government was less than one percent.

[9] The expansion in the central bank's balance sheet was only partially offset by reductions in FX reserves and liquidity operations.

- The tightening of monetary conditions in advanced economies will have mostly indirect effects, through external demand. However, although the financial system is mostly reliant on deposit funding, demand for wholesale funding by some institutions has been increasing. The plans to increase issuance of sovereign debt will face a more competitive environment for funding.

12. These new stresses have been associated with a surge in inflation. Cambodia's reliance on imported fuel is higher than many other regional comparators; the recent increases in global fuel and fertilizer prices have resulted in historically high inflation rates. Headline inflation hit 7.8 percent y/y in June 2022 but has subsequently fallen to 4.9 percent y/y in August. The contribution of core items has increased, but remains muted so far.

13. The authorities' have largely continued with crisis policy responses, such as loans and guarantees, tax breaks, and wage subsidies and retraining. The authorities plan to fold the system of cash transfers introduced in 2020 into a broader social protection program. The National Bank of Cambodia (NBC) has maintained reserve requirements and the capital conservation buffer at current levels but has issued instructions for the end of loan forbearance.

14. The recovery is assumed to continue in the baseline projections. The Cambodian economy is projected to grow at 5 percent in 2022, nearly 5½ percent in 2023, reflecting external pressures and some drag from real estate and construction. Growth is expected to increase to just over 6 percent in 2024, and to gradually return to trend growth rates of around 6½ percent over the medium term, in line with projections in the previous DSA (text table 4). The trend growth rate is somewhat below pre-COVID-19 rates of 7 to 7½ percent, but comparable with those seen in neighboring countries at similar stages of development, and reflects a judgment that, although the COVID-19 crisis will have some lingering effects, the authorities' ongoing reforms (e.g. the new investment law) and new trade agreements (specifically, the RCEP and an FTA with China) will support growth over the medium term.

Text Table 4. Baseline Macroeconomic Assumptions (2021-2030)

	Previous DSA (2021)				Current DSA (2022)			
	2021	2022	2023	2024-2030	2021	2022	2023	2024-2030
Real GDP (%, YOY)	2.2	5.1	5.9	6.4	3.0	5.0	5.4	6.4
Inflation (%, YOY)	2.9	3.0	3.0	3.2	2.9	5.8	3.5	3.0
Primary Deficit (% to GDP)	5.2	3.6	3.4	2.9	6.7	3.8	4.7	2.6
Current Account Deficit (% to GDP)	26.9	16.7	9.2	8.8	47.5	30.0	14.1	7.2

Sources: staff estimates and projections

- *Growth and inflation.* The baseline outlook is for stronger growth, notwithstanding external pressures and risks. Growth is supported by relatively moderate but nonetheless solid goods exports, continued recovery of tourism, and ongoing policy support. It is dampened by the impact of inflation on real disposal income and the slowdowns in external demand growth. Inflation is expected to peak this year, be lower in 2023, and then decline further, assuming it remains mostly confined to imported goods.

- *External sector*. The current account deficit is expected to narrow in 2022 as energy prices and gold imports recede. Over the medium term, the current account deficit is estimated to narrow further as the tourism sector normalizes. Given the sizable current account deficit was partially offset by financial inflows, gross reserves decreased slightly in 2021, to US$ 21 billion. They are expected to remain at around 8 months of projected imports over the projection horizon.

- *Fiscal sector*. Staff projects the fiscal deficit to narrow to 4 percent of GDP in 2022, from 7 percent in 2021, on the back of broad-based tax revenue rebound and lower spending, increase somewhat in 2023, and to decline steadily thereafter. Staff expects that fiscal support will be contained in 2022 because of winding back emergency COVID-19 healthcare spending. In 2023, current spending is expected to increase slightly, reflecting planned wage increases and some decompression of government operations (e.g., travel), and social protection and capital spending levels are to be maintained. The overall deficit is then expected to narrow and to stabilize at around 3 percent of GDP over the long run, consistent with debt stabilizing at 40 percent of GDP.

15. Uncertainty around the outlook is particularly high; risks are tilted to the downside.

- *Credit:* The level of private debt raises concerns about the drag on the economy if borrowers struggle to meet repayments and large amounts of non-interest-paying assets in banks' balance sheets.

- *Conditions in key large economies:* Cambodia is highly export oriented. Further lockdowns in China could lead Cambodian manufacturers to suspend production for want of supplies, while a further slowdown could slow inward investment. Demand in advanced countries is vulnerable to tightening financial conditions; vulnerabilities in Europe are accentuated by energy supply risks.

- *Inflation:* Global food and fuel price inflation could prove to be more persistent, and inflation expectations could de-anchor in advanced countries, incurring further and more rapid tightening of monetary conditions and borrowing costs, and lower growth in advanced economies. Imported food and fuel price increases could generate second-round effects in domestic inflation that would damage aggregate demand, which would be accentuated if the currency depreciated, given extensive dollarization.

Over the medium term, the economy faces ongoing risks from a resurgence of COVID-19 or other epidemics, and the country is especially vulnerable to natural disasters arising from drought, floods, and tropical storms.

16. Financing assumptions reflect growing domestic debt issuance, while external debt remains the dominant source. The level of external borrowing is set at around 3.5-4 percent of GDP over the medium term, before declining to 2.8 percent of GDP by 2030 as the fiscal deficit narrows and domestic financing increases. For the purposes of this DSA, new external debt is expected to remain largely concessional, with an average maturity of 24 years and a nominal interest rate of less than or equal to 2 percent. Consistent with the authorities' plans, the analysis assumes that the authorities start to issue domestic debt from the second half of 2022 onward; the annual amount issued increases gradually, from 0.4 percent of GDP in 2022 to about 2 percent of GDP in 2042. Demand for domestic securities is supported by the growing insurance and pension industry.[10] Outstanding domestic PPG debt is therefore estimated to reach around 10 percent of GDP by 2042, accounting for about 25 percent of the total outstanding PPG debt.

17. Macroeconomic and fiscal assumptions are broadly reasonable, although subject to uncertainty, especially about external balances (figure 4).

- The projected growth path is higher than suggested by standard fiscal multipliers, mainly reflecting the recovery from the COVID-19 shock and growth convergence. The contribution of public capital to GDP growth in the baseline scenario is broadly in line with historical values. The primary deficit-to-GDP ratio improves by 3.5 percentage points over the next three years in the baseline projection—although this adjustment falls in the top quartile of the distribution for LICs, it is feasible, as the 2021 fiscal deficit was exceptionally large due to temporary measures taken to address the COVID-19 pandemic.

- The current account deficit is assumed to steadily shrink in the baseline projection. The services balance is assumed to recover because of growth in tourism and other exports. Crucially, the surge in gold imports seen in 2021 is assumed to be temporary. The deficit remains mostly financed in the baseline, as in previous years—as a result, reserves are expected to remain high and stable, at about 8 months of imports throughout the projection period. There is high uncertainty about the prospects for gold imports and financing of the deficit. A large component of the inflows that have financed the current account deficits has been from unidentified other short-term inflows, rather than FDI (as reflected in the large residuals identified in Table 1).[11] The large share of unidentified inflows in turn reflects measurement issues in the BoP data, which complicate the assessment of external sustainability.

COUNTRY CLASSIFICATION AND DETERMINATION OF SCENARIO STRESS TESTS

18. Cambodia's debt-carrying capacity is classified as medium, same as that in the previous DSA. Cambodia's composite indicator (CI)[12] score based on the 2022 April WEO and 2020

[10] Should demand for domestic issuance be less than expected, the government could choose to further draw down domestic deposits it holds at the central bank.

[11] Table 1 shows that external debt increased by only 1.5 percentage points of GDP between 2020 and 2021, despite a non-interest current account deficit of 47.1 percent of GDP. Only 13.1 percentage points were financed by net FDI inflows.

[12] The revised LIC-DSF determines the debt sustainability thresholds by calculating a Composite Indicator. The CI is a function of the World Bank's Country Policy and Institutional Assessment (CPIA) score, international reserves, remittances, individual country and global economic growth. The calculation is based on 10-year averages of the variables, across 5 years of historical data and 5 years of projection.

CPIA data corresponds to a medium rating. There has not been further deterioration of debt-carrying capacity since the 2021 DSA (text tables 5 and 6).

