

**Cambodia: Second Review Under the Poverty Reduction and Growth Facility--Staff Report;
Staff Statement; News Brief on the Executive Board Discussion; and Statement by Authorities
of Cambodia**

In the context of the second review under the Poverty Reduction and Growth Facility, the following documents have been released and are included in this package:

- the staff report for the second review under the Poverty Reduction and Growth Facility, prepared by a staff team of the IMF, following discussions that ended on **October 28, 2000**, 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 January 3, 2001.** The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- a staff statement of January 19, 2001 updating information on recent economic developments.
- a News Brief summarizing the views of the Executive Board as expressed during its **January 19, 2001, discussion** of the staff report that completed the review.
- a statement by the authorities of Cambodia.

The document(s) listed below have been or will be separately released.

Interim Poverty Reduction Strategy Paper
Joint Staff Assessment of the Interim Poverty Reduction Strategy Paper
Letter of Intent by the authorities of the member country
Memorandum of Economic and Financial Policies by the authorities of the member country
Technical Memorandum of Understanding

The policy of publication of staff reports and other documents by the IMF allows for the deletion of market-sensitive information.

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CAMBODIA

Second Review Under the Poverty Reduction and Growth Facility

Prepared by the Asia and Pacific Department and
Policy Development and Review Department

(In consultation with the Fiscal Affairs, Legal, Monetary
and Exchange Affairs, Statistics and Treasurer's Department)

Approved by R. Anthony Elson and Mark Allen

January 3, 2001

- A staff team visited Phnom Penh during October 16–28 to conduct the second review under the PRGF arrangement. The team consisted of Messrs. Rumbaugh (head), Marciniak, Ishi (all APD), Ms. Sun (EP-APD), Mr. Adachi (PDR), and Ms. Jupp (Administrative Assistant, APD). The mission was assisted by Mr. de Zamaróczy (Resident Representative) and worked jointly with a World Bank mission on civil service reform, expenditure management, and governance issues, and with an MAE mission on bank restructuring.
- The mission met with H.E. Keat Chhon, Senior Minister and Minister of Economy and Finance, H.E. Sok An, Senior Minister in charge of the Council of Ministers; H.E. Chea Chanto, Governor of the National Bank of Cambodia; and other senior officials.
- A three-year PRGF arrangement for SDR 58.5 million (67 percent of quota) was approved by the Executive Board on October 22, 1999. The first review under the arrangement, together with the 2000 Article IV consultation, was concluded on September 15, 2000. The staff report was released under the policy for the voluntary release of Article IV consultation reports. The authorities have also agreed to have the current report published as well as the I-PRSP and Joint Staff Assessment.
- This report was prepared by the staff team under the direction of Mr. Rumbaugh.

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Executive Summary

Background: Cambodia's performance during the first year under the PRGF arrangement was generally successful. Economic growth resumed, inflation was moderate, government revenue mobilization improved, and fiscal balance was restored. All quantitative and structural performance criteria under the arrangement were observed. Structural reforms were implemented broadly as programmed, including notable progress in forestry policy and in bank restructuring.

Economic Prospects: Economic recovery was interrupted in the second half of 2000 by severe flooding. With substantial damage to crops, economic growth for 2000 is estimated at 4 percent compared to 5½ percent projected under the program. Food price increases, and the impact of high oil prices, are expected to increase inflation to 8–10 percent in the near term. Agricultural performance is expected to rebound in 2001, and with an increase in infrastructure rehabilitation, GDP growth is projected to recover to 6 percent. With the maintenance of prudent monetary and fiscal policies, inflation is projected to return to below 5 percent by the end of 2001.

Poverty Reduction Strategy: The authorities have prepared an *Interim Poverty Reduction Strategy Paper* that meets core requirements and provides a sound basis for developing a fully participatory PRSP, as well as an adequate framework for Fund and Bank concessional assistance. As indicated in the Joint Staff Assessment, the main concern for the full PRSP relates to the government's weak administrative capacity and difficulties in coordinating arrangements among different agencies and policy initiatives.

Main Policy Issues

The budget framework for 2001: The budget aims for a further improvement in revenue mobilization and expenditure management in line with PRGF objectives. Measures to broaden the tax base and improve tax and customs administration will need to be fully implemented to achieve the revenue objective. Improved spending for the social sectors will depend on the successful implementation of Priority Action Programs, and will be needed to support the authorities' poverty reduction goals.

Bank Restructuring: Substantial progress has been made in bank relicensing and in consolidating the banking system. The priority for 2001 will be to monitor closely the performance of potentially viable banks against their Memoranda of Understanding, and to instill a commercial culture into the restructured Foreign Trade Bank as part of its preparation for privatization.

Military demobilization and civil service reform: Delays experienced to date in these difficult, but vital, areas of structural reform will need to be made up to protect the program's medium-term macroeconomic and poverty reduction objectives.

I. INTRODUCTION

1. **In concluding the first review under the PRGF arrangement and the 2000 Article IV consultation, Executive Directors commended the authorities for their economic performance and emphasized that achieving sustained growth and poverty reduction will require continued strong efforts on a wide front.** Critical elements would include an increase in fiscal revenue, and a continued redirection of expenditures to priority social objectives in an environment of improved governance. Directors also stressed the need to refrain from nonconcessional borrowing, and to follow through on agreed structural measures relating to civil service reform, military demobilization, and forestry policy.
2. **In the attached letter to the Managing Director, the authorities request completion of the second PRGF review.** In the accompanying Memorandum of Economic and Financial Policies (Attachment), the authorities report on progress made under the PRGF-supported program, describe their policies for the second program year, and establish performance criteria through end-2001. The program continues the main thrust of policies established under the first-year program centering on revenue mobilization, expenditure management, bank restructuring, and forestry policy. The program has been designed to support the objectives of the authorities' Interim Poverty Reduction Strategy Paper (I-PRSP).

II. PERFORMANCE UNDER THE PROGRAM IN 2000

3. **Performance under the first year of Cambodia's PRGF-supported program was strong, with a resumption of growth, low inflation, and significant progress in major areas of structural reform.** The political situation has stabilized since the current coalition government was formed in November 1998, providing Cambodia with an improved environment to implement reforms that have restored growth momentum (Table 1 and Charts 1 and 2). Quantitative benchmarks and performance criteria, and structural performance criteria, have been observed through end-November 2000 (Tables 2-3). Delays have been experienced in some areas of structural reform because of weak implementation capacity, difficulties in reaching internal consensus, or delays in donor financing.
4. **For the first half of 2000, economic activity was buoyant.** Manufacturing activity, particularly in the garment sector, increased significantly, tourist arrivals increased by 40 percent from the previous year, and good agricultural output led to substantial declines in food prices. As a result, economic growth was projected at mid-year to reach 5½ percent for 2000 with inflation under 5 percent (on an end-of-period basis).
5. **However, in July–November 2000, Cambodia was hit by unusually severe flooding.** The flooding affected about 20 percent of the population, and the government's preliminary estimate indicates that 30 percent of rice fields were damaged, major parts of key roads and irrigation facilities were washed away, and a number of schools and hospitals were damaged. Total damage, including rehabilitation needs, was estimated by the AsDB at about US\$100 million (3 percent of GDP) (Box 1).

Box 1. Cambodia: Effects of the Flooding

Background

During the second half of 2000 Cambodia suffered the worst flooding in 70 years, directly affecting 2.2 million people (20 percent of the population) in 18 of the 24 provinces, primarily in rural areas. The flooding has taken a major human and economic toll: (i) 350 deaths and 200,000 people displaced; (ii) 350,000 ha. of cropland damaged (30 percent of the total); and (iii) extensive damage to economic infrastructure. The information below provides a preliminary assessment of the main effects of the flooding based on information available as of end-November 2000; a full assessment is expected in early 2001.

Flooding impact^{1/}

Real Sector: Real GDP growth is now projected to slow to 4 percent as against 5½ percent in the program, reflecting a flood-related loss in agricultural output. Agriculture accounts for 40 percent of GDP and about 80 percent of the rice harvest takes place during the wet season (June–October).

End-period inflation is projected to rise to about 8 percent, compared with the program target of 5 percent, largely due to higher food prices. Despite timely food aid relief, retail rice prices increased by 38 percent during July–October.

Damage to infrastructure and equipment (i.e. roads, irrigation equipment and facilities, and education and health facilities) is officially estimated at US\$105 million (3.2 percent of GDP).

Fiscal: Current expenditure for flood relief in 2000 is estimated at 0.3 percent of GDP, while rehabilitation of infrastructure will be carried out primarily through donor-financed projects beginning in 2001. Program targets for end-December 2000 have been adjusted to reflect this additional spending while avoiding domestic financing of the budget.

External sector: The external current account deficit (excluding transfers) is expected to remain broadly unchanged at 13 percent of GDP, as total flood-related imports are not large relative to overall imports.

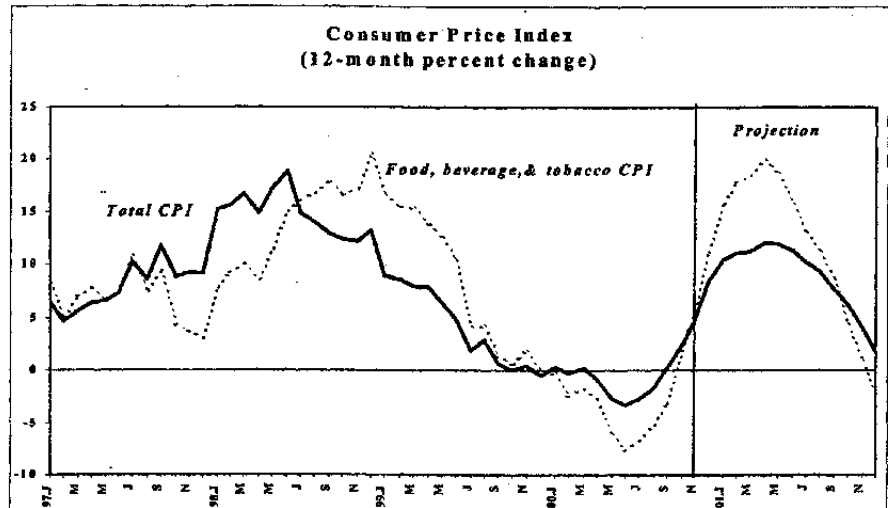
Structural reforms: The process of establishing a computerized civil service payroll was temporarily delayed, owing to the interruption of fingerprinting operations in the provinces. More generally, limited administrative capacity has also been diverted to focus on flood relief and rehabilitation.

International Response

International emergency relief—US\$10.7 million, 0.3 percent of GDP—has been provided in response to the authorities' request. Further assistance, equivalent to 3 percent of GDP, has been envisaged under concessional loans from the AsDB (US\$55 million) and the World Bank (US\$40–45 million), to assist the government in the rehabilitation of key infrastructure which will be reflected in the budget for 2001 and following years.

^{1/} Although the deviations of key macroeconomic aggregates from the program's projections are largely attributable to the flooding, the high oil prices have also been a contributing factor.

6. **The serious flooding, and to a lesser extent sustained higher oil prices, are adversely affecting economic growth and inflation.** Growth in real GDP is now estimated at 4 percent, reflecting a sharp fall in agricultural production in the final quarter of the year. Although the domestic retail prices of

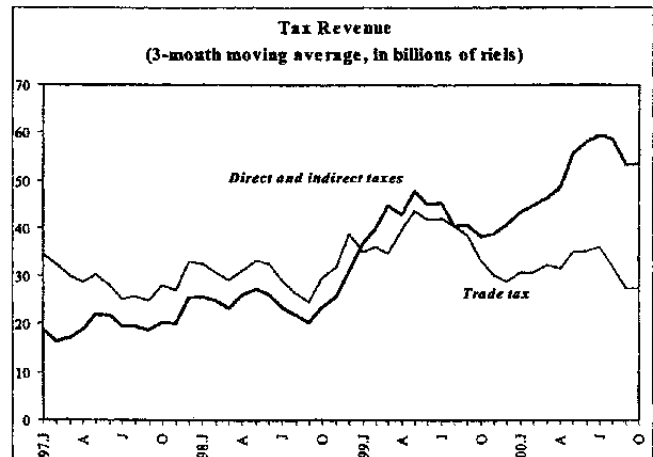
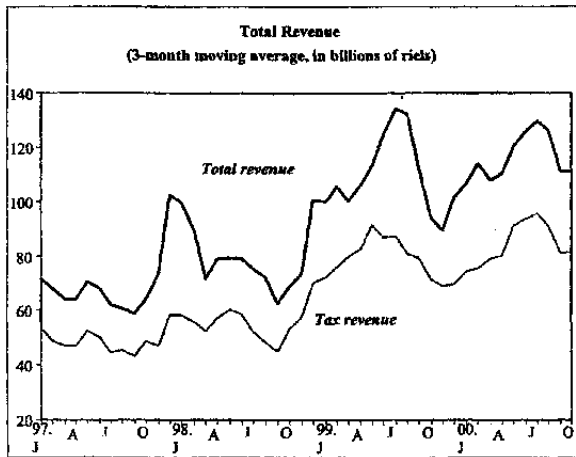


petroleum products rose, the increases have had only a marginal impact on the CPI because of a relatively low weight for petroleum products in the index.¹ However, food prices began to pick up after July, and further increases are expected owing to flood-induced shortages. As a result, the 12-month CPI inflation rate is projected to reach about 8 percent by end-2000 before falling back to less than 5 percent by the end of 2001.