Text Table 5. Cambodia's CI Index

Debt Carrying Capacity	Medium		
Final	Classification based on current vintage	Classification based on the previous vintage	Classification based on the two previous vintages
Medium	Medium 2.968	Medium 2.974	Medium 2.966

Text Table 6. Debt Burden Thresholds

EXTERNAL debt burden thresholds	Weak	Medium	Strong
PV of debt in % of			
Exports	140	180	240
GDP	30	40	55
Debt service in % of			
Exports	10	15	21
Revenue	14	18	23
TOTAL public debt benchmark			
PV of total public debt in percent of GDP	35	55	70

19. Stress tests include additional tailored stress tests. Cambodia is highly vulnerable to climate change and is likely to experience an increase in temperatures, as well as longer and more intense droughts and flooding. Hence, in addition to the six standardized stress tests, the analysis includes a natural disaster scenario, calibrated assuming a significant mitigation cost of 10 percent of GDP (around US$ 2.6 billion) and a fall in GDP growth and exports using interaction coefficients of 1.5 and 3.5, respectively. The contingent liability stress test is based on the quantification of potential risks stemming from PPPs (5.8 percent of GDP) and financial markets (10 percent of GDP).

EXTERNAL AND PUBLIC DEBT SUSTAINABILITY

20. The external debt indicators show that Cambodia's risk of debt distress remains low. External debt is projected to increase marginally by 2025, from 36 percent of GDP in 2022, falling to 33 percent by 2032 and 30 percent by 2042 (table 1). In present value terms, the external debt-to-GDP ratio also falls, from 24 percent to 21 percent over the same timeframe (table 1). The large share of concessional loans means the debt service-to-exports and debt service-to-revenue ratios remain far below their indicative benchmarks throughout the forecast horizon.

21. Stress tests suggests that Cambodia's external debt is vulnerable to shocks to exports. Compared to shocks to real growth, the fiscal balance, exchange rate depreciation, and external flows, the impact of an exports shock is the most severe—the present value of the external debt-to-

GDP ratio[13] increases sharply, from 24 percent of GDP in 2022 to just over the 40 percent threshold of GDP[14], and gradually falls back to about 35 percent over the medium term (figure 1).[15]

22. Public debt broadly follows external debt. Under the baseline, the total PPG debt level increases from 36 percent of GDP in 2021 to 41 percent of GDP in 2032, with an increased domestic financing mix. The present value of the total debt-to-GDP ratio is estimated to reach 30 percent in 2032, but remains well below the 55 percent benchmark. The debt service-to-revenue ratio is estimated to pick up briefly over the long term, along with a rising share of domestic debt[16] (figure 2). The stress tests indicate that PPG debt is vulnerable to shocks to growth: under the growth shock scenario, the present value of the total debt-to-GDP ratio rises to 53 percent by 2032, but does not breach the indicative threshold of 55 percent. The contingent liability stress test is the most extreme shock for the debt service-to-revenue ratio, which results in a noticeable spike in 2025 (figure 2), as the stress from the financial market (10 percent of GDP) results in temporary borrowing needs, increasing debt servicing.

RISK RATING AND VULNERABILITIES

23. Cambodia overall remains at low risk of both external and overall debt distress. Public debt is projected to rise by around 4 percentage points during the next decade. The present value of the external debt-to-GDP ratio breaches its threshold in the exports stress test, which would imply a moderate risk rating. However, the breaches are small, short-lived (only four periods, the last barely) and driven by the exceptional volatility of exports through the COVID-19 pandemic that has increased the sample volatility for the standardized shock. Moreover, other debt burden indicators are projected to remain well below their thresholds under the baseline and the shock scenarios. Against the expectation of a steady and solid recovery, coupled with the small and temporary nature of the breaches, judgment has therefore been applied that the external risk of debt distress remains low. However, the analysis shows that debt sustainability remains vulnerable to shocks in exports and growth.

24. Potential vulnerabilities to growth and external shocks highlight the importance of maintaining fiscal discipline and public debt management while promoting long-term

[13] The baseline scenario's results for this ratio deviate from the historical scenario because the baseline scenario treats the large current account deficit in 2021 as temporary, albeit with some persistence.

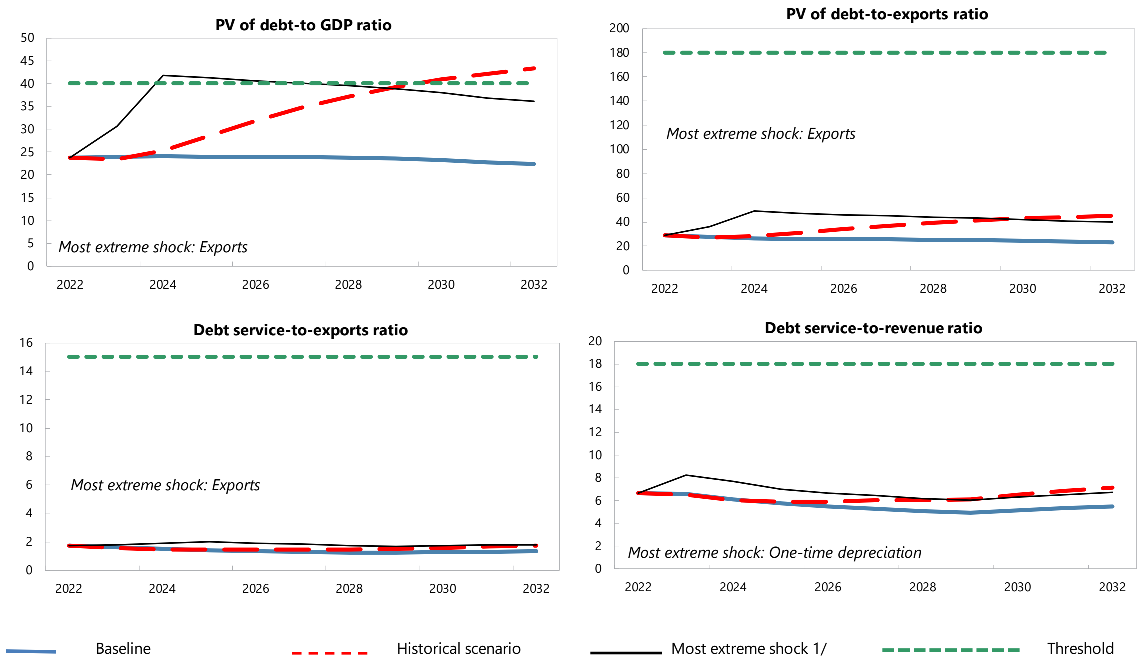
[14] The breaches are 1.81 percentage points in 2024, 1.21 in 2025, 0.63 in 2026, and 0.08 in 2027.

[15] This mechanical breach of the threshold is driven by transitory factors stemming from the COVID-19 crisis: Cambodia's exports fell by over 8 percent in 2020, substantially due to travel restrictions, compared with growth of over 15 percent y/y on average from 2011 to 2019. As a result, the standard deviation of exports used to scale the standardized shock increases significantly. Tourism remained moribund in 2021, but has bounced back with the relaxation of travel restrictions in 2022. On this basis, the large shocks to exports during 2020 and 2021 are viewed as exceptional and temporary.

[16] The stress test financing parameters have been customized to reflect domestic public debt issuing conditions (footnote 6) and the current tighter financing conditions than the DSA default.

growth. In light of heightened global risks, targeted and managed fiscal measures are important to safeguard near-term recovery. This reinforces the need to preserve macroeconomic stability, diversify the economy and exports to increase resilience to external shocks, and improve spending efficiency and the successful implementation of the revenue mobilization strategy. Further efforts to implement sound public investment management and PPP frameworks and strengthen analysis of PPP risks are needed. Finally, the authorities should focus on closing data gaps, in particular regarding data on external private debt and the PPP stock.

Figure 1. Cambodia: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2022–2032



Customization of Default Settings 2/	Size	Interactions
Tailored Stress		
Combined CL	Yes	
Natural disaster	No	No
Commodity price	n.a.	n.a.
Market financing	No	No

Note: "Yes" indicates any change to the size or interactions of the default settings for the stress tests. "n.a." indicates that the stress test does not apply.

Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG MLT debt	100%	
Terms of marginal debt		
Avg. nominal interest rate on new borrowing in USD	1.2%	1.2%
USD Discount rate	5.0%	5.0%
Avg. maturity (incl. grace period)	26	26
Avg. grace period	9	9

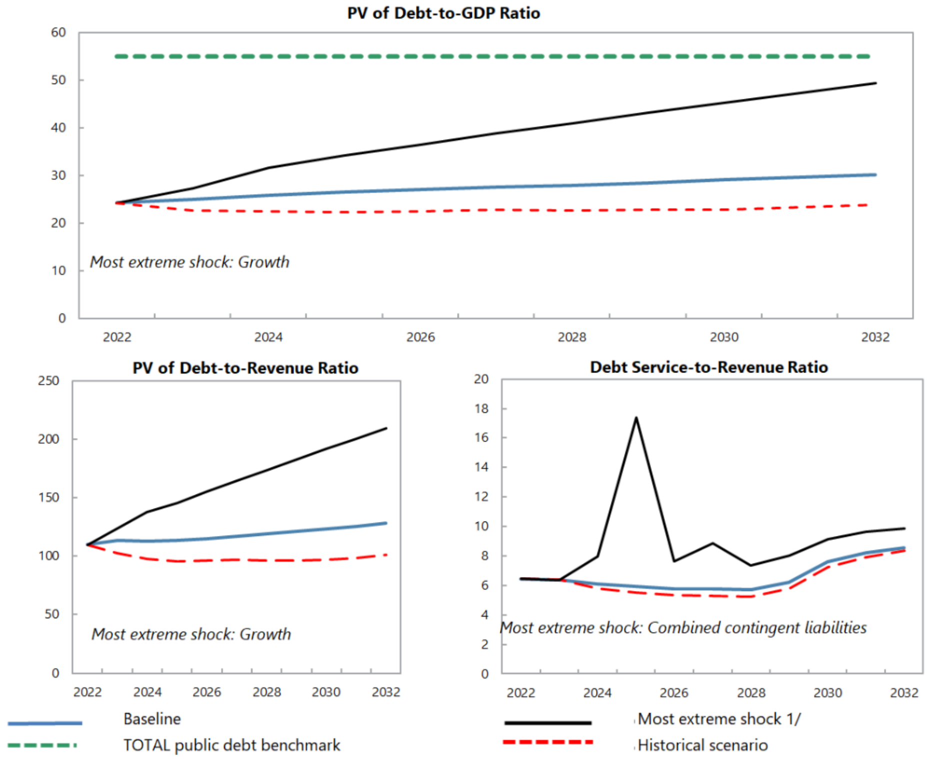
* Note: All the additional financing needs generated by the shocks under the stress tests are assumed to be covered by PPG external MLT debt in the external DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2032. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

2/ The magnitude of shocks used for the commodity price shock stress test are based on the commodity prices outlook prepared by the IMF research department.

Figure 2. Cambodia: Indicators of Public Debt Under Alternative Scenarios, 2022-2032



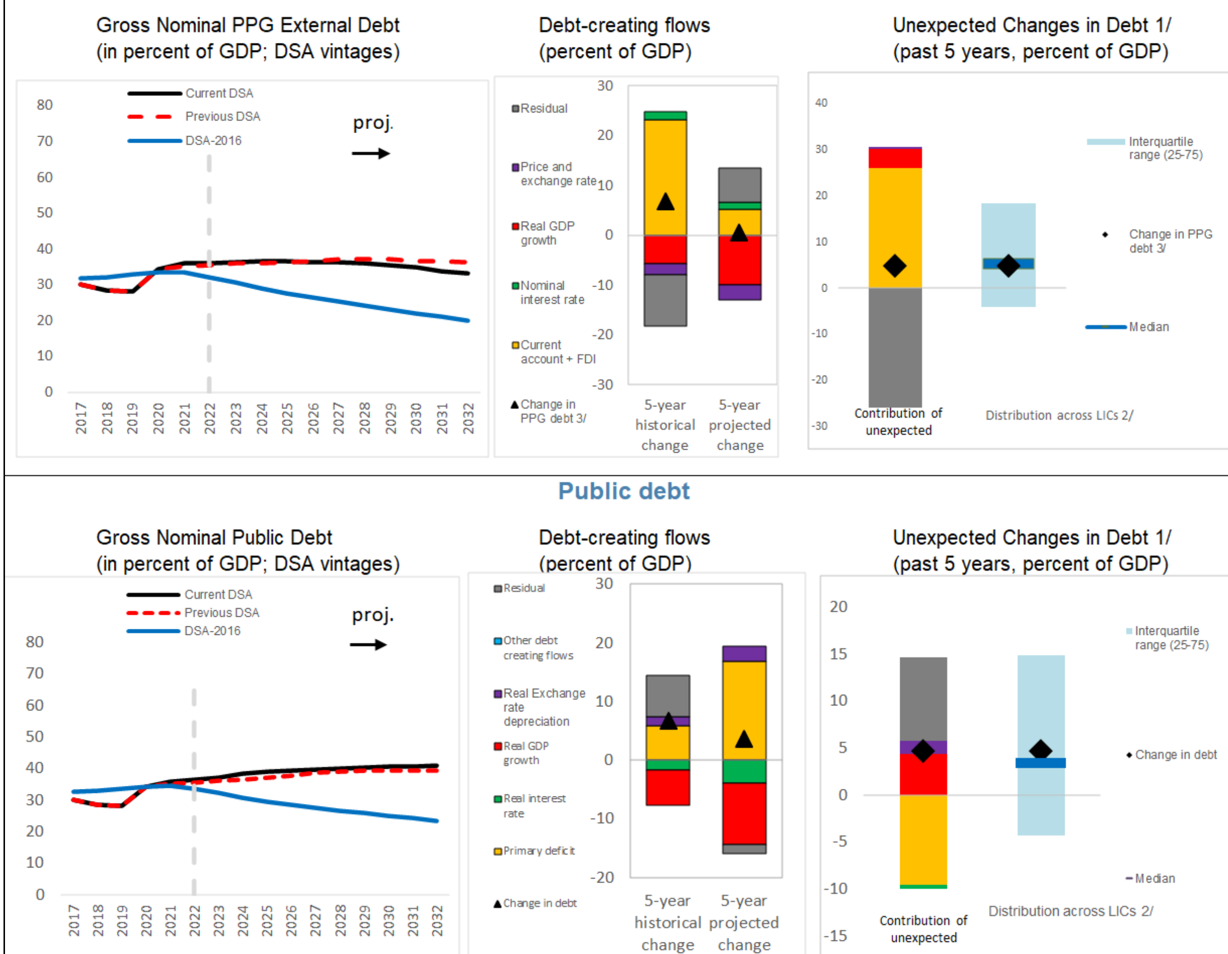
Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG medium and long-term	76%	83%
Domestic medium and long-term	24%	17%
Domestic short-term	0%	0%
Terms of marginal debt		
External MLT debt		
Avg. nominal interest rate on new borrowing in USD	1.2%	2.7%
Avg. maturity (incl. grace period)	26	20
Avg. grace period	9	9
Domestic MLT debt		
Avg. real interest rate on new borrowing	2.2%	2.0%
Avg. maturity (incl. grace period)	7	3
Avg. grace period	6	1
Domestic short-term debt		
Avg. real interest rate	-3.7%	3.0%

* Note: The public DSA allows for domestic financing to cover the additional financing needs generated by the shocks under the stress tests in the public DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2032. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

Figure 3. Cambodia: Drivers of Debt Dynamics - Baseline Scenario



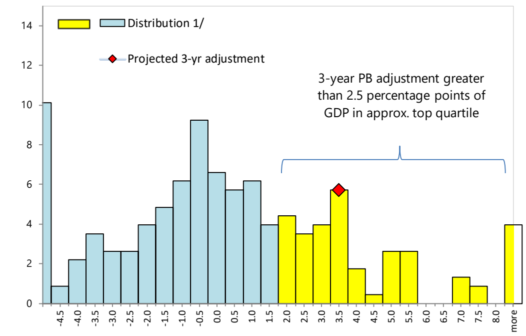
1/ Difference between anticipated and actual contributions on debt ratios.

2/ Distribution across LICs for which LIC DSAs were produced.

3/ Given the relatively low private external debt for average low-income countries, a ppt change in PPG external debt should be largely explained by the drivers of the external debt dynamics equation.