7. **Fiscal policy in 2000 has been prudent, with improved revenue mobilization, and expenditure restraint.** The government has implemented the budget cautiously in the first ten months of the year, making room for spending for flood relief without a significant deterioration in the underlying fiscal balance. Current expenditure for flood relief in 2000 is estimated at 0.3 percent of GDP. Reflecting expenditure savings in other areas, the current budget surplus is projected at 1.3 percent of GDP, compared with the program target of 1.4 percent (Table 4). Improved implementation of donor-financed capital expenditure will lead to an increase in the overall deficit to 5.7 percent of GDP, compared with the program estimate of 4.6 percent. Taking into account available foreign financing, domestic financing of the budget would only marginally exceed the original program target, leading to a small reduction in the government's net indebtedness to the banking system by CR 20 billion (1½ percent of broad money).

¹ This reflects a relatively low dependence on petroleum products compared with more advanced economies, but also a need to revise the weights in the CPI. A new CPI series reflecting updated weights and covering additional provinces is expected in 2001.

8. **Underlying revenue performance has improved, and is likely to reach 11½ percent of GDP in 2000, close to the program target.²** Revenue from direct and indirect taxes, in particular profit tax from large companies and value-added tax (VAT), performed strongly, and above expectations. The increase partly reflects the revenue-enhancing measures implemented during mid-2000.³ However, revenue from trade taxes has continued to be weak and is expected to fall short of the program target. The poor performance in trade taxes reflects changes in the composition of imports (especially a decline in cigarette imports), and relatively slow progress in improving customs administration.



9. **Overall expenditure was contained, but only limited progress was made in increasing social sector spending.** The wage bill has been kept within the program target, and expenditure for defense and security is projected to decline in nominal terms in 2000 for the first time in more than a decade. Social sector spending was budgeted to increase by ½ percentage point of GDP over 1999. However, owing to a delay in the implementation of the Priority Action Program (PAP), and technical difficulties in administering spending at the district level, actual disbursements in the first ten months of the year have been lower than targeted.⁴ Disbursements are expected to increase considerably during the last two months of

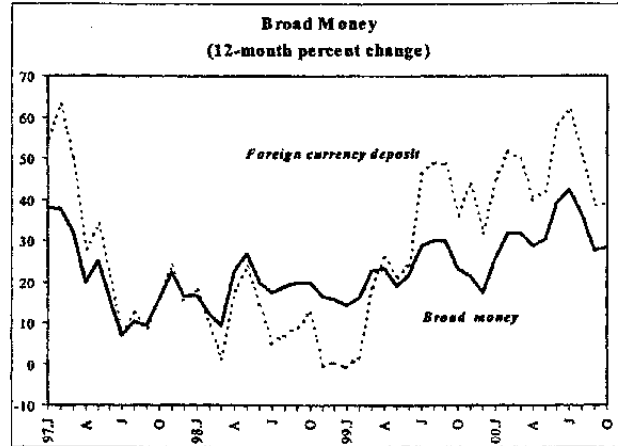
² After excluding exceptional revenue from the auction of garment export quotas in 1999, underlying revenue has improved from 10¾ percent of GDP in 1999.

³ These included a broadening of the VAT base to include 500 additional firms, increased royalties by tourist service providers (including from the Angkor Wat Temple Complex) and casinos, and stepped-up collection of arrears from telecommunications and leases of state assets.

⁴ Priority Action Programs aim to protect critical expenditures for such programs as primary education, basic health, and rural roads from possible revenue shortfalls.

the year, and total funds committed for the social sectors are expected to be broadly in line with the program.

10. Monetary developments have reflected the prudent fiscal policy and increased activity by the private sector. The growth rate of currency in circulation is expected to remain under 10 percent at end-2000, reflecting, in part, net repayments by the government to the banking system, and the overall importance of fiscal operations on changes in local currency. Broad money is expected to increase by 35 percent, in line with the program target. The increase in broad money is led by a rise in foreign currency deposits, reflecting increased economic activity and improved confidence in the context of a highly dollarized economy. Private sector credit growth picked up in mid-2000 from a very low base (about 8 percent of GDP) and is expected to increase by about 26 percent for the whole year (Table 5).



11. External developments have reflected increased garment exports and tourism earnings, sharply higher oil imports, and higher capital inflows. As a result, the current account deficit for 2000 (excluding official transfers) is projected to reach 13 percent of GDP, in line with the original program target. Net capital inflows improved, and official international reserves increased to US\$490 million (3 months of imports) as of end-November, in line with the program target (Table 7). The external value of the riel has remained broadly stable, while depreciating slightly against the U.S. dollar in the second half of the year (Chart 3).

12. Further progress was made in the major structural areas, broadly in line with program expectations, except on civil service reform and demobilization.⁵

- A new Financial Institutions Law was adopted at end-1999, and all banks were subject to relicensing under this law. After a period of supervisory assessment and MAE technical assistance, the National Bank of Cambodia (NBC) made final decisions on bank relicensing in November 2000. At the same time, the first phase of the Foreign Trade Bank's recapitalization was completed and the bank was granted a conditional commercial banking license.

⁵ A summary report on the implementation of structural reforms is contained in Table 3.

- A civil service census was completed in March 2000. Following the initial census, the government has implemented a computerized payroll system for the central administration and will extend the system to the provinces in 2001. However, formulation of a strategy for rationalizing the size of the civil service (originally targeted for June 2000) has been delayed.
- A military census was completed in December 1999, and the discharge of 1,500 soldiers under a pilot military demobilization program has been completed. Although implementation of the full program was delayed, the overall assessment of experience under the pilot has generally been positive, and a national workshop discussing this experience will be held by end-February 2001, as a key input into the preparation of the full program.
- In the area of forestry, a review of concessions was completed, several concessions have been canceled, and logging activities have been severely restricted for others. A Forest Crime Monitoring Unit (FCMU) was established in October 1999 with external participation, and several monitoring reports have been issued. Also, steps have been taken to establish the legal framework for forestry activities, including preparation of a revised Forestry Law which is expected to be presented to the National Assembly by end-February 2001.
- In tax and customs administration, the number of companies subject to VAT was increased, preshipment inspection for imports was reinstated in October, and ad hoc customs duty exemptions have continued to be avoided. The Ministry of Economy and Finance has also taken steps to improve the collection of tax arrears, and arrears associated with telecommunication charges and leases of state assets.

13. **In line with these developments, all quantitative and structural performance criteria were met, and other conditions proposed during the last review for completing the second review were observed, except for that related to the timing of the military demobilization program.**⁶ The completion of a pilot program for military demobilization has taken longer than expected because of significant delays in the release of committed donor financing. As a result, the first phase of military demobilization, involving 10,000 soldiers, is now expected to be launched by mid-2001. Since all of the donor funds have now been released for the completion of the pilot program, and measures are being taken to improve the mobilization of donor financing—including through a planned World Bank credit—prospects are good that the revised target date would be met, providing a basis for the completion of the second review.

⁶ At the time of the first review, launching of the first phase of the full demobilization program by November 2000 had been included as a prior action for the second review.

14. **The social effect of reforms initiated since 1999 has generally been considered to be positive.** Cambodia emerged from conflict with basic economic institutions and overall governance that did not meet even minimal standards, and there was ample scope for reforms to improve the welfare of vulnerable groups. While there is not yet the quantitative basis for a full analysis, staff expect that the reforms already implemented will have a positive impact on the poor. A significant expansion in spending for social services and infrastructure has been financed by the introduction of the VAT (which applies only to large tax payers) and other fiscal measures. Initial steps have been taken to build a banking system that should better serve future development needs, and forestry policy reforms should pave the way for setting standards for community forestry in the future. Social safety nets have been prominent in the design of the military demobilization program and are expected to be incorporated as part of a civil service reform strategy (see paragraph 23). Further progress in all these areas is dependent on the steadfast implementation of reforms, which will require substantial effort by the authorities.

III. POLICY DISCUSSIONS AND THE PROGRAM FOR 2001

A. Poverty Reduction Strategy and Medium-Term Objectives

15. **The government recently finalized an *Interim Poverty Reduction Strategy Paper (I-PRSP)*.**⁷ Unlike past poverty alleviation efforts primarily centered on promoting projects in the rural sector, the strategy outlined in the I-PRSP is broader and based on a multidimensional assessment of poverty. The new strategy provides for further strengthening macroeconomic stability to foster sustainable growth. The strategy also emphasizes the importance of improving access of the poor to employment opportunities and public services through human resource development and social sector spending. The strategy has been designed through a participatory process involving line ministries, civil society, the World Bank, the Asian Development Bank, other donors, and NGOs. The full PRSP is expected to address the areas of weakness identified in the Joint Staff Assessment (JSA) and to elaborate on the monitoring, sequencing, and costing of the policy actions identified in the I-PRSP, and will be completed by end-2001.

16. **Sustained economic growth is the foundation of the government's poverty reduction strategy.** This strategy is fully consistent with the objectives of the PRGF-supported program's macroeconomic framework.⁸ The medium-term program aims to restore economic growth to an annual average rate of 6 percent, keep inflation in low single digits, contain the external current account deficit to a level consistent with concessional financing and-FDI flows, and increase gross official reserves to about 4 months of import coverage

⁷ See Cambodia—Assessment of the Interim Poverty Reduction Strategy Paper, EBS/00/123.

⁸ See for example paragraphs 2.13 and 3.18 to 3.24 of the I-PRSP.

(Table 8).⁹ Following the recent flooding, agricultural production is projected to rebound in 2001, and continued growth in industrial production, construction, and tourism-related services should contribute to an increase in GDP growth to about 6 percent. The projected increases in output growth over the medium term are envisaged to be broad-based, stemming from agricultural and rural development, further growth in industrial production, and tourism development, and are premised on rising levels of private investment and savings, and improved delivery of public services in the context of fiscal reform.

B. Fiscal Policy

17. **The budget for 2001 has been framed to be in line with the medium-term fiscal objectives of the program (Box 2).** These objectives are to improve revenue mobilization, increase spending on essential public services, and maintain a sustainable fiscal position. The targeted restructuring of spending will rely heavily on a reduction in military and security spending. The staff emphasized the importance of further improving revenue mobilization to reach 13 percent of GDP in 2002.¹⁰ The 2001 budget, approved by the National Assembly in December, targets a current budget surplus of 1.4 percent of GDP and provides for additional measures to increase revenue to 12.1 percent of GDP. The authorities also indicated that a fundamental review of revenue policy and administration would be made in the context of the 2002 budget, taking into account technical assistance and support to be provided under the Technical Cooperation Action Plan (TCAP). Spending for priority social sectors and locally financed development expenditure is budgeted to increase further, but the overall fiscal deficit is targeted not to exceed 5¾ percent of GDP, similar to the estimated outturn in 2000. Taking into account projected external project financing and budget support, a further modest reduction in the governments' net indebtedness to the banking system is programmed. In the event of shortfalls in nonproject budget support, the expenditure program will be implemented cautiously, and the budgeted increase in locally financed development spending reduced, if necessary, to achieve the domestic financing target. Further room for expenditure adjustment is provided by contingency and reserve items (about 0.5 percent of GDP).

⁹ The medium-term framework presented in Table 8 is consistent with the one presented in the I-PRSP, but has been updated to reflect recent estimates of the near-term impact of flooding. The medium-term objectives remain fully consistent with the authorities' I-PRSP.

¹⁰ This will require a further broadening of the tax base, including through revisions to the Law on Investment. Weaknesses in the current revenue system and the reform agenda are described in the recent selected issues paper (SM/00/200, August 31, 2000).

Box 2. Cambodia: The 2001 Budget

In line with the medium-term fiscal objectives, the 2001 budget is aimed at raising total revenue by $\frac{1}{2}$ percentage point of GDP to 12.1 percent, and restructuring total expenditure to direct more funds to the social sectors and away from security and defense. The current balance is budgeted to remain in surplus (1.4 percent of GDP), and with expected external financing on concessional terms, no domestic financing of the budget will be needed.

In addition to the full-year effect of policies introduced in mid-2000, additional measures to yield revenue of CR 40 billion (0.3 percent of GDP) include:

- Expanding the VAT base by an additional 150 companies. Together with the full-year effect of FY2000 expansion by 500 companies, this broadening is projected to increase domestic VAT revenue by 10 percent compared to 2000.
- Other new revenue measures: (i) a 10 percent excise tax on entertainment services; (ii) new license fees on casinos; (iii) the introduction of a stamp system for tobacco products; and (iv) adjustments in excise tax rates to offset tariff reductions, with additional increases expected for a few selected products.
- In addition, the authorities will continue to strengthen revenue administration. The MEF will increase the number of qualified tax auditors and the number of companies subject to tax audits, and will improve the collection of visa fees. Pending the completion of revisions to the Law on Investment, the MEF will pay particular attention to investment companies, so that they comply with monthly advance payments of profit tax on the basis of one percent of monthly turnover, as required under the Law on Taxation. The reintroduction of preshipment inspection should improve overall customs administration. Under Cambodia's TCAP, a tax advisor (expected to be placed in early 2001) and customs advisor will assist the authorities in strengthening administration, and computer hardware and software will be provided. The authorities will also continue to strengthen nontax revenue collection, in particular from leased enterprises, the tourism sector, and telecommunication services.

On the expenditure side, the budget allocates increased funds for priority sectors.

- Expenditure for health, education, agriculture, and rural development is budgeted at 3 percent of GDP up from $2\frac{1}{2}$ percent in 2000, while expenditure for defense and security, is budgeted to fall to 3 percent of GDP from $3\frac{1}{2}$ percent in 2000.
- Recurrent expenditure will be contained, and appropriate contingency measures will be included, to avoid risks of expenditure overruns. The civil service wage bill will be kept at 1.7 percent of GDP, as the removal of irregular cases from the payroll has helped provide room for a 10 percent increase in basic wages. The budget includes CR 64 billion for contingencies, including for flood relief, and commune elections.
- To effectively increase the flow of funding for the social sectors, the government will continue to make efforts to improve budget operations. A Budget Strategy and Enforcement Center established in 2000 will be strengthened to improve the operational efficiency of budget execution. In addition, the 2001 budget increases funds under the Accelerated District Development and Priority Action Programs to CR 68 billion (compared to CR 27 billion in 2000). These programs allow provincial and district budget managers discretion to execute allocated funds; 30 percent of the total health budget and 9 percent of the total education budget are allocated under these programs. However, additional training for provincial and district budget managers is required. Technical assistance in this area will be provided by the World Bank and the Fund.

18. **The authorities are currently undertaking a comprehensive review of investment incentives in consultation with the World Bank, the Foreign Investment Advisory Service (FIAS), and the Fund (Box 3).** To protect the revenue position, the staff argued that granting of additional incentives for investors eligible for privileges under the Law on Investment should be considered as part of the ongoing comprehensive review of investment incentives, which is envisaged to include rationalization of several existing incentives that lead to significant revenue leakages. In the face of declining investment approvals in 2000, the authorities were concerned about the fragility of the garment sector and general difficulties in attracting foreign investors. During budget discussions in November 2000, they opted to eliminate the requirement for investment companies to pay the minimum profit tax (with effect from 2001), as a signal of the government's intent to address investor concerns. The authorities believe the revenue impact of this measure in 2001 will be limited, since monthly advance payment of profit taxes should continue to be made and will give rise to refunds (if eligible) in 2002. The mission noted that this decision could nonetheless undermine tax compliance, with a potential negative impact on revenue (0.1–0.2 percent of GDP). To compensate for this loss, the authorities have formulated additional revenue measures to protect the revenue position and are accelerating work to complete revision of the Law on Investment to rationalize investment incentives and support improvements in overall tax administration.

Box 3. Cambodia: Reform of the Tax Incentive System for Investment

Rationalizing tax incentives by revising the Law on Investment is essential for broadening the tax base. The current law, which governs all investment projects by Cambodians and foreigners, provides a complex and generous system of tax incentives, even by regional standards. Moreover, the regime remains heavily distortionary, selective, and complex, with significant foregone revenue.

The government is revising the Law on Investment with assistance from the Foreign Investment Advisory Service (FIAS). The revisions mainly aim at simplifying the system to improve transparency, reduce distortions, and increase fiscal revenue by eliminating excessive tax incentives. Notable revisions are expected to include: (i) eliminating a reduced 9 percent profit tax for all new projects; (ii) gradually replacing the 9 percent profit tax with the statutory rate of 20 percent for existing projects; (iii) reducing the tax holiday period from 8 years to 3 years and rationalizing eligibility criteria; and (iv) eliminating customs duties exemption and subjecting all imports of investment companies to a reduced and uniform duty rate.

In response to concerns about the profitability of investment companies, the minimum profit tax of 1 percent is being eliminated in 2001. This tax secures revenue of about 0.4 percent of GDP annually (0.2 percent from investment companies), but as it applies to all companies making profits or losses, the tax is considered distortionary and negates many of the benefits under the Law on Investment. With the repeal of the minimum profit tax for investment companies, monthly estimated profit tax (1 percent of monthly turnover) would continue to be paid, and would be subject to potential refunds after the filing of 2001 tax returns in 2002. Envisaged revisions to the Law on Investment, would provide the compensating revenue sources for 2002.

19. **Current expenditure is budgeted to increase in line with revenue.** Total current expenditure is projected to increase to 10½ percent of GDP from 10 percent in 2000, reflecting increased spending for the priority sectors, as well as additional funds for flood relief. During the first PRGF review, the authorities had agreed that further wage increases would be tied to the formulation of a reform strategy for the civil service by end-March 2001. The staff team strongly urged the authorities to maintain this policy so that any wage increase could be announced at the same time as the reform strategy. This was particularly important because further fundamental adjustments in wages in the future, within an affordable fiscal envelope, will require well-designed plans for a rationalization in the size of the civil service.¹¹ Nonetheless, in view of mounting social pressure for a salary adjustment, the authorities announced in December that basic wages for civil service, military and security forces will be increased by 10 percent with effect from January. The budget for wages and salaries will remain at 4 percent of GDP, as the increase applies only to basic wages (and not allowances) and the removal of irregular cases through the use of the recently established computerized payroll has limited the financial impact of the wage increase. The net cost of the increase for the whole year is estimated at CR 15 billion (0.1 percent of GDP) and will be financed by already approved contingency funds in the 2001 budget. In undertaking the wage increase, the authorities have reaffirmed their commitment to complete a rationalization plan for the civil service by end-March 2001 as agreed under the previous program review.

20. **The efficiency of spending for the priority social sectors will be critical to the success of the poverty reduction strategy.** The introduction of Priority Action Programs (PAP) in October 2000, although later than expected, should improve the delivery of funds to priority social areas. Funds provided to priority sectors under the program will be substantially expanded in the 2001 budget (by 0.5 percent of GDP) and capacity problems at the district level in the Ministry of Health will be addressed through training of district managers in the new disbursement procedures. The authorities were encouraged to advance the needed funds to the social sectors and to fully meet conditionality in this area as called for under the World Bank's SAC program. Improving coordination between the Treasury and line ministries in the implementation and monitoring of government expenditure figures prominently in the technical assistance that will be provided under the TCAP program.

21. **Further progress in reorienting public expenditure to priority areas is dependent on the timely implementation of the military demobilization program.** Now that the pilot program is being completed, donors are beginning to come forward to finance the full program, but firm assurances will be needed in the coming months for implementation to begin by mid-2001, as now envisaged. Any further delays would affect the reorientation of expenditure for the social sectors—particularly for the 2002 budget. The staff urged the authorities to build momentum behind this important initiative and take

¹¹ The last increase in basic wages was a 30 percent increase granted in April 1999. Current wage levels are extremely low (averaging about \$20–25 per month).

necessary steps to secure donor financing and implement the program so as to demobilize 30,000 soldiers by the end of 2002, as targeted. The authorities emphasized their determination to fully implement the program and expressed frustration with delays in the disbursement of donor financing, including the delays that were experienced under the pilot program. In the meantime, the authorities are preparing the technical work for the full implementation of the program so that at least 10,000 soldiers can be demobilized in 2001 (Box 4).¹²

22. Adopting a civil service reform strategy is also needed to improve the overall delivery of public services and ensure the medium-term viability of the fiscal program. The government has achieved significant progress in completing the census earlier in 2000. As a result, more than 6,000 "ghost" workers and irregular cases were identified (4 percent of the civil service), and these workers were ordered in August 2000 to be removed from the payroll. A monitoring committee has been established to verify removal of all of the irregular cases using the computerized payroll for central administration. Since the severe flooding delayed the finalization of the computerized payroll for provincial administration, the staff urged the authorities to complete the computerized payroll as soon as possible to establish a monitorable and controllable database as a necessary condition for effectively implementing the civil service reform strategy. The authorities reaffirmed that the delays in completing the computerized payroll would not affect their ability to formulate a strategy to rationalize the civil service, in consultation with the World Bank and other development partners, by end-March 2001.

23. The social impact of military demobilization and civil service reform will be an important issue as the reform program proceeds. The military demobilization program has been formulated in close consultation with the World Bank and major donors, and provides financial and in-kind assistance spread out over several years for the reintegration of soldiers into local communities. For civil service reform, the authorities have been conducting a study of social safety nets, with technical assistance from the UNDP, as part of their preparation for formulating a comprehensive reform strategy.

¹² Implementing the military demobilization program forms part of the conditionality under the World Bank SAC program.

Box 4. Cambodia: Pilot Military Demobilization Program

Background

In January 2000, the Cambodian government presented to donors the first draft of the pilot demobilization program involving 1,500 soldiers in four provinces. The program included four components: registration, discharge, reinsertion and reintegration. The total cost of the pilot program on a per soldier basis was estimated at about US\$1,500, consisting of cash payment (US\$240), in-kind assistance, such as rice allowance (US\$741), expenses associated with the discharge centers (US\$333), and administrative costs (US\$122). The first phase of the full-scale program was expected to begin in November 2000 with 10,000 soldiers to be discharged, followed by 10,000 soldiers each in 2001 and 2002.

Implementation of the Pilot Program

Under the pilot program, 1,500 soldiers in four provinces were discharged and reinsertion benefits were provided between May and July. However, the planned reintegration activities, which included the provision of shelter and agricultural assistance, were substantially delayed by the slow release of committed donor funds. As a result, it became impossible to launch the first phase of the full demobilization program by end-November. In late October, the remaining funds for the pilot program were received and will be disbursed through the administered account set up by the World Bank. Currently, the World Bank is preparing a US\$15 million credit to finance the full-scale demobilization program, which is tentatively expected to be approved by the Bank Board in April 2001.

A roundtable meeting between the government and donors was held in November to discuss how to proceed with the rest of the pilot program. With donor funds available, the meeting focused on completing the pilot project, and drawing lessons and using them to finalize the design of the full program. The following agreements were reached:

- The full-scale demobilization program would not start until all donor funds have been disbursed in the special account for demobilization;
- The timing of launching the first phase of the full program should coincide with the agricultural season, implying no discharge during the rainy season (June to October);
- The number of soldiers to be discharged in the first phase of the full program would not be limited to 10,000, provided that the funds are available and the government has adequate implementation capacity;
- All demobilized soldiers would receive "equal value" in assistance, but under different forms of goods and services based on the assessed individual needs.

Preliminary Assessment of the Pilot Program

As part of the design and implementation of the pilot program, the socio-economic profiles of the demobilized soldiers have been updated to provide a more realistic assessment of the needs of soldiers and their families. The studies available so far include: (i) a labor market study, (ii) a baseline survey on the needs of vulnerable soldiers in two provinces, (iii) a study of the needs of vulnerable groups, (iv) a study of underage soldiers, and (v) a health assessment of demobilized soldiers. Some of the studies were not restricted to the four provinces involved in the pilot program, and actions are already under way to apply the results to the design of the full demobilization program.

The implementation of the pilot program has been closely monitored by the international community because of concerns about the surrender of weapons, the factional makeup of demobilized soldiers, and the potential for financial abuse. Key donors oversaw financial aspects, and monitored the discharge operations of the pilot program. Four assessment reports on the pilot program are available, including: (i) a report from the Working Group for Weapons Reduction in Cambodia, (ii) a report from a key donor, (iii) a review of the financial and accounting system of CVAP by Pricewaterhouse Coopers, and (iv) a review by an independent consultant commissioned by the donors.