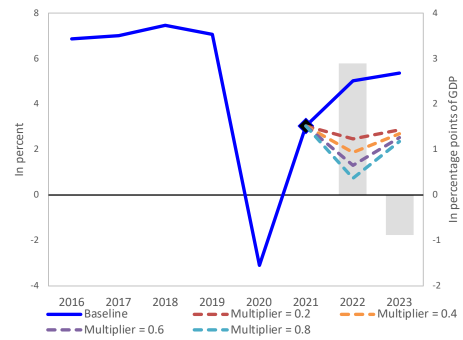
Figure 4. Cambodia: Realism tools

3-Year Adjustment in Primary Balance
(Percentage points of GDP)



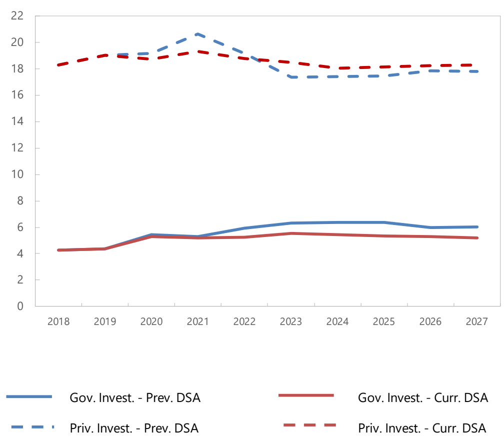
1/ Data cover Fund-supported programs for LICs (excluding emergency financing) approved since 1990. The size of 3-year adjustment from program inception is found on the horizontal axis; the percent of sample is found on the vertical axis.

Fiscal Adjustment and Possible Growth Paths 1/



1/ Bars refer to annual projected fiscal adjustment (right-hand side scale) and lines show possible real GDP growth paths under different fiscal multipliers (left-hand side scale).

Public and Private Investment Rates
(percent of GDP)



Contribution to Real GDP growth
(percent, 5-year average)

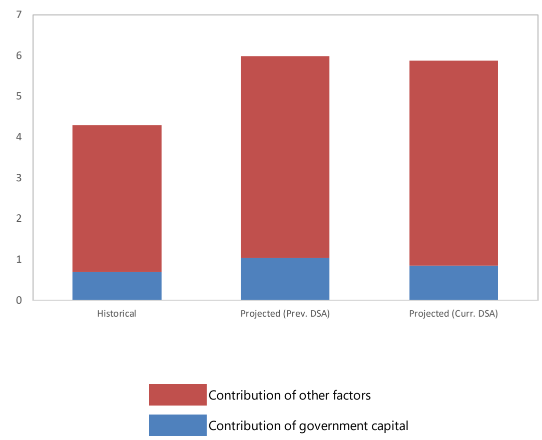
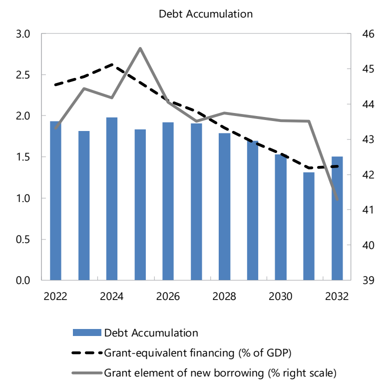


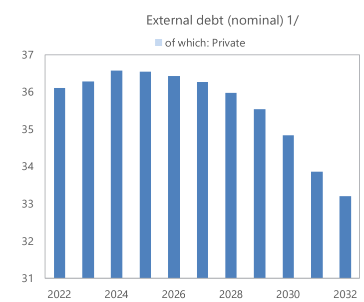
Table 1. Cambodia: External Debt Sustainability Framework, Baseline Scenario, 2019-2042

(In percent of GDP, unless otherwise indicated)

	Actual			Projections								Average 8/	
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2032	2042	Historical	Projections
External debt (nominal) 1/	**28.2**	**34.4**	**35.9**	**36.1**	**36.3**	**36.6**	**36.5**	**36.4**	**36.3**	**33.2**	**30.1**	**31.2**	**35.6**
of which: public and publicly guaranteed (PPG)	**28.2**	**34.4**	**35.9**	**36.1**	**36.3**	**36.6**	**36.5**	**36.4**	**36.3**	**33.2**	**30.1**	**31.2**	**35.6**
Change in external debt	-0.2	6.2	1.5	0.2	0.2	0.3	0.0	-0.1	-0.2	-0.7	-0.5		
Identified net debt-creating flows	**-1.1**	**-4.1**	**33.3**	**15.5**	**-0.3**	**-4.4**	**-7.1**	**-7.1**	**-6.9**	**-4.8**	**-1.9**	**-1.3**	**-3.5**
Non-interest current account deficit	**14.7**	**8.1**	**47.1**	**29.7**	**13.8**	**9.6**	**6.6**	**6.3**	**6.2**	**6.6**	**6.6**	**13.0**	**9.5**
Deficit in balance of goods and services	16.4	10.8	47.8	30.4	14.2	10.1	7.1	6.7	6.7	7.3	8.2	**16.3**	**10.0**
Exports	77.8	78.5	75.7	82.4	87.2	90.4	92.6	93.6	94.0	95.8	95.6		
Imports	94.2	89.3	123.4	112.9	101.5	100.4	99.8	100.3	100.7	103.1	103.9		
Net current transfers (negative = inflow)	-7.2	-6.4	-5.7	-5.5	-5.1	-5.0	-4.8	-4.6	-4.6	-4.0	-3.2	**-8.1**	**-4.6**
of which: official	-2.0	-1.7	-2.1	-2.0	-2.0	-1.9	-1.9	-1.8	-1.8	-1.6	-1.5		
Other current account flows (negative = net inflow)	5.4	3.7	5.0	4.8	4.6	4.5	4.3	4.2	4.1	3.3	1.5	**4.8**	**4.0**
Net FDI (negative = inflow)	**-13.5**	**-14.0**	**-13.1**	**-12.8**	**-12.5**	**-12.2**	**-11.9**	**-11.5**	**-11.2**	**-9.7**	**-6.9**	**-12.5**	**-11.2**
Endogenous debt dynamics 2/	**-2.3**	**1.8**	**-0.7**	**-1.4**	**-1.5**	**-1.8**	**-1.9**	**-1.9**	**-1.9**	**-1.7**	**-1.6**		
Contribution from nominal interest rate	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.4	0.4		
Contribution from real GDP growth	-1.8	0.9	-1.0	-1.7	-1.8	-2.1	-2.2	-2.2	-2.2	-2.0	-2.0		
Contribution from price and exchange rate changes	-0.8	0.5	-0.1	...	...	...	...	...	...	...	...		
Residual 3/	**0.9**	**10.3**	**-31.8**	**-15.3**	**0.4**	**4.7**	**7.0**	**7.0**	**6.7**	**4.1**	**1.3**	**1.9**	**3.2**
of which: exceptional financing	0.0	-0.1	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Sustainability indicators													
PV of PPG external debt-to-GDP ratio	**...**	**...**	**23.7**	**23.8**	**23.9**	**24.1**	**24.0**	**24.0**	**23.9**	**22.3**	**20.9**		
PV of PPG external debt-to-exports ratio	**...**	**...**	**31.4**	**28.9**	**27.4**	**26.6**	**25.9**	**25.6**	**25.5**	**23.3**	**21.9**		
Total external debt service-to-exports ratio	**...**	**...**	**118.6**	**111.5**	**113.2**	**109.6**	**106.2**	**104.9**	**104.5**	**95.7**	**88.1**		
PPG debt service-to-exports ratio	**1.5**	**1.8**	**1.9**	**1.7**	**1.6**	**1.5**	**1.4**	**1.3**	**1.3**	**1.3**	**1.5**		
PPG debt service-to-revenue ratio	**4.6**	**6.3**	**7.2**	**6.7**	**6.6**	**6.1**	**5.8**	**5.5**	**5.3**	**5.5**	**6.0**		
Gross external financing need (Million of U.S. dollars)	622.5	-1155.6	9436.5	5259.6	820.5	-416.3	-1397.1	-1550.8	-1584.0	-1109.6	1571.9		
Key macroeconomic assumptions													
Real GDP growth (in percent)	7.1	-3.1	3.0	5.0	5.4	6.1	6.4	6.5	6.6	6.6	7.1	**5.7**	**6.2**
GDP deflator in US dollar terms (change in percent)	2.9	-1.8	0.2	2.6	1.8	1.3	1.5	1.6	1.5	1.7	1.7	**1.8**	**1.7**
Effective interest rate (percent) 4/	1.3	1.1	1.0	0.8	0.8	0.9	0.9	1.0	1.0	1.2	1.6	**1.2**	**1.0**
Growth of exports of G&S (US dollar terms, in percent)	14.4	-4.1	-0.5	17.4	13.5	11.4	10.6	9.3	8.6	8.6	8.6	**10.2**	**10.3**
Growth of imports of G&S (US dollar terms, in percent)	16.7	-9.9	42.7	-1.5	-3.6	6.5	7.2	8.7	8.6	8.7	8.7	**13.8**	**6.3**
Grant element of new public sector borrowing (in percent)	...	...	...	43.3	44.4	44.2	45.6	44.1	43.5	41.3	35.6	**...**	**43.7**
Government revenues (excluding grants, in percent of GDP)	24.8	22.0	20.0	21.4	21.1	22.0	22.6	22.8	22.9	23.3	23.7	**19.0**	**22.6**
Aid flows (in Million of US dollars) 5/	544.1	497.4	416.4	719.2	868.5	991.1	1073.2	987.7	989.8	866.5	774.6		
Grant-equivalent financing (in percent of GDP) 6/	...	...	...	2.4	2.5	2.6	2.4	2.2	2.1	1.4	1.1	**...**	**2.0**
Grant-equivalent financing (in percent of external financing) 6/	...	...	...	51.8	54.5	54.7	54.9	52.3	51.5	45.4	36.2	**...**	**51.3**
Nominal GDP (Million of US dollars)	27,087	25,771	26,601	28,647	30,729	33,047	35,673	38,592	41,736	61,743	141,194		
Nominal dollar GDP growth	10.1	-4.9	3.2	7.7	7.3	7.5	7.9	8.2	8.1	8.3	9.0	**7.7**	**8.0**
Memorandum items:													
PV of external debt 7/	...	...	23.7	23.8	23.9	24.1	24.0	24.0	23.9	22.3	20.9		
In percent of exports	...	...	31.4	28.9	27.4	26.6	25.9	25.6	25.5	23.3	21.9		
Total external debt service-to-exports ratio	1.5	1.8	1.9	1.7	1.6	1.5	1.4	1.3	1.3	1.3	1.5		
PV of PPG external debt (in Million of US dollars)			6315.1	6829.2	7349.7	7958.3	8565.1	9249.8	9984.9	13791.0	29523.3		
(PVt-PVt-1)/GDPt-1 (in percent)				1.9	1.8	2.0	1.8	1.9	1.9	1.5	1.6		
Non-interest current account deficit that stabilizes debt ratio	14.9	2.0	45.6	29.5	13.6	9.3	6.7	6.4	6.3	7.2	7.1		