The preliminary assessments have generally been positive. The handling of the pilot program by the government has exceeded expectations in many aspects, while also providing valuable input and lessons for the full-scale program, especially in the areas of the administration of donor funds and the provision of reintegration packages for discharged soldiers. The preliminary assessments found the pilot to be well-organized, and cost savings were identified in several aspects of the program. Although no evidence of financial mismanagement was discovered during the pilot, some shortcomings in the accounting system were noted and these will be addressed in the full-scale program.

Next Steps

With donor funds available, it is envisaged that the pilot program will be completed in early 2001, and a national workshop to evaluate and draw lessons for the full program is envisaged to take place before end-February 2001. As a result, the government plans to launch the first phase of the full-scale program before end-May 2001, and continue the process in late 2001 with a view to completing the program by end-2002.

C. Monetary Policy and Bank Restructuring

24. **The monetary program for 2001 is designed to support the growth and inflation objectives.** Reflecting the continued avoidance of bank financing of the budget, the net domestic assets of the NBC are programmed to decline by 7 percent of reserve money, and currency in circulation is projected to increase by 8 percent. The annual increase in broad money is targeted at 24 percent, owing to the continued growth in foreign currency deposits. Domestic credit is programmed to increase by 20 percent, with restrained fiscal policy providing room for a significant increase in private credit (25 percent) to support economic recovery. The implied further reduction in velocity in 2001 is consistent with the ongoing monetization of the economy from a very low base.¹³ Given the recent strong growth in private credit, and the risk that increased foreign currency deposits could lead to a further expansion of credit if and when financial intermediation improves, the staff emphasized that improving oversight and analysis of credit developments will become increasingly important. The NBC agreed with this concern, and noted that they had recently stepped up their monitoring of credit developments, including by requiring banks to make regular submissions of their business and credit plans. They also felt, however, that given the very low level of existing credit there was room for further strong growth in line with economic expansion.

25. **Substantial progress has been made in bank restructuring in 2000 (Box 5).** The staff welcomed the actions that have been taken to liquidate nonviable banks and initiate a restructuring process for others, including the state-owned Foreign Trade Bank (FTB). The authorities were encouraged to continue their strong cooperation with MAE technical assistance in implementing a well-designed bank restructuring strategy that would require consistent and timely action. In particular, it will be important to closely monitor steps taken by potentially viable banks against their MOUs, signed with the NBC, and to introduce a commercial culture in the FTB in 2001 to prepare the bank for eventual privatization by end-2001 as programmed. The authorities expressed their commitment to follow through in these areas, while also stressing difficulties they have faced in finding liquidators for nonviable banks. Regarding the accounts of the NBC, the data that has been provided comply with the Fund's initial requirements under the Safeguards Assessment, and the authorities have agreed to undertake an external audit of the 2000 financial accounts by end-April 2001.

¹³ Reflecting the limited development of the banking system, the stock of broad money currently amounts to only 14 percent of GDP. Over the medium term, reductions in velocity are expected to level off, with the money supply eventually growing more in line with overall GDP growth.

Box 5. Cambodia: Banking Reform

Cambodia's banking system consists of 31 banks, comprising 2 state-owned banks, 7 foreign bank branches, and 22 privately-owned local banks. Total loans and deposits amount to only 8 percent and 14 percent of GDP, respectively, mostly denominated in foreign currency. With technical assistance from MAE, the NBC has made progress in restructuring the banking system since late 1999.

Private commercial bank reform

A major problem is the significant number of inactive banks. In the past, the NBC's supervision capacity was weak and compliance with prudential regulations was limited. There was little transparency in banking activities, leading to lack of confidence on the part of the public and mutual distrust among the banks.

The new Financial Institutions Law adopted in November 1999 has strengthened the NBC's supervision authority, enabling it to relicense all existing banks. As a first step, on July 31, 2000, the NBC closed three insolvent banks. For the remaining 26 banks, the NBC evaluated their viability using CAMELS rating methodology and on-site inspections, and classified them into three categories: those relicensed unconditionally (4 branches of foreign banks), relicensed with corrective measures (14 banks), and nonviable (8 banks).

On December 8, 2000, the NBC publicly announced that the 8 nonviable banks would be liquidated. Memoranda of Understanding (MOU) which detail the timetable of capital injection and corrective actions are being signed with the remaining banks that require corrective actions. The NBC will supervise these banks intensively and monitor their performance in accordance with the MOUs. If a bank fails to meet its commitments, the NBC will take additional action, including suspension or withdrawal of the banking license. The staff expects that several more banks will not be able to fully adhere to their MOUs and will require further corrective action in the future.

Thus far, the closure of banks has gone smoothly. Consistent support was received from the relevant government agencies and the Prime Minister. The highly segmented nature of the banking system also helped avoid bank runs and other systemic risks. The amount of total deposits and loans with nonviable banks is relatively small, and the impact on depositors and borrowers is limited. There are no interbank loans to nonviable banks, and an impact on other relicensed banks would not be a major concern.

Foreign Trade Bank (state-owned bank) reform^{1/}

The purposes of the FTB restructuring are to: (i) separate it from the NBC as an independent entity; (ii) develop it as a market-oriented commercial bank; and (iii) privatize it by end-2001. The size of the FTB's assets and liabilities in local currency is the largest among all banks (1 percent of GDP). With effective restructuring, the FTB can potentially play a major role in Cambodia's banking sector.

In August 2000, the legal separation of the FTB from the NBC was completed. The NBC finalized a Memorandum of Understanding that established the FTB's legal and operational independence and its Board of Directors. However, in the transition period, the NBC still owns the FTB, and the Board of Directors includes representatives of the NBC.

In early December 2000, the NBC gave the FTB a banking license. In October, Price Waterhouse Coopers completed the FTB audit and calculated its net worth as CR 3.9 billion (US\$1 million). In November, the NBC transferred part of its physical assets, estimated at CR 6.4 billion (US\$ 1.7million), for the FTB's headquarters. The total capital of FTB amounts to CR 10.3 billion, thus satisfying the initial minimum capital requirement of CR 10 billion.

To fully recapitalize the FTB to CR 50 billion (US\$ 13 million), the Ministry of Economy and Finance (MEF) will issue a recapitalization bond by mid-2001. In January 2001, the NBC, the MEF, and the FTB set up a working committee to make preparations for a recapitalization bond. MAE will provide technical assistance in designing the details of the bond issue.

To support eventual privatization, modernizing the FTB's management and introducing a market-oriented business culture is essential. The FTB is currently seeking an experienced manager as one of the Board members. The government is also requesting technical assistance from the International Finance Cooperation and the AsDB to complete the restructuring and prepare for privatization.

^{1/} Another state-owned bank, the Rural Development Bank (RDB), is operating as a wholesale bank for microfinance institutions. The AsDB is providing technical assistance in improving the operation of the RDB and developing microfinance institutions.

D. External Sector Policies and Capacity to Repay the Fund

26. **The program will continue the present exchange rate policy.** Noting the commitment of the authorities to keep the margin between the official exchange rate and the private market rate at no more than 1 percent, the staff urged the authorities to move to eliminate the margin entirely and unify the rates. The authorities stressed the signaling effect provided by setting the official rate, and that this still plays a stabilizing role in the context of a thin foreign exchange market. They emphasized their commitment to keep any divergence at less than 1 percent, and have moved to eliminate the margin entirely during orderly market conditions. The authorities concurred with the mission's recommendation to accept the obligations of Article VIII, Sections 2, 3, and 4 in the context of the 2001 Article IV Consultation.

27. **The program provides for prudent external debt management and further trade liberalization.** The prohibition on new nonconcessional borrowing will be continued, and the staff stressed the importance of a careful review of all external borrowing to ensure that any loan contracted is consistent with established concessionality criteria. The program assumes that Cambodia will reach agreement on the outstanding bilateral agreements under the 1995 Paris Club agreement, which provided for Naples terms treatment of Cambodia's debt. Technical discussions have taken place, but have not been concluded, and the staff urged the authorities to make further progress in completing outstanding bilateral agreements (e.g., with the Russian Federation and the United States).¹⁴ Cambodia is liberalizing its trade system as part of the WTO accession process and the implementation of the ASEAN Free-Trade Agreement. The authorities have already provided answers to the WTO questionnaire in June and December 2000, and are hopeful that the accession process will be completed by 2002.

28. **The staff welcomed the authorities' decision to reduce the number of tariff bands to 4, and the maximum tariff rate to 35 percent in the context of the 2001 budget.**¹⁵ They urged the authorities to continue this process in the formulation of the 2002 budget by further lowering the maximum rate to 30 percent and reducing the unweighted average to less than 15 percent as called for under the program, and in line with FAD recommendations for compensating revenue measures. The authorities reaffirmed their

¹⁴ With regard to very small amounts outstanding with other former CMEA countries where comparable action is needed, progress has been made toward completing rescheduling agreements with the Czech Republic and Slovakia.

¹⁵ This reduction is estimated to lower the average unweighted tariff rate from 17½ percent to about 16½ percent. Cambodia is currently rated 6 in the Fund's trade restrictiveness index (moderately restrictive). The tariff changes being taken in 2001 would have only a marginal impact on the index. However, reducing the average tariff rate below 15 percent, and progress in eliminating more of the remaining nontariff barriers (e.g., on log exports) could reduce the rating to 2 by 2002.

commitment to reduce the average tariff rate to below 15 percent, but expressed concern with the revenue implications of reducing the maximum rate from 35 percent to 30 percent. The mission emphasized that estimates of compensating revenue measures have been provided, and indicated that the modalities of meeting the target of an average tariff rate below 15 percent should be agreed in the context of the formulation of the 2002 budget, based on the experience with tariff reduction in 2001, and taking into account technical assistance support in customs administration to be provided under the TCAP program.

29. **The projected external current account deficit should be sustainable over the medium term in view of prospective net official concessional financing and debt relief.** Notwithstanding the recent floods and rising oil prices, the current account deficit (excluding official transfers) is expected to stay in the range of 12–13 percent of GDP during 2000–01, owing to the strong performance of garment exports and tourism. It is projected to decline gradually to about 10 percent in 2005, partly aided by the resumption of forestry exports and further export diversification. Including official transfers, the deficit would decline from about 5½ percent of GDP in 2001 to about 4 percent by 2005. The main risks to external sustainability would be slower export growth, perhaps due to economic slowdown or reduced market access to Cambodia's primary market (the United States), and reduced inflows of donor support and other capital flows arising from delayed implementation of demobilization or other aspects of the reform agenda.

30. **Cambodia should have no difficulty in continuing to service its obligations to the Fund.** In addition to its recent good record of meeting scheduled payments, the targeted level of international reserves under the current medium-term scenario provides sufficient room for future payments. Given the highly concessional nature of Cambodia's rescheduled debts, once outstanding bilateral agreements are concluded, debt service payments, including on Fund credit, are projected to remain at around 4 percent of goods and service receipts.

E. Other Structural Reforms

31. **Structural reforms for 2001 will focus on those areas critical for achieving the macroeconomic objectives.** Foremost among these are improvements in tax administration and expenditure management, bank restructuring, military demobilization, civil service reform, and trade liberalization—all discussed above. Other priority areas are forestry policy and legal reform. Additional structural policies for supporting the authorities' poverty reduction efforts are described in detail in the I-PRSP.

32. **Forestry policy has undergone a fundamental change in its orientation during the first year of the program.**¹⁶ The staff team welcomed the progress that has been made and encouraged the authorities to continue with the important actions scheduled for the year

¹⁶ The history of forestry policy and the overall reform effort is described in the Selected Issues paper prepared for the 2000 Article IV consultation (SM/00/200).

ahead, including submission of a revised Forestry Law to the National Assembly by end-February 2001, conducting a review of forest revenue policy by end-April 2001, canceling further forestry concessions that do not complete restructured concession agreements by end-September 2001, and taking steps to further improve the operations of the FCMU.

33. Progress in preparing basic legislation to improve the legal environment for private sector activity has been slower than expected, but strong efforts will be made in the period ahead. The delays were caused primarily by an overloaded agenda of legal reform in the face of extremely limited implementation capacity. A draft law on commercial standards has already been approved by the National Assembly, a draft law on trademarks and commercial enterprises will be submitted to the Assembly in early 2001, laws on commercial contracts and arbitration by mid-2001, and laws on corporate insolvency (with technical assistance from LEG) and secured transactions by end-2001.

F. Economic Statistics and Fiscal Transparency

34. Key economic data needed for program monitoring and surveillance purposes are available, but Cambodia's statistical capabilities need further upgrading. Revised national account estimates have been recently developed with AsDB assistance, but the reliability of the estimates remains uncertain, largely owing to difficulties in recording informal sector activities. The National Institute of Statistics is also in the process of updating the weights and coverage of the consumer price index. As a result, new inflation benchmarks covering five provinces and reflecting updated patterns of household consumption are expected to be available in the near future. Largely due to limited capacity in the Ministry of Economy and Finance and the NBC, earlier technical assistance recommendations in the areas of government finance, and balance of payments statistics fell short of full implementation. Recent experience has been more positive, and additional Fund assistance on government finance and balance of payments statistics has been scheduled for the first quarter of 2001. In the period ahead, compilation of relevant social indicators to improve poverty diagnosis and monitoring capabilities will be made a high priority to meet the requirements set under the full PRSP. The authorities have also indicated interest in participating in the General Data Dissemination System (GDDS) with a view to using GDDS as a framework for statistical development.

35. A comprehensive framework for enhancing governance and fighting corruption has been agreed with donors and will be important for improving fiscal transparency. The Governance Action Plan (GAP) initially presented at the May 2000 Consultative Group Meeting has been amended following discussions with donors. The government plans to formally adopt the revised version by January 2001 and to prioritize reform actions within a timeframe agreed with donors while seeking adequate funding. The GAP calls for reforms in crosscutting areas where improvements are pre-requisites for addressing governance concerns, including reform in the judicial and legal system, civil service administration, and public finance management. Improvement of customs and tax administration, as well as budget management, are priority areas. Cambodia also still lacks an adequate legal framework that would establish the rule of law and underpin the development of basic

economic institutions. A new Audit Law was recently adopted, but its implementation has been hampered by delays in appointing board members of the National Audit Authority. Civil and penal codes and procedures, as well as key land, natural resources and commercial legislation, are also under preparation.

G. Implementation Capacity and Program Monitoring

36. **Thus far, sufficient internal consensus to move the program forward has been maintained, but important reforms fundamental to the success of the program remain to be implemented in the period ahead**—in particular, revenue mobilization, expenditure management, and military and civil service reform. Significant progress has been made in the macroeconomic program and in key structural policies, particularly bank restructuring. However, delays have been experienced in some areas, owing to weaknesses in implementation capacity and difficulties in reaching internal consensus on reforms affecting entrenched interests. To strengthen administrative capacity, effective implementation of the forthcoming TCAP (Annex IV) will be critical. The TCAP program is aimed at strengthening basic economic institutions and improving capacity to conduct macroeconomic policy, with a focus on those components judged as most critical to achieve the objectives of the government's poverty reduction strategy. The government will need to devote sufficient resources to the development of local capacity to make this program effective.

37. **The program for 2001 will continue to be monitored through quantitative and structural performance criteria outlined in paragraph 25 of the MEFP.** The quantitative benchmark/performance criterion on net domestic assets (NDA) of the banking system has been replaced with the NDA of the central bank to improve the authorities' ability to monitor, control, and be accountable for the target. The coverage of the program ceiling on external debt has also been revised in accordance with the new guidelines. Structural conditionality in 2001 focuses on bank restructuring, tax administration, financial transparency, and forestry policy. Given the importance of administrative reform and military demobilization for achieving the fiscal and poverty reduction objectives, the program also sets structural benchmarks in these areas that will be monitored in close consultation with the World Bank. Semi-annual disbursements of SDR 8.4 million each are envisaged for the remainder of the arrangement (Table 10) subject to the observance of performance criteria and the completion of semi-annual reviews. The third review is expected to be completed by end-July 2001.

IV. STAFF APPRAISAL

38. **Cambodia has made a good start in the implementation of economic reforms so far under its PRGF-supported program, but the reform agenda remains large.** Further strong efforts are needed in the period ahead to build basic economic institutions, protect macroeconomic stability, improve governance, and make inroads to reducing pervasive poverty.

39. **Economic performance in 2000 remained broadly satisfactory, despite the adverse impact of severe flooding in the second half of the year.** This performance was due to further improvements in revenue mobilization and continued restraint in spending. These efforts have kept core inflation at a low level and made room for the needed emergency flood relief. Furthermore, good progress was made in key structural reforms, particularly in the areas of forestry policy, bank restructuring, and initial steps to improve tax and customs administration.

40. **The second year of the PRGF-supported program seeks to build on this initial progress while addressing areas where reforms have been delayed or further improvement is required.** Its main goals are to raise revenue and improve expenditure composition and budget management, continue bank restructuring, and deepen other structural policies that are key to macroeconomic stability and poverty reduction. Prudent monetary and exchange rate policies will continue to be needed, supported by the avoidance of domestic financing of the budget.

41. **The staff welcomes the I-PRSP that the authorities have prepared.** The Joint Staff Assessment notes the strengths of the authorities approach, particularly the detailed discussion of the existing strategy and a clear agenda for a participatory process. Coordination should be strengthened among government ministries, as well as with internal and external partners, to ensure the preparation of a high quality PRSP by end-2001.

42. **Fiscal reform will continue to be the cornerstone of the economic reform effort.** Initial progress has been made in improving revenue, albeit from a very low starting point. To meet the program's revenue objective, it will be critical to implement the new tax measures and make further headway in improving tax and customs administration in 2001. More specifically, the staff urges the government to complete in a timely way revisions to the Law on Investment to rationalize tax incentives and improve transparency, while strengthening the application of existing provisions under the Law on Taxation. Further progress in improving the flow and efficiency of government spending for the priority social sectors will also be important for achieving poverty reduction objectives.

43. **Successful implementation of military demobilization and civil service reform—both of which pose particular challenges—will be vital to the success of the government's poverty reduction and growth strategy.** Further reductions in defense and security spending will be necessary to allow increased spending for priority areas. The staff urges the authorities to build momentum to bring the demobilization program back on track—making up as much as possible the delays to date—and to complete the necessary preparation and secure donor financing to begin the first phase of the program by mid-2001. Administrative reform is one of the priority areas for preserving a sound fiscal position, improving the delivery of public services, and reducing corruption. The staff welcomes the progress that has been made in conducting a civil service census, eliminating irregular workers, and beginning to establish a computerized payroll system. It is essential that the computerized payroll system be completed to validate the results of the census and to provide a monitorable benchmark for the implementation of civil service reform. The staff

would have preferred that the recently granted wage increase be timed with the announcement of a civil service reform strategy. While the recent increase was cautious and the macroeconomic impact has been contained, it highlights the importance of the government accelerating its efforts to formulate such a strategy consistent with resource constraints, and in consultation with the Bank and other development partners, by end-March 2001, as envisaged under the program.

44. Banking reform has proceeded successfully, as envisaged under the program. The staff welcomes the actions taken by the central bank—in line with MAE recommendations—to close nonviable banks, and initiate a restructuring process for other banks that are potentially viable. It will be critical for the central bank to closely monitor performance of these banks in the period ahead and continue to take timely action when banks do not meet the requirements of their restructuring agreements. It will also be important for the authorities to take follow-up steps to introduce a commercial culture in the Foreign Trade Bank, and fully prepare the bank for eventual privatization as programmed.

45. Cambodia's external position is expected to remain manageable over the medium term. The external current account deficit widened in 2000, primarily reflecting strong growth in imports, in line with economic recovery. This deficit is expected to decline gradually over the medium term and be financed by higher aid flows and foreign direct investment. Over the medium term, external viability will continue to depend on the sustained implementation of policies and continued donor support. In this regard, successful conclusion of outstanding bilateral rescheduling agreements and prudent debt management will be key elements. The staff also welcomes the authorities' commitment to complete the process for joining the WTO, and to further reduce average import tariff rates during the program period. The staff encourages the authorities to maintain their commitment to reduce maximum rates from 35 to 30 percent as agreed under the program.

46. The staff urges the authorities to make effective use of planned technical assistance under the Technical Cooperation Action Plan. The TCAP program will provide comprehensive support in key areas to support macroeconomic stability and poverty reduction objectives. It will be important for the authorities to take the necessary steps to ensure that envisaged improvements in local capacity will take place. The staff also urges the authorities to make further progress in improving economic statistics, especially for government finance, balance of payments, and national accounts statistics. Participating in the GDDS in the near future would be very useful as a framework for statistical development.

47. Cambodia has made good progress under the first year of the program and the staff supports the authorities' request for the completion of the second review under the PRGF. Risks to program implementation continue, however, stemming from the still fragile governance environment, difficulties in reaching internal consensus given the complex nature of some reforms, and weak implementation capacity. Close program monitoring and a comprehensive program of technical assistance seek to address these risks. The policies for 2001 set out in the Memorandum of Economic and Financial Policies are designed to make

further progress in implementing reforms and address areas where delays have been experienced, and provide a solid basis for the continuation of Fund support. Accordingly, the staff recommends that the Executive Board complete the second review under the PRGF.

V. PROPOSED DECISION

48. The proposed decision, which may be adopted by a majority of the votes cast, is proposed for adoption by the Executive Board:

1. Cambodia has consulted with the Fund in accordance with paragraph 2(dd) of the three-year arrangement for Cambodia under the Poverty Reduction and Growth Facility (PRGF) (EBS/99/188, Supplement 1, 2/22/00) and paragraph 4 of the letter dated August 31, 2000 from the Senior Minister of the Ministry of Economy and Finance and the Governor of the National Bank of Cambodia, in order to review program implementation and reach understandings regarding the conditions for disbursements under the arrangement for the period through December 2001.

2. The letter dated December 18, 2000 from the Senior Minister of the Ministry of Economy and Finance and the Governor of the National Bank of Cambodia, together with its Memorandum of Economic and Financial Policies for 2001 ("the Memorandum"), shall be attached to the PRGF arrangement for Cambodia, and the letters dated September 29, 1999 and August 31, 2000 from the Senior Minister of the Ministry of Economy and Finance and the Governor of the National Bank of Cambodia, together with their respective attachments, shall be read as supplemented and modified by the letter dated December 18, 2000 and the Memorandum.

3. Accordingly, the PRGF arrangement for Cambodia shall be amended as follows:

a. the word "and" shall be deleted at the end of paragraph 1(cc)(i);

b. the full-stop at the end of paragraph 1(cc)(ii) shall be replaced with "and", and the following shall be added as a new paragraph 1(cc)(iii):

“(iii) the fifth disbursement, in an amount equivalent to SDR 8.357 million, will be available on December 15, 2001, at the request of Cambodia and subject to paragraph 2 below.”;

c. paragraph 2(a)(i) shall be amended to read as follows:

“(i) the ceiling on the net domestic assets of the central bank, or”;

d. paragraph 2(a)(v) shall be amended to read as follows:

“(v) the ceiling and sub-ceilings on the contracting or guaranteeing of external debt by the public sector.”;

e. the second sentence of paragraph 2(aa) shall be replaced with the following:

“Cambodia will not request the fourth disbursement referred to in paragraph 1(cc)(ii) above if the Managing Director of the Trustee finds that the data as of March 31, 2001 indicate that any of the ceilings and floors referred to in paragraphs 2(a)(i) to 2(a)(v) of this arrangement, as specified in Table 1 of the Memorandum of Economic and Financial Policies attached to the letter from the Senior Minister of the Ministry of Economy and Finance of Cambodia and the Governor of the National Bank of Cambodia dated December 18, 2000, was not observed. Cambodia will not request the fifth disbursement referred to in paragraph 1(cc)(iii) above if the Managing Director of the Trustee finds that the data as of September 30, 2001 indicate that any of the ceilings and floors referred to in paragraphs 2(a)(i) to 2(a)(v) of this arrangement, as specified in Table 1 of the Memorandum of Economic and Financial Policies attached to the letter from the Senior Minister of the Ministry of Economy and Finance of Cambodia and the

Governor of the National Bank of Cambodia dated December 18, 2000, was not observed.”;

f. the following shall be added to the end of paragraph 2(bb):

“Cambodia will not request the fourth and fifth disbursements referred to in paragraph 1(cc)(ii) above if the Managing Director of the Trustee finds that Cambodia has not carried out its intentions with respect to the structural performance criteria specified in Table 2 of the Memorandum of Economic and Financial Policies attached to the letter from the Senior Minister of the Ministry of Economy and Finance of Cambodia and the Governor of the National Bank of Cambodia dated December 18, 2000.”;

g. in paragraph 2(cc), the words “third and fourth” shall be amended to read as “third, fourth and fifth”; and

h. the second and third sentences of paragraph 2(dd) shall be replaced with the following:

“Cambodia will not request the fourth disbursement specified in paragraph 1(cc)(ii) above until the Trustee has determined that the third review referred to in paragraph 5 of the letter from the Senior Minister of the Ministry of Economy and Finance of Cambodia and the Governor of the National Bank of Cambodia dated December 18, 2000, and paragraph 25 of the Memorandum of Economic and Financial Policies attached thereto, has been completed. Cambodia will not request the fifth disbursement specified in paragraph 1(cc)(iii) above until the Trustee has determined that the fourth review under this arrangement has been completed. The timing of the fourth review shall be established during the third review referred to above.”