Definition of external/domestic debt	Currency-based
Is there a material difference between the two criteria?	No





Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Current-year interest payments divided by previous period debt stock.

5/ Defined as grants, concessional loans, and debt relief.

6/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

7/ Assumes that PV of private sector debt is equivalent to its face value.

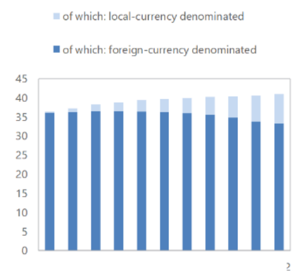
8/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

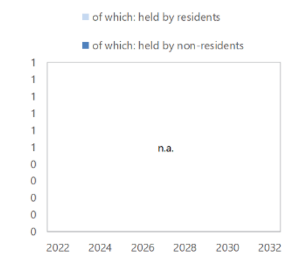
Table 2. Cambodia: Public Sector Debt Sustainability Framework, Baseline Scenario, 2019-2042
(In percent of GDP, unless otherwise indicated)

	Actual			Projections								Average 6/	
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2032	2042	Historical	Projections
Public sector debt 1/	28.2	34.4	35.9	36.3	37.2	38.2	38.9	39.3	39.7	40.9	40.4	31.2	39.3
of which: external debt	28.2	34.4	35.9	36.1	36.3	36.6	36.5	36.4	36.3	33.2	30.1	31.2	35.6
Change in public sector debt	-0.2	6.2	1.5	0.5	0.9	1.0	0.6	0.5	0.4	0.3	-0.5		
Identified debt-creating flows	-5.3	4.8	6.0	0.3	2.1	0.4	0.0	-0.4	-0.6	-0.5	-0.7	-0.4	0.0
Primary deficit	-3.3	3.0	6.7	3.8	4.7	3.1	2.7	2.4	2.3	2.3	2.1	1.4	2.9
Revenue and grants	26.8	23.9	21.6	22.1	22.0	22.9	23.4	23.5	23.5	23.6	23.8	21.4	23.2
of which: grants	2.0	1.9	1.6	0.7	0.8	0.9	0.7	0.6	0.6	0.2	0.0		
Primary (noninterest) expenditure	23.5	27.0	28.3	25.9	26.6	26.0	26.1	25.9	25.7	25.8	25.8	22.8	26.0
Automatic debt dynamics	-2.0	1.8	-0.7	-3.5	-2.6	-2.7	-2.8	-2.8	-2.8	-2.7	-2.8		
Contribution from interest rate/growth differential	-2.0	0.9	-2.0	-3.5	-2.6	-2.7	-2.8	-2.8	-2.8	-2.7	-2.8		
of which: contribution from average real interest rate	-0.1	0.0	-1.0	-1.8	-0.7	-0.5	-0.5	-0.4	-0.4	-0.3	0.0		
of which: contribution from real GDP growth	-1.9	0.9	-1.0	-1.7	-1.8	-2.2	-2.3	-2.4	-2.4	-2.5	-2.7		
Contribution from real exchange rate depreciation	0.0	0.9	1.3	...	...	...	...	...	...	...	...		
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	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 contingent liabilities (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		
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 debt creating or reducing flow (please specify)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Residual	5.1	1.4	-4.4	0.2	-1.2	0.6	0.7	0.9	1.0	0.8	0.2	1.0	0.4
Sustainability indicators													
PV of public debt-to-GDP ratio 2/	...	...	23.9	24.2	25.0	25.9	26.5	27.0	27.5	30.2	31.4		
PV of public debt-to-revenue and grants ratio	...	...	110.6	109.7	113.8	113.1	113.3	115.2	117.3	128.1	132.0		
PV of public debt-to-revenue ratio	...	...	119.3	113.3	118.2	117.7	117.0	118.3	120.2	129.3	132.2		
Debt service-to-revenue and grants ratio 3/	4.3	5.8	6.7	6.4	6.4	6.1	5.9	5.8	5.7	8.5	12.0		
Debt service-to-revenue ratio 3/	4.6	6.3	7.2	6.7	6.6	6.3	6.1	5.9	5.9	8.6	12.0		
Gross financing need 4/	-2.2	4.4	8.1	5.2	6.1	4.5	4.1	3.8	3.6	4.3	4.9		
in billions of U.S. dollars	-584.1	1143.4	2166.1	1499.6	1871.2	1484.6	1468.2	1469.5	1511.3	2657.0	6961.9		
Key macroeconomic and fiscal assumptions													
Real GDP growth (in percent)	7.1	-3.1	3.0	5.0	5.4	6.1	6.4	6.5	6.6	6.6	7.1	5.7	6.2
Average nominal interest rate on external debt (in percent)	1.3	1.1	1.0	0.8	0.8	0.9	0.9	1.0	1.0	1.2	1.6	1.1	1.0
Average real interest rate on domestic debt (in percent)	-1.9	1.8	-0.3	-2.8	2.0	2.5	2.4	2.3	2.4	2.1	2.1	-0.9	1.8
Real exchange rate depreciation (in percent, + indicates depreciation)	-0.1	3.0	4.0	...	...	...	...	...	...	...	...	0.2	...
Inflation rate (GDP deflator, in percent)	3.2	-0.7	1.3	3.7	2.9	2.4	2.6	2.7	2.6	2.8	2.9	2.0	2.8
Growth of real primary spending (deflated by GDP deflator, in percent)	10.7	11.3	8.0	-3.9	8.5	3.5	6.8	5.8	5.9	6.6	7.1	9.3	5.4
Primary deficit that stabilizes the debt-to-GDP ratio 5/	-3.1	-3.1	5.2	3.3	3.8	2.1	2.1	2.0	1.9	1.9	2.6	-0.3	2.4
PV of contingent liabilities (not included in public sector debt)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		