4. The Fund has reviewed the Interim Poverty Reduction Strategy Paper (“IPRSP”) submitted by Cambodia and determines that it provides a sound basis for Fund concessional financial assistance.

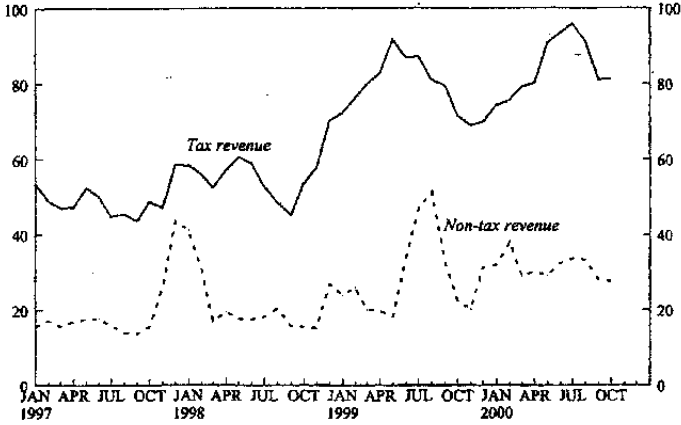
5. The Fund adopts the following decision in principle, which shall become effective on the date on which the Fund decides that the World Bank has concluded that the IPRSP submitted by Cambodia provides a sound basis for World Bank concessional financial assistance:

“The Fund decides that the second review contemplated in 2(dd) of the arrangement for Cambodia under the Poverty Reduction and Growth Facility (PRGF) (EBS/99/188, Supplement 1, 2/22/00) is completed, and that Cambodia may request the third disbursement referred to in paragraph 1(cc)(i) of the arrangement, on the condition that the information provided by Cambodia on the implementation of the measures specified in Table 2 of the Memorandum of Economic and Financial Policies attached to the letter from the Senior Minister of the Ministry of Economy and Finance of Cambodia and the Governor of the National Bank of Cambodia dated December 18, 2000 is accurate.”

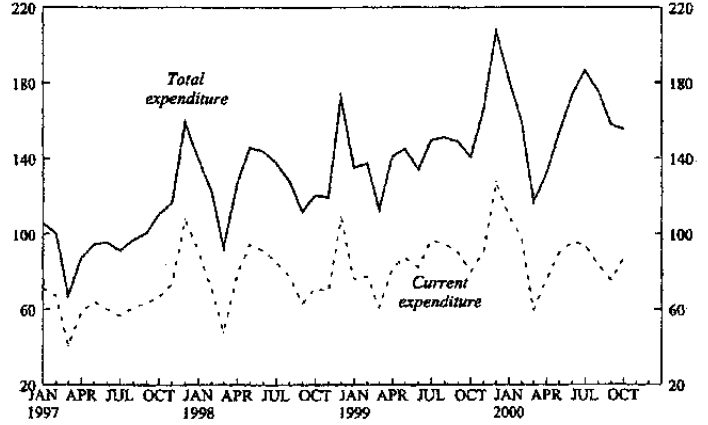
CHART 1

CAMBODIA
SELECTED ECONOMIC INDICATORS, 1997-2000

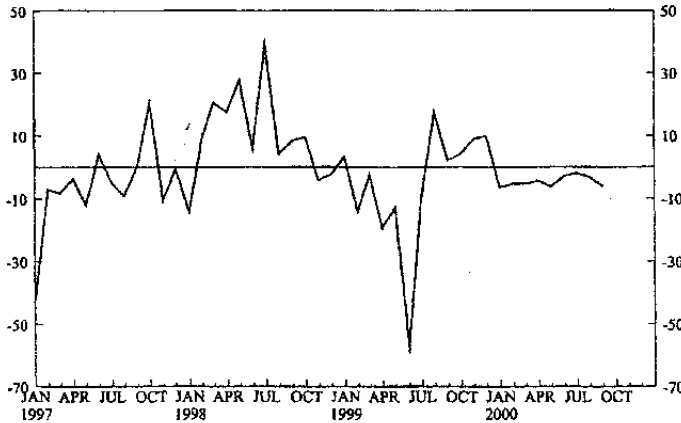
General Government Revenue
(3-month moving average, in billions of riel)



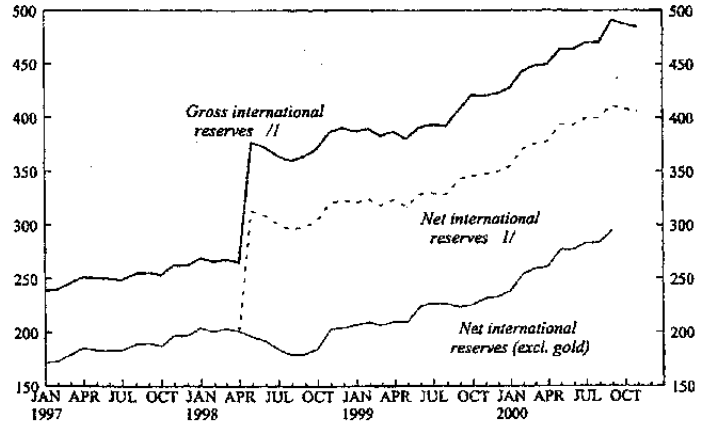
General Government Expenditure
(3-month moving average, in billions of riel)



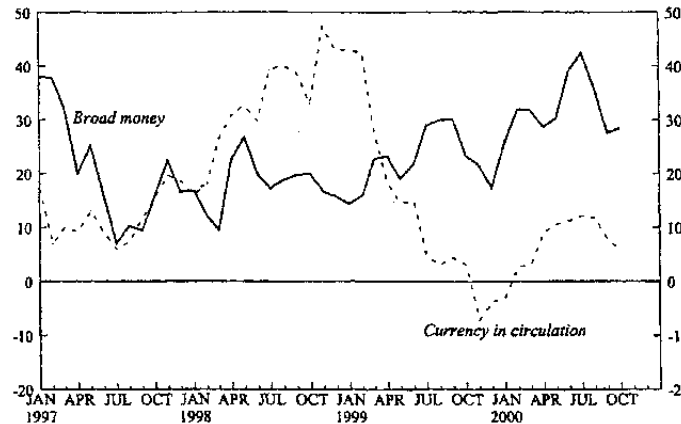
Bank Financing of the Budget
(Monthly flow, in billions of riel)



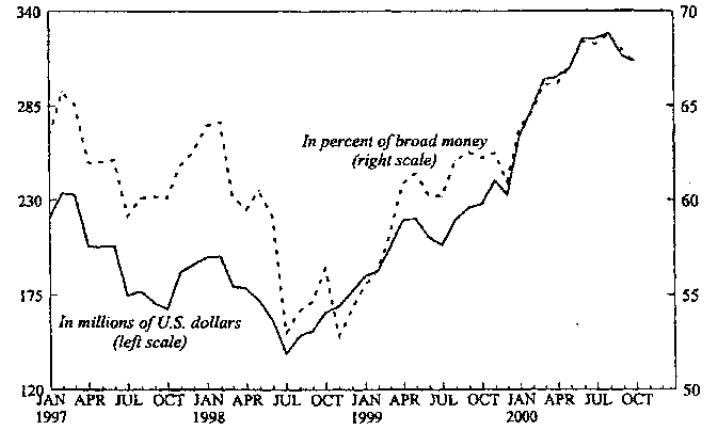
International Reserves
(In millions of U.S. dollars)



Monetary Indicators
(12-month percent change)



Foreign Currency Deposits
(End of period stock)



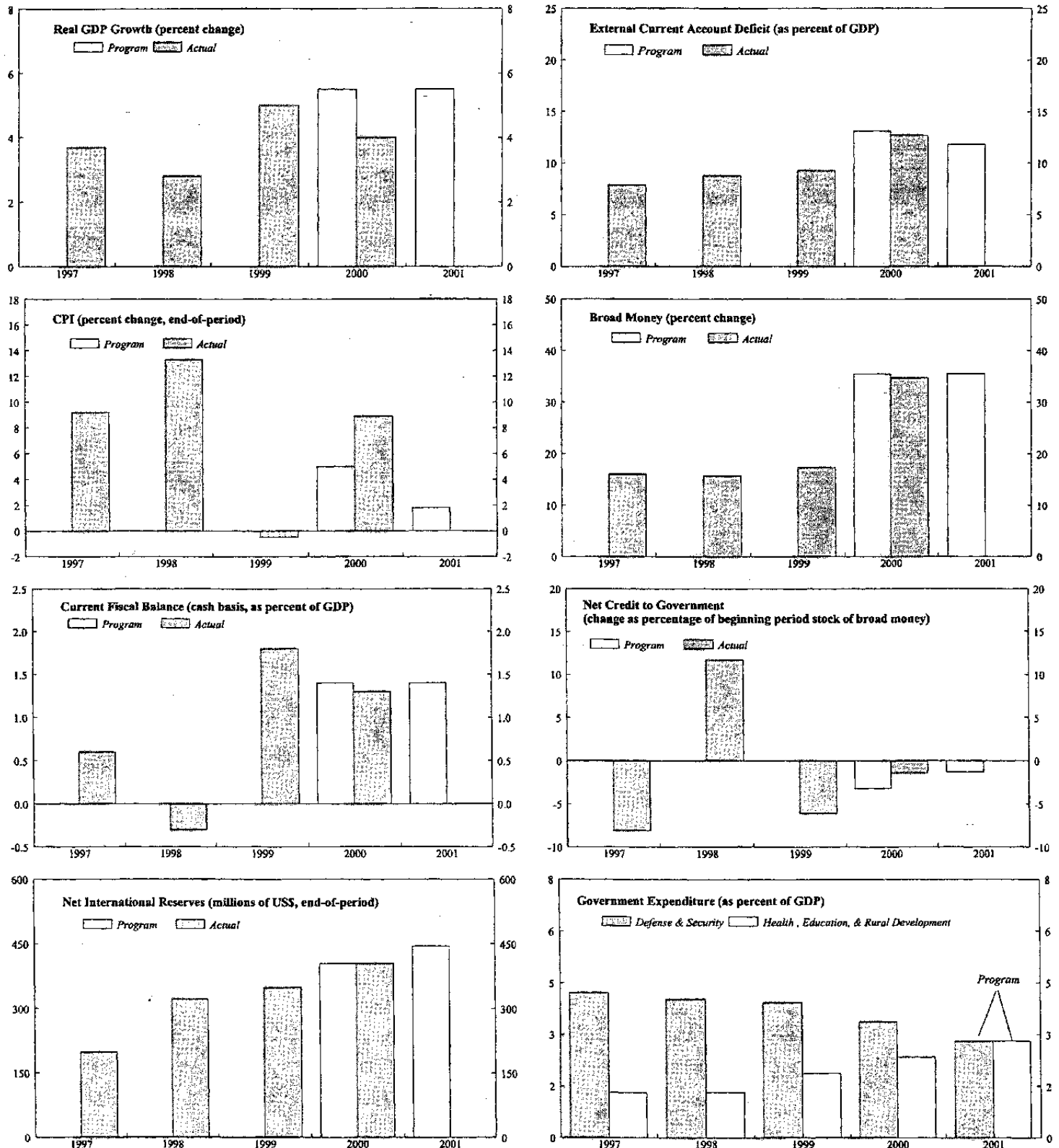
Source: Data provided by the Cambodian authorities.

// Includes US\$117 million associated with the return in 1998 of Cambodian gold previously held by the BIS.