Definition of external/domestic debt	**Currency-based**
Is there a material difference between the two criteria?	**No**

Public sector debt 1/





Sources: Country authorities; and staff estimates and projections.
1/ Coverage of debt: The central government, central bank, government-guaranteed debt, non-guaranteed SOE debt . Definition of external debt is Currency-based.
2/ The underlying PV of external debt-to-GDP ratio under the public DSA differs from the external DSA with the size of differences depending on exchange rates projections.
3/ Debt service is defined as the sum of interest and amortization of medium and long-term, and short-term debt.
4/ 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 and other debt creating/reducing flows.
5/ Defined as a primary deficit minus a change in the public debt-to-GDP ratio ((-): a primary surplus), which would stabilizes the debt ratio only in the year in question.
6/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

Table 3. Cambodia: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2022–2032 (in percent)

	Projections 1/										
	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
PV of debt-to GDP ratio											
Baseline	24	24	24	24	24	24	24	24	23	23	22
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2032 2/	24	23	25	29	32	35	37	39	**41**	**42**	**43**
B. Bound Tests											
B1. Real GDP growth	24	25	27	27	27	27	26	26	26	25	25
B2. Primary balance	24	26	30	29	29	29	29	29	28	27	27
B3. Exports	24	31	**42**	**41**	**41**	**40**	40	39	38	37	36
B4. Other flows 3/	24	26	27	27	27	27	27	26	26	25	25
B5. Depreciation	24	30	27	27	27	27	27	27	27	26	26
B6. Combination of B1-B5	24	30	31	31	31	31	30	30	30	29	28
C. Tailored Tests											
C1. Combined contingent liabilities	24	34	34	35	34	34	34	33	33	32	31
C2. Natural disaster	24	31	31	32	32	32	32	32	31	31	30
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	24	24	24	24	24	24	24	24	23	23	22
Threshold	40	40	40	40	40	40	40	40	40	40	40
PV of debt-to-exports ratio											
Baseline	29	27	27	26	26	25	25	25	24	24	23
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2032 2/	29	27	28	31	34	37	39	41	43	44	45
B. Bound Tests											
B1. Real GDP growth	29	27	27	26	26	25	25	25	24	24	23
B2. Primary balance	29	29	33	32	31	31	31	30	29	29	28
B3. Exports	29	36	49	47	46	45	44	43	42	41	40
B4. Other flows 3/	29	29	30	29	29	29	28	28	27	26	26
B5. Depreciation	29	27	24	23	23	23	23	23	22	22	21
B6. Combination of B1-B5	29	35	32	34	34	33	33	32	31	31	30
C. Tailored Tests											
C1. Combined contingent liabilities	29	39	37	38	37	36	36	35	34	33	32
C2. Natural disaster	29	36	35	35	35	34	34	34	33	32	32
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	29	27	27	26	26	25	25	25	24	24	23
Threshold	180	180	180	180	180	180	180	180	180	180	180
Debt service-to-exports ratio											
Baseline	2	2	1	1	1	1	1	1	1	1	1
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2032 2/	2	2	1	1	1	1	1	1	2	2	2
B. Bound Tests											
B1. Real GDP growth	2	2	1	1	1	1	1	1	1	1	1
B2. Primary balance	2	2	2	2	2	2	2	1	1	2	2
B3. Exports	2	2	2	2	2	2	2	2	2	2	2
B4. Other flows 3/	2	2	2	1	1	1	1	1	1	1	1
B5. Depreciation	2	2	1	1	1	1	1	1	1	1	1
B6. Combination of B1-B5	2	2	2	2	2	2	1	1	1	2	2
C. Tailored Tests											
C1. Combined contingent liabilities	2	2	2	2	2	2	2	2	2	2	2
C2. Natural disaster	2	2	2	2	2	2	2	1	2	2	2
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	2	2	1	1	1	1	1	1	1	1	1
Threshold	15	15	15	15	15	15	15	15	15	15	15
Debt service-to-revenue ratio											
Baseline	7	7	6	6	5	5	5	5	5	5	5
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2032 2/	7	7	6	6	6	6	6	6	7	7	7
B. Bound Tests											
B1. Real GDP growth	7	7	7	6	6	6	6	6	6	6	6
B2. Primary balance	7	7	7	7	7	6	6	6	6	6	6
B3. Exports	7	7	7	8	7	7	7	7	7	7	7
B4. Other flows 3/	7	7	6	6	6	6	5	5	5	6	6
B5. Depreciation	7	8	8	7	7	6	6	6	6	7	7
B6. Combination of B1-B5	7	7	7	7	6	6	6	6	6	6	6
C. Tailored Tests											
C1. Combined contingent liabilities	7	7	8	7	7	7	6	6	6	7	7
C2. Natural disaster	7	7	7	7	7	6	6	6	6	6	6
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	7	7	6	6	5	5	5	5	5	5	5
Threshold	18	18	18	18	18	18	18	18	18	18	18

Sources: Country authorities; and staff estimates and projections.
1/ A bold value indicates a breach of the threshold.
2/ Variables include real GDP growth, GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
3/ Includes official and private transfers and FDI.

Table 4. Cambodia: Sensitivity Analysis for Key Indicators of Public Debt, 2022–2032

	Projections 1/										
	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
	PV of Debt-to-GDP Ratio										
Baseline	24	25	26	26	27	28	28	28	29	30	30
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2032 2/	24	23	22	22	23	23	23	23	23	23	24
B. Bound Tests											
B1. Real GDP growth	24	27	32	34	36	39	41	43	45	47	49
B2. Primary balance	24	27	32	33	33	33	33	34	34	34	35
B3. Exports	24	30	39	39	39	39	39	39	39	39	40
B4. Other flows 3/	24	27	29	30	30	30	31	31	32	32	33
B5. Depreciation	24	30	29	27	26	24	23	22	21	20	19
B6. Combination of B1-B5	24	25	28	29	29	30	30	30	31	31	32
C. Tailored Tests											
C1. Combined contingent liabilities	24	38	38	38	38	38	38	38	38	39	39
C2. Natural disaster	24	34	34	35	35	36	36	37	37	38	38
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	24	25	26	26	27	28	28	28	29	30	30
TOTAL public debt benchmark	55	55	55	55	55	55	55	55	55	55	55
	PV of Debt-to-Revenue Ratio										
Baseline	110	114	113	113	115	117	119	121	123	125	128
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2032 2/	110	103	98	96	96	97	96	97	97	99	101
B. Bound Tests											
B1. Real GDP growth	110	124	137	145	155	165	174	183	192	201	209
B2. Primary balance	110	124	141	139	140	141	141	143	144	145	147
B3. Exports	110	135	169	167	166	166	166	167	167	168	169
B4. Other flows 3/	110	121	127	127	128	130	131	133	134	136	138
B5. Depreciation	110	137	126	116	110	104	99	94	90	86	83
B6. Combination of B1-B5	110	116	123	123	124	126	127	129	130	132	134
C. Tailored Tests											
C1. Combined contingent liabilities	110	171	167	162	162	162	162	162	163	164	165
C2. Natural disaster	110	153	151	149	150	152	154	156	158	160	163
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	110	114	113	113	115	117	119	121	123	125	128
	Debt Service-to-Revenue Ratio										
Baseline	6	6	6	6	6	6	6	6	8	8	9
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2022-2032 2/	6	6	6	6	5	5	5	6	7	8	8
B. Bound Tests											
B1. Real GDP growth	6	7	7	8	9	9	9	10	12	13	13
B2. Primary balance	6	6	7	9	9	7	7	8	9	9	10
B3. Exports	6	6	6	7	7	7	7	7	8	9	9
B4. Other flows 3/	6	6	6	6	6	6	6	6	8	8	9
B5. Depreciation	6	7	8	7	6	7	6	6	8	8	8
B6. Combination of B1-B5	6	6	7	7	8	7	7	7	9	9	9
C. Tailored Tests											
C1. Combined contingent liabilities	6	6	8	17	8	9	7	8	9	10	10
C2. Natural disaster	6	6	7	14	7	8	7	8	9	10	10
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	6	6	6	6	6	6	6	6	8	8	9

Sources: Country authorities; and staff estimates and projections.
1/ A bold value indicates a breach of the benchmark.
2/ Variables include real GDP growth, GDP deflator and primary deficit in percent of GDP.
3/ Includes official and private transfers and FDI.