CHART 2

CAMBODIA

INDICATORS OF PROGRAM PERFORMANCE, 1997-2001 1/

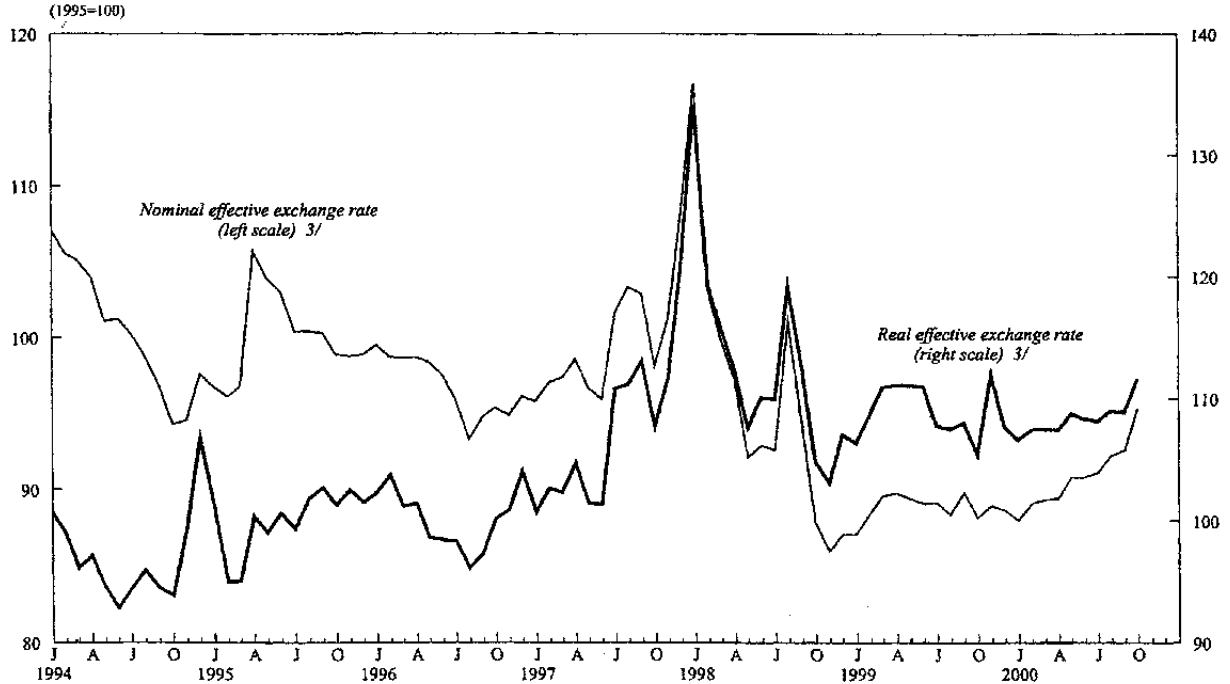
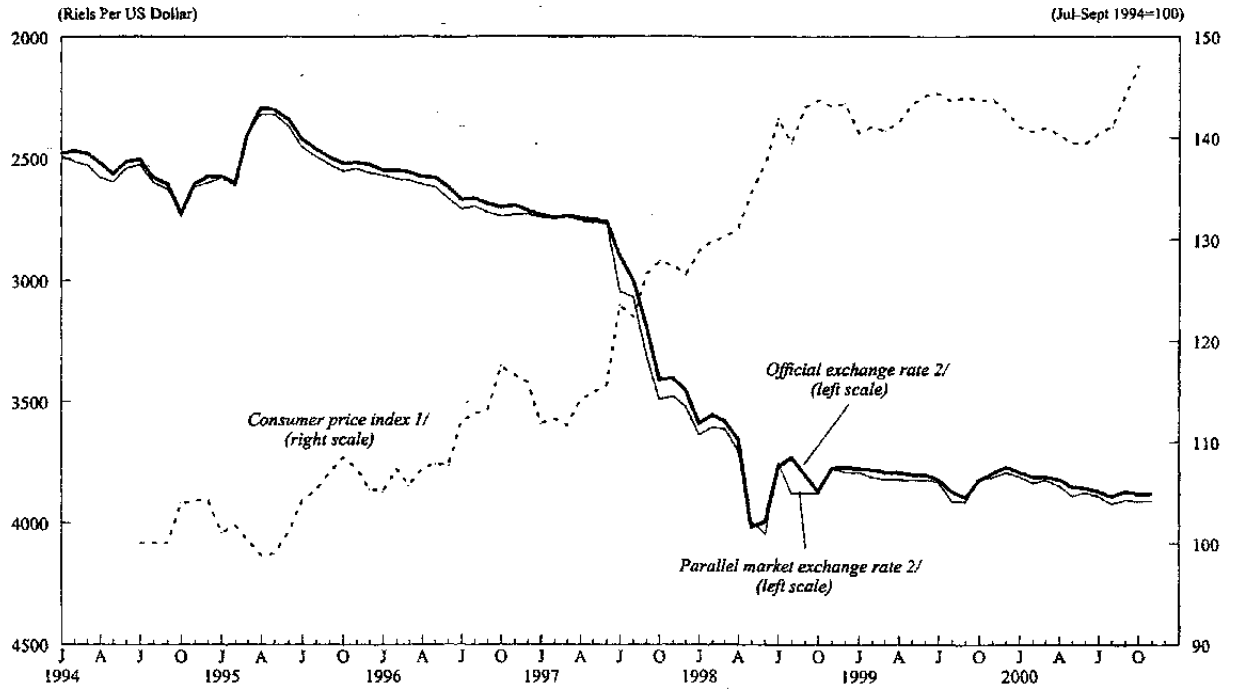


Sources: Data provided by the Cambodian authorities, and Fund staff estimates.

1/ Data for 2000 are projections.

CHART 3

CAMBODIA
CONSUMER PRICES AND EXCHANGE RATE DEVELOPMENTS, 1994-2000



Sources: Data provided by the Cambodian authorities, and Fund staff estimates.

1/ NBC consumer price index through December 1995; thereafter, NBC index based on change in CPI of National Institute of Statistics, which has been adopted as the official consumer price index.

2/ Riels per US Dollar, end-period buying rate.

3/ Based on the official exchange rate; an upward movement indicates an appreciation of the exchange rate.

Table 1. Cambodia: Selected Economic Indicators, 1997-2001

Nominal GDP (1999 est.) US\$3,008 million
 Population (1999 est.) 11.7 million
 GDP per capita (1999 est.) US\$256
 Fund Quota SDR 87.5 million

	1997	1998	1999	2000			2001 Prog.
				Orig.Prog.	Rev.Prog.	Most recent	
(Percent change; unless otherwise indicated)							
Real economy							
Real GDP	3.7	1.8	5.0	5.5	4.0	...	6.0
GDP deflator	6.0	13.1	3.8	3.2	4.0	...	5.7
Consumer prices (end-of-period)	9.2	13.3	-0.5	5.0	8.4	2.4 6/	1.8
(annual average)	8.0	14.8	4.0	2.3	0.4	...	8.9
Money and credit							
Broad money (incl. foreign currency deposits)	16.6	15.7	17.3	35.5	34.7	28.5 6/	24.0
Of which: riels in circulation	18.8	43.0	-3.8	4.1	7.8	3.4 7/	8.0
Net credit to the government 1/	-8.1	11.7	-6.1	-3.2	-1.4	-6.0 6/	-1.3
Velocity of money 2/	9.7	9.5	8.5	7.4	7.0	...	6.2
(In percent of GDP)							
Government budget							
Revenue (incl. capital revenue)	9.6	9.0	11.5	11.7	11.6	11.0 8/	12.1
Of which: tax revenue	6.5	6.5	8.3	8.8	8.6	8.1 8/	8.7
non-tax revenue	3.0	2.2	3.1	2.8	2.9	2.8 8/	3.2
Expenditure	13.8	14.9	15.9	16.3	17.3	15.2 8/	17.9
Current expenditure	8.8	8.9	9.6	10.1	10.2	8.4 8/	10.5
Capital expenditure	4.9	6.0	6.3	6.2	7.1	6.8 8/	7.4
Current budget balance	0.7	-0.3	1.8	1.4	1.3	2.6 8/	1.4
Overall budget balance	-4.1	-6.0	-4.4	-4.6	-5.7	-4.2 8/	-5.8
Overall budget balance (incl. grants)	-0.5	-2.7	-1.5	-0.6	-2.1	-0.1 8/	-2.0
Foreign financing	4.9	4.8	4.5	5.2	5.9	5.6 8/	5.9
Domestic financing	-0.7	1.1	-0.4	-0.6	-0.2	-1.0 8/	-0.2
Outstanding operation 3/	-0.1	0.1	0.3	0.0	0.0	-0.4 8/	0.0
Domestic investment	13.0	12.9	15.8	17.5	17.5 .....	...	17.8
Government investment 4/	4.8	5.7	6.2	6.0	7.1	6.8 8/	7.2
Non-government investment	8.2	7.3	9.6	11.5	10.4	...	10.6
National saving	11.7	11.1	13.8	10.7	12.4	...	12.3
Government saving	0.7	-0.3	1.8	1.4	1.3	2.6 8/	1.4
Non-government saving	11.0	11.4	12.0	9.3	11.1	...	10.9
(In millions of U.S. dollars; unless otherwise indicated)							
Balance of payments							
Exports 5/	534	604	715	608	939	...	1,002
Imports 5/	-798	-831	-989	-1,005	-1,338	...	-1,433
Current account (excluding official transfers)	-252	-246	-281	-448	-408	...	-437
(In percent of GDP)	-8.1	-8.8	-9.3	-13.1	-12.7	...	-12.4
Current account (including official transfers)	-43	-52	-61	-231	-165	...	-192
(In percent of GDP)	-1.4	-1.9	-2.0	-6.8	-5.1	...	-5.5
Capital account	-47	-53	-37	95	100	...	192
Overall balance	-90	-105	-98	-136	-65	...	0
Gross official reserves	262	390	422	486	484	490 9/	529
(In months of imports of goods and services)	2.4	3.5	3.4	3.5	3.1	3.1 10/	3.2
(In percent of broad money)	85.1	119.9	110.5	97.0	97.1	105.4 6/	97.2
Net official reserves	197	323	349	399	405	412 9/	445
External debt	2,050	2,044	2,059	1,146	2,132	...	1,339
(In percent of GDP)	66.0	72.7	68.4	35.1	66.3	...	38.1
Debt service	132	124	132	37	29	...	53
(In percent of domestic exports of goods and services)	17.8	16.1	14.5	3.9	2.4	...	4.1
Memorandum items:							
Nominal GDP (in billions of riels)	9,149	10,531	11,470	12,489	12,406	...	13,900
(in millions of U.S. dollars)	3,105	2,813	3,008	3,267	3,217	...	3,519
Exchange rate (riels per dollar, end-of-period)	3,452	3,780	3,775	3,900	3,900	3,905 11/	4,000
Terms of trade (percent change)	-4.9	12.6	11.8	-4.6	-9.7	...	3.6

Source: Data provided by the Cambodian authorities, and Fund staff estimates and projections.

1/ Contributions to 12-month percent change of broad money.

2/ Ratio of nominal GDP to average stock of broad money.

3/ Includes expenditure committed but not yet allocated to the accounts of the government agencies that execute the budget.

4/ Includes externally financed technical assistance for implementation of capital projects.

5/ Excludes re-exports.

6/ October 2000.

7/ November 2000.

8/ October 2000; annualized totals relative to projected annual GDP.

9/ November 30, 2000. Gold reserves are evaluated at end-1999 gold price.

10/ Ratio of current reserves to 2000 projected imports of goods and services.

11/ December 15, 2000.

Table 2. Cambodia: Quantitative Performance Criteria and Benchmarks, 2000

	1999	2000									
	Stock at End -Dec.	End-March 1/			End-June			End- Sept.1/			
	Actual	Prog.	Adj. Prog.	Actual	Prog.	Adj. Prog.	Actual	Prog.	Adj. Prog.	Actual	
		(Cumulative change from beginning of year)									
Net domestic assets of the banking system (in billions of riels) 2/ 3/	-576	7	44	-57	1	33	-81	-43	-25	-77	
Net credit to the government from the banking system (in billions of riels) 3/	103	-19	18	-9	-49	-17	-62	-58	-40	-97	
Net domestic financing of the budget (in billions of riels) 3/	...	-19	18	-32	-49	-17	-70	-66	-48	-111	
Contracting or guaranteeing of external debt by the public sector 4/											
Up to one-year maturity 5/	...	0	0	0	0	0	0	0	0	0	
1-5 year's maturity	...	0	0	0	0	0	0	0	0	0	
Medium- and long-term non-concessional debt 6/	...	0	0	0	0	0	0	0	0	0	
External payments arrears 7/	...	0	0	0	0	0	0	0	0	0	
		(Cumulative change from beginning of year)									
Net official international reserves (in millions of US dollars) 8/	349	13	3	25	26	17	44	43	38	62	
<i>Memorandum items:</i>											
		(Cumulative flows from beginning of year)									
Nonproject budget support (in millions of U.S. dollars)		10	...	0	20	...	11	30	...	25	
		(Stock at end of period)									
Net domestic assets of the banking system (in billions of riels)	-576	-569	-532	-634	-575	-543	-657	-619	-601	-653	
Net credit to the government from the banking system (in billions of riels)	103	84	121	94	54	86	41	45	63	6	
Net official international reserves (in millions of U.S. dollars) 8/	349	362	352	375	375	367	393	392	387	411	
		(At end of period)									
Exchange rate (riels per U.S. dollar, end of period)	3,775	3,800	3,800	3,820	3,800	3,800	3,865	3,870	3,870	3,880	

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

1/ Performance criteria (as set in EBS/00/186 Attachment).