INTERNATIONAL MONETARY FUND

CAMBODIA

November 12, 2022

STAFF REPORT FOR THE 2022 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By

Asia and Pacific Department
(In consultation with other departments)

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FUND RELATIONS

(As of September 30, 2022)

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	100.00
Fund holdings of currency (Holdings Rate)	153.13	87.50
Reserve Tranche Position	21.88	12.50

SDR Department:	**SDR Million**	**Percent Allocation**
Net cumulative allocation	251.65	100.00
Holdings	256.69	102.00

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				
	2022	2023	2024	2025	2026
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

The currency of Cambodia is the Cambodian riel. Cambodia's de facto exchange rate arrangement is classified as *stabilized*. The *de jure* exchange rate arrangement is a *managed float*. The exchange rate regime comprises two rates: the official rate and the market rate. 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 multiple currency practices and 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 previous Article IV consultation discussions were held during September 13–27, 2021. The Executive Board concluded the Article IV consultation (IMF Country Report 21/260) on November 19, 2021.

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.

Resident Representative

Mr. Yasuhisa Ojima has been the IMF Resident Representative for Cambodia since September 2019.

RELATIONS WITH OTHER INTERNATIONAL FINANCIAL INSTITUTIONS

World Bank: http://www.worldbank.org/en/country/cambodia

Asian Development Bank: https://www.adb.org/countries/cambodia/main

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
Public Debt Bulletin

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

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

National Summary Data Page (https://www.nbc.org.kh/english/economic_research/NSDP.html)

STATISTICAL ISSUES

(September 2022)

I. Assessment of Data Adequacy for Surveillance
General. Data provision is broadly adequate for surveillance. Extensive technical assistance (TA) has been provided by the Fund, United Nations Development Program, 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 and statistics, several shortcomings in macroeconomic data still hamper timely and comprehensive analysis.
National accounts. The reliability of the national accounts is affected by an outdated base year (2000). The Cambodian economy has rapidly evolved, as has its informal sector which is using technology to increase value-added (such as in the transportation sector). Sectors such as agriculture and construction lack adequate volume measures, and more broadly the absence of relevant price deflators underscore the need for upgrading statistical techniques and data sources used for compiling GDP by output. For GDP by expenditure, data source constraints impact in particular, the measurement of household final consumption expenditure, and gross capital formation. The NIS is currently revising the sources and methods for compiling national accounts including the GDP rebasing with new base year of 2014, assisted by SIDA and UNESCAP; and plans to disseminate the rebased GDP in 2023. Technical Review by the IMF's statistics department has confirmed that the rebasing exercise has followed internationally accepted practices. The availability turnover and financial statements data, high frequency indicators such as quarterly GDP and a production index to NIS would support more agile monitoring of economic developments.
Price statistics. With technical assistance from the Fund, the NBC officially launched a residential property price index (RPPI) in June 2022 to facilitate the monitoring of price developments in the real estate market. The compilation of the consumer price index (CPI) suffers from outdated weights—drawn from the 2004 Cambodia Socio-Economic Survey-based household expenditure data—and insufficient geographic coverage, as well as delays in data dissemination. The NIS is planning to update the CPI series, using 2014 household expenditures to update the basket and weights. A producer price index (PPI) is under development as part of broader efforts to strengthen price measures for the national accounts.
Government finance statistics (GFS). The Ministry of Economy and Finance (MEF) is making steady progress on improving government finance (GFS) and public sector debt statistics (PSDS). As an outcome of Fund TA, GFS are compiled following the *Government Finance Statistics Manual 2014 (GFSM 2014)*. The MEF disseminates monthly GFS for budgetary central government (BCG) and quarterly GFS covering BCG and local governments (LGs) on its website, together with the metadata and the derivation table from the national presentation (TOFE). The MEF reported 2019 GFS for consolidated general government, including the National Social Security Fund and other extrabudgetary units (public administrative establishments) to the Fund and started reporting PSDS covering BCG debt securities and loans to the joint World Bank/IMF Database on a semi-annual basis. The MEF bridged the BCG program classification with the Classification of the Functions of Government (COFOG) and reported the BCG Environmental Protection Expenditure for 2018-2020 to the Fund's Climate Indicators Dashboard. COFOG for LGs has been work-in-progress. The availability of source data for the net acquisition of government nonfinancial assets remains limited. A

prototype financial balance sheet covering BCG has been compiled for 2015-2018. Work needs to be continued on reconciling the coverage of government deposits and other statistics for general government between the MEF, the NBC, and the National Institute of Statistics. To facilitate policy dialog, promoting the use of GFS would improve budget planning and enhance data transparency. To this end, streamlining the budget table with the GFSM2014 framework would enhance comparative analysis of actuals and projections. The MEF GFS team has started developing the Technical Compilation and Dissemination Guidelines for GFS and PSDS. The authorities are encouraged to review available source data for SOEs and conclude on the possibility of compiling GFS for the public sector.
Monetary and financial statistics (MFS). The NBC reports monthly monetary data using STA's standardized reporting forms (SRFs) for the central bank, other depository corporations (ODCs), and other financial corporations (OFCs). For OFCs, there is a need to improve information on the counterpart sector, especially for loans, and expand the institutional coverage to include insurance companies (ICs), and leasing companies. The current SRF 4SR covers non-deposit taking microfinance institutions and specialized banks. Further, there is little information to gauge the exact size of the shadow banking sector which includes institutions such as real estate developers, pawn shops and payment service providers. A recent MCM diagnostic review of the NBC's IT needs for regulatory reporting—which provides source data for MFS—has proposed a roadmap to support NBC's efforts to fully automate regulatory reporting. Future work on streamlining data collections by simplifying and harmonizing reporting requirements and templates should take full account of MFS and FSI compilation requirements. A recent remote MFS mission assisted in improving the framework for compiling the SRF for ODCs, using a new chart of accounts as source data and for expanding the coverage of the SRF for OFCs to include NDTMFIs. In addition, the NBC, the Ministry of Economy and Finance, and the Insurance Association of Cambodia have agreed on a work plan to collect data from ICs.
Financial sector surveillance/financial access. The NBC reports to the Fund 13 core and 8 additional FSIs for deposit takers, two FSIs for OFCs, one FSI for households, and two FSIs for real estate markets on a quarterly frequency and with one quarter timeliness. The NBC has used the new FSIs templates based on the (new) 2019 FSIs Compilation Guide starting with 2021Q1 data. Several series and indicators of the Financial Access Survey (FAS), including the two indicators—commercial bank branches per 100,000 adults and ATMs per 100,000 adults—used to monitor Target 8.10.1 of the SDGs are disseminated.
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 and International Investment Position Manual, sixth edition (BPM6). There are gaps in coverage, resulting from source data limitations. Discrepancies in trade data, although somewhat reduced, are yet to be resolved. Persistent mirror discrepancies with partners' trade data have major potential impact on the current account balance and, hence, the most important from the surveillance point of view. There is scope for improving the data on inward direct investment (DI) — a key component of Cambodia's external transactions and positions, as estimation draws heavily on DI approvals. The work continues to address shortages in recording other financial accounts components, most importantly trade credits, other debt liabilities, and debt reorganization transactions. External debt statistics do not cover borrowing by resident nonfinancial corporations. Technical assistance is ongoing under the Project on Improvement of External Sector Statistics which is funded by the government of Japan and executed through the IMF Capacity Development Office in Thailand (CDOT). In July 2020, TA from IMF CDOT assisted in revising compilation practices for the balance of payments trade credit components, refining the model on remittances, advancing work on trade data validation, and enhancing consistency with other macroeconomic data sets.

II. Data Standards and Quality	
Cambodia participates in the IMF's General Data Dissemination System (e-GDDS). Its National Summary Data Page (NSDP) was launched on May 30, 2018. **(https://www.nbc.org.kh/english/economic_research/NSDP.html)**	No data ROSC are available.

Cambodia: Table of Common Indicators Required for Surveillance

(As of October 1, 2022)

	Date of Latest Observation	Date Received	Frequency of Data[1]	Frequency of Reporting[1]	Frequency of Publication[1]
Exchange Rates	9/29/2022	9/30/2022	D	D	W
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[2]	7/2022	9/2022	M	M, 2 month lag	M
Reserve/Base Money	7/2022	9/2022	M	M, 2 month lag	M
Broad Money	7/2022	9/2022	M	M, 2 month lag	M
Central Bank Balance Sheet	7/2022	9/2022	M	M, 2 month lag	M
Consolidated Balance Sheet of the Banking System	7/2022	9/2022	M	M, 2 month lag	M
Interest Rates[3] (Loan and Deposit rates)	7/2022	9/2022	M	M, 2 month lag	M
Consumer Price Index	8/2022	9/2022	M	M, 1-2 month lag	M
Revenue, Expenditure, Balance and Composition of Financing[4]—General	7/2022	9/2022	M	M, 1-2 month lag	M
Revenue, Expenditure, Balance and Composition of Financing—Central	7/2022	9/2022	M	M, 1-2 month lag	M
Stocks of Central Government and Central Government-Guaranteed Debt[5]	6/2022	9/2022	S	S, 3 month lag	S
External Current Account Balance	Q2/2022	9/2022	Q	Q, 3 month lag	Q
Exports and Imports of Goods and Services	Q2/2022	9/2022	Q	Q, 3 month lag	Q
GDP/GNP	2021	9/2021	A	A, 6 month lag	A
Gross External Debt	Q2/2022	9/2022	Q	Q, 3 month lag	Q
International Investment Position	Q2/2022	9/2022	Q	Q, 3 month lag	Q

[1] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Semi-annual (S), 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] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

[5] Including currency and maturity composition.

Statement by Rosemary Lim, Executive Director for Cambodia, Raja Anwar, Alternate Executive Director, and Ms. Sukjai Wongwaisiriwat, Senior Advisor to Executive Director
November 23, 2022

1. INTRODUCTION

1.1 On behalf of the Cambodian authorities, we would like to thank the IMF mission team for the constructive policy discussions during the 2022 Article IV consultation. The authorities are encouraged by staff's positive assessment on Cambodia's macroeconomic developments, and broadly share staff's view on medium-term structural challenges. The authorities are in broad agreement with staff's recommendations and will carefully take them into consideration when formulating policies.

2. RECENT ECONOMIC DEVELOPMENTS AND OUTLOOK

2.1 **Cambodia's economy has experienced a relatively slow growth in 2021 due to the pandemic, but has since recovered steadily.** Rapid vaccination efforts and the reduction of COVID-19 infection rates enabled Cambodia to fully reopen to foreign tourists since November 2021. This allowed the authorities to roll back some of the support measures and gradually build up the fiscal space for future shocks.

2.2 **The authorities welcome staff's assessment that growth outlook is broadly positive, underpinned by both domestic and external stability.** Despite emerging headwinds from external shocks, from the conflict in Ukraine and slowdown in key trading partners' economies (China, Europe and the US) in the second half of 2022, the momentum of economic recovery is expected to continue with growth projections, at around 5% in 2022 and around 6% in 2023. This is supported by a solid recovery in tourism sector and a bright prospect of exports. As a result, Cambodia's external sector has improved, as primarily reflected in the narrowing of current account (CA) deficit. Tourism and FDI are expected to have larger contributions to CA in 2023. Supported by abundant labor force and stable macroeconomic environment, the authorities expect more relocations of exporting firms from other neighboring countries to Cambodia – contributing to its medium-term growth.

2.3 **Despite the recent surge in inflation, its effects have been manageable with limited risk of second-round effects and de-anchoring of inflation expectation.** Faster recovery from the pandemic allowed the government to channel its funds to mitigate the impact of rising prices on vulnerable households in the form of extended cash transfers.

3. FISCAL POLICY

3.1 **The authorities remain committed to using available fiscal space to mitigate the impacts of the global economic slowdown and the conflict in Ukraine on growth and inflation, with a view to maintaining debt sustainability.** Cambodia's fiscal position has been improving steadily on the back of the resumption of economic activities. This is driven by a broad-based recovery in tax revenue and a partial rollback of Covid-related spending. Meanwhile, measures to mitigate the impact of rising prices have been well-targeted using the government's ID Poor database to identify poor and vulnerable individuals. The Debt Sustainability Analysis (DSA) indicates that Cambodia has fiscal space to cope with further adverse shocks; nevertheless, authorities will continue to use fiscal measures in a targeted manner and embark on initiatives to improve the efficiency of targeting different types of vulnerable households.

3.2 **As part of the effort to ensure debt sustainability, the government continues to develop domestic financial markets in line with the recommendation in previous Article IV reports.** Significant progress was made in 2022 by issuing domestic government bonds for the first time in local currency. The auction was well-received by financial institutions, due primarily to close market consultations and clear communication by the Ministry of Finance. The authorities will continue to work on long-term policy framework for market development in line with staff's recommendations. Efforts to develop a comprehensive framework for bond issuance up until 2028 are already underway.

4. MONETARY AND FINANCIAL SECTOR POLICIES

4.1 **Monetary policy continued to be accommodative to support the recovery at the early stage.** However, as the recovery gathered momentum in 2022, the National Bank of Cambodia (NBC) has started to normalize its policy primarily by ending regulatory forbearance on new restructured loans in June 2022 and considering gradually raising reserve requirements to pre-pandemic levels. The share of non- performing loans (NPLs) in banks' loan portfolios has naturally risen after the end of forbearance but should gradually decline in line with improving debt servicing ability of borrowers.

4.2 **Credit growth has been robust, reflecting positive sentiments for medium-term economic prospects and sound fundamentals of Cambodia. Nevertheless, the authorities note staff's concerns on the high level of growth and will closely monitor the developments.** According to staff's assessment, Cambodia's economic growth is projected to converge to a potential rate of about 6.5 percent – higher than most countries in ASEAN. Thanks to several trade agreements and continued efforts in economic diversification, Cambodia has seen broad-based increase in investment, not only in garments and footwears but also in agro-processing, automotives, as well as electronics and electrical appliances. A recent increase in credit growth largely reflects funding given to these productive sectors. Nevertheless, the NBC will continue to ensure that banks maintain adequate capital buffers, and, amid high uncertainty, will closely monitor developments in the banking system with preemptive measures to safeguard financial stability.

4.3 **Overall financial stability remains sound, but amid high uncertainty in the global economy, authorities will carefully monitor associated risks**, including staff's concerns on the buildup of private debt and potential risks in the real estate sector. On the latter however, the authorities are of the view that the potential risks should have limited impacts on consumption as they remain concentrated in some provinces and only certain segments of the housing market.

5. STRUCTURAL POLICIES

Over the past years, the authorities have made significant progress in enhancing economic diversification and addressing weaknesses in governance framework, and have placed both issues among Cambodia's top reform priorities in the medium term.

5.1 **In promoting further diversification and productivity, new investment law has been introduced to allow for more targeted tax incentives to high-potential sectors and firms.** The current Industrial Development Policy (2015-2025) has undergone a mid-term review and has produced a roadmap to promote investment in higher value-add manufacturing sectors such as automotive, electronics and machinery. Moreover, the new investment law provides incentives for qualified investment projects in climate adaptation and mitigation. An advisory council has also been established as a channel for authorities to gain feedbacks and have regular dialogues with firms in these key sectors.

5.2 **The authorities remain committed to strengthening governance and anti- corruption frameworks, and will continue work to implement the necessary measures.** Interagency cooperation among agencies charged with the anti-corruption and AML/CFT mandates – the Anti-Corruption Unit (ACU) directly tasked with anti- corruption mandates, the National Council Against Corruption (NCAC) that oversees the operations of the ACU, the National Coordination Committee (NCC) on AML/CFT/CPF[1] and the Financial Intelligence Unit (FIU) – has improved over the past years. They have also collaborated with other ministries to, for instance, identify sectors most prone to corruption risks. With joint efforts made by interagency cooperation and coordination, Cambodia has completed all the action plan items imposed by the FATF and is expected to undergo an exit onsite visit in January 2023. In relation to the pending laws on whistleblower and transparency, the draft legislation on whistleblower protection has been submitted to the Ministry of Justice for review. The authorities have also sought further IMF technical assistance to enhance capacity in human and technological resources.

[1] Anti-Money Laundering / Countering the Financing of Terrorism / Countering the Financing of Proliferation of weapons of mass destruction