2/ Net domestic assets are defined as broad money minus net foreign assets of the banking system, adjusted for valuation changes arising from the difference between program and actual exchange rates.

3/ For purposes of verifying compliance with the program, the ceiling for net domestic assets, net credit to the government from the banking system, and net domestic financing of the budget were adjusted upward by CR18.2 billion in September 2000 due to shortfalls in external nonproject budget support.

4/ Maturity based on original contract.

5/ Ceiling applies to amount outstanding. Excludes normal import-related credit and any borrowing associated with debt rescheduling.

6/ Excludes amounts contracted under the government loan agreement with China dated July 26, 2000 for a maximum loan amount equivalent to US\$12 million.

7/ Continuous performance criterion.

8/ For purposes of verifying compliance with the program, the floor on net official international reserves was adjusted downward by US\$4.8 million in September 2000 due to shortfalls in external non-project budget support. For program purposes, valuation Effects on the stock of gold holdings are excluded, and gold holdings will be evaluated at the end-December 1999 gold price.

Table 3. Cambodia: Key Structural Policy Actions for 1999-2000

Policy Action	Status
<p>I. Structural Performance Criteria</p> <ol style="list-style-type: none"> 1. Complete census to ascertain the precise number and status of civil servants and military personnel by end-March 2000 2. Complete evaluation of all commercial banks that reapplied for a banking license by end-November 2000. 	<p>Military census was completed in December 1999 and the civil service census in March 2000.</p> <p>Evaluations were completed and decisions made in November 2000. Public announcement was made in early December.</p>
<p>II. Other key structural policies</p> <ol style="list-style-type: none"> 1. Financial Sector Development <ol style="list-style-type: none"> a. Adoption of a new Financial Institutions Law.¹ b. Complete on-site inspections of commercial banks by end-December 1999.² c. Following adoption of the Financial Institutions Law, subject all banks to relicensing and begin process of liquidating nonviable banks by end-June 2000.² d. Provide initial recapitalization of the Foreign Trade Bank (FTB) and issue a commercial banking license to the FTB by end-November 2000.² 	<p>The law was approved by the National Assembly in October 1999.</p> <p>Completed in December 1999</p> <p>The relicensing process started as envisaged, and the first 3 banks were liquidated in August 2000.</p> <p>Implemented in November 2000.</p>
<ol style="list-style-type: none"> 2. Tax Administration <ol style="list-style-type: none"> a. Implement 1997 Law on Taxation. b. Maintain higher timber royalties consistent with the 1999 Budget Law. c. Launch an open tender for a service provider for preshipment inspection (PSI) of imports and initiate PSI services.¹ d. Unify import duty rates for cigarettes.¹ e. No ad hoc tax exemptions to be granted any time during the program period.¹ f. Complete review of timber revenue mechanism, in consultation with the Bank and the Fund.¹ 	<p>VAT was introduced in January 1999.</p> <p>Implemented.</p> <p>A new contract for PSI was signed in August 2000.</p> <p>Duty rates were unified in September 1999.</p> <p>Remaining exemptions are limited to those specified under the Law on Investment and a few duty-free shops in border regions.</p> <p>Preliminary studies were carried out by the government and the World Bank. A consultant has been hired to present an independent study which will be completed by March 2001.</p>

¹ Condition for review or prior action.

² Structural benchmark.

Policy Action	Status
<p>3. Forestry and Public Resource Management</p> <p>a. Continue ban on log exports, stop granting new concessions, and cancel all permits for log collection.</p> <p>b. Submission of revised subdecree on forestry concession management (in consultation with the World Bank) to the Council of Ministers.¹</p> <p>c. Establish a Forest Crime Monitoring Unit (FCMU) and publish quarterly monitoring reports.¹</p> <p>d. Complete review of concession contracts and cancel additional concessions in violation of contract terms or Cambodian law by end-June 2000.³</p> <p>e. Initiate national consultations on a revised Forestry Law by June 2000 and submit the revised law to the National Assembly by December 2000.</p>	<p>Implemented in the context of January 22, 1999 declaration.</p> <p>The subdecree was submitted to the Council of Ministers in October 1999 and adopted in December 1999.</p> <p>The Unit was established in October 1999 and regular reports have been published.</p> <p>The review was completed in May 2000, 3 concessions were cancelled, and logging activity of others was restricted.</p> <p>National consultations were initiated in June 2000 and the revised law was submitted to the Council of Ministers in December 2000. The law is expected to be submitted to the National Assembly by end-February 2001.</p>
<p>4. Civil Service and Military Reform</p> <p>a. Adopt civil service policy entailing a strict limit on hiring of new workers, and a reduction in staff through eliminating "ghost" workers and normal attrition.</p> <p>b. Formulation of a medium-term strategy and reform program for the civil service and military, entailing annual phasing by end-June 2000.²</p> <p>c. Complete pilot demobilization program and launch the first phase of military demobilization by end-2000, involving 10,000 soldiers.¹</p>	<p>Ghost workers are being eliminated during the process of establishing a computerized payroll. New hiring has been limited to teachers and medical graduates.</p> <p>Specification of a reform strategy will be made by end-March 2001, based on ongoing studies and technical assistance from the World Bank, UNDP, and AsDB.</p> <p>Discharge under the pilot program was completed, but the first phase of the full program has been postponed until mid-2001 because of delays in securing donor financing.</p>
<p>5. Trade Reform</p> <p>Commitment to reduce the maximum tariff rate to 30 percent and the average tariff rate to below 15 percent within the PRGF period.</p>	<p>In the context of the 2001 budget, the maximum tariff rate was reduced to 35 percent, the number of tariff bands reduced to 4, and the average tariff rate reduced to less than 16½ percent.</p>
<p>6. Private Sector Development</p> <p>Submit two commercial laws to the National Assembly by end-December 1999.^{2/}</p>	<p>Drafts of five laws have been completed. One was submitted to the National Assembly in November 1999 and the others are being finalized in 2001.</p>

³ Originally intended as a structural performance criteria for end-June 2000, it was converted to a prior action, owing to delays in completing the first review.

Table 4. Cambodia: General Government Operations, 1997-2001

	1997	1998	1999	2000		2001	1997	1998	1999	2000			2001	
				Budget	Prog.	Rev.Proj.	Budget				Budget	Prog.	Proj.	Budget
	(In billions of riels)						(In percent of GDP)							
Total revenue	881	943	1,338	1,529	1,466	1,438	1,683	9.6	9.0	11.7	12.2	11.7	11.6	12.1
1. Tax revenue	597	679	965	1,083	1,093	1,071	1,213	6.5	6.5	8.4	8.7	8.8	8.6	8.7
Direct taxes	44	56	83	104	83	125	131	0.5	0.5	0.7	0.8	0.7	1.0	0.9
o.w. profit taxes	35	42	61	82	...	105	108	0.4	0.4	0.5	0.7	...	0.6	0.8
Indirect taxes	206	248	432	469	495	522	677	2.3	2.4	3.8	3.8	4.0	4.2	4.9
o.w. Excise taxes	74	76	92	94	106	123	248	0.8	0.7	0.8	0.8	0.8	1.0	1.8
Domestic	11	16	16	22	...	23	23	0.1	0.2	0.1	0.2	...	0.2	0.2
Import	63	60	76	72	...	101	225	0.7	0.6	0.7	0.6	...	0.8	1.6
VAT	...	...	315	359	355	384	417	...	...	2.7	2.9	2.8	3.1	3.0
Domestic	...	...	43	73	...	73	86	...	...	0.4	0.6	...	0.6	0.6
Import	...	...	286	316	...	331	331	...	...	2.5	2.5	...	2.7	2.4
Trade taxes	347	376	433	492	515	407	379	3.8	3.6	3.8	3.9	4.1	3.3	2.7
Tax revenue from provinces	...	...	17	18	...	18	26	...	...	...	0.1	...	0.1	0.2
2. Nontax revenue	271	230	360	426	348	357	445	3.0	2.2	3.1	3.4	2.8	2.9	3.2
o.w. Timber Royalties	37	23	36	52	61	40	55	0.4	0.2	0.3	0.4	0.5	0.3	0.4
Tourism income	1	1	1	4	4	10	15	0.0	0.0	0.0	0.0	0.0	0.1	0.1
Royalties (casino)	...	...	0	16	...	12	16	...	...	0.0	0.1	...	0.1	0.1
PTT	83	87	109	150	110	101	144	0.9	0.8	0.9	1.2	0.9	0.8	1.0
Quota Auction	...	...	87	10	10	20	10	...	...	0.8	0.1	0.1	0.2	0.1
Garment licenses	...	...	21	36	22	46	50	...	...	0.2	0.3	0.2	0.4	0.4
Revenue from Provinces	...	...	6	6	...	6	6	...	...	0.0	0.0	...	0.0	0.0
3. Capital revenue	12	33	14	20	25	10	25	0.1	0.3	0.1	0.2	0.2	0.1	0.2
Total expenditure 1/	1,258	1,571	1,848	2,359	2,037	2,150	2,483	13.7	14.9	16.1	18.9	16.3	17.3	17.9
1. Current expenditure	806	941	1,120	1,339	1,267	1,265	1,458	8.8	8.9	9.8	10.7	10.1	10.2	10.5
Wages 2/	382	451	525	527	535	507	557	4.2	4.3	4.6	4.2	4.3	4.1	4.0
Civil administration	132	154	194	218	220	212	238	1.4	1.5	1.7	1.7	1.8	1.7	1.7
Defense and security	250	297	331	309	315	294	319	2.7	2.8	2.9	2.5	2.5	2.4	2.3
Nonwage	424	490	572	788	732	735	869	4.6	4.7	5.0	6.3	5.9	5.9	6.2
Operating expenditures	322	372	410	505	501	489	576	3.5	3.5	3.6	4.0	4.0	3.9	4.1
Civil administration	164	220	276	376	370	366	476	1.8	2.1	2.4	3.0	3.0	3.0	3.4
Defense and security	158	152	134	129	131	123	100	1.7	1.4	1.2	1.0	1.0	1.0	0.7
Economic transfers	7	14	12	46	17	17	38	0.1	0.1	0.1	0.4	0.1	0.1	0.3
Social transfers	68	71	104	117	114	113	122	0.7	0.7	0.9	0.9	0.9	0.9	0.9
Interest	10	15	22	25	25	25	25	0.1	0.1	0.2	0.2	0.2	0.2	0.2
Other non-wage	18	18	21	51	50	40	43	0.2	0.2	0.2	0.4	0.4	0.3	0.3
Reserve funds(chap. 40)	0	0	2	45	25	51	64	0.0	0.0	0.0	0.4	0.2	0.4	0.5
o.w. Floods	...	...	...	0	...	39	25	...	...	...	0.0	...	0.3	0.2
Provincial budget	...	...	23	24	...	23	32	...	...	...	0.2	...	0.2	0.2
2. Capital expenditure	452	630	728	1,020	770	885	1,025	4.9	6.0	6.3	8.2	6.2	7.1	7.4
Locally financed	110	120	224	320	273	270	325	1.2	1.1	1.9	2.6	2.2	2.2	2.3
Externally financed	342	510	504	700	496	615	700	3.7	4.8	4.4	5.6	4.0	5.0	5.0
Current Balance	63	-32	204	170	174	163	200	0.7	-0.3	1.8	1.4	1.4	1.3	1.4
Overall Balance	-377	-628	-510	-830	-571	-712	-800	-4.1	-6.0	-4.4	-6.6	-4.6	-5.7	-5.8
Overall Balance (incl. grants)	-36	-286	-168	-280	-134	-259	-275	-0.4	-2.7	-1.5	-2.2	-1.1	-2.1	-2.0
Financing	379	628	509	830	571	712	800	4.1	6.0	4.4	6.6	4.6	5.7	5.8
1. Foreign financing (net)	446	505	515	843	647	732	825	4.9	4.8	4.5	6.8	5.2	5.9	5.9
Project grants	245	341	337	400	283	336	400	2.7	3.2	2.9	3.2	2.3	2.7	...
Project loans	106	163	174	300	213	279	300	1.2	1.5	1.5	2.4	1.7	2.3	...
Budget support (grant)	96	2	4	150	153	117	125	1.0	0.0	0.0	1.2	1.2	0.9	0.9
2. Domestic financing	-57	117	-45	-13	-76	-20	-25	-0.6	1.1	-0.4	-0.1	-0.6	-0.2	-0.2
o.w. Central bank financing	-75	120	-70	-13	-76	-20	-25	-0.8	1.1	-0.6	-0.1	-0.6	-0.2	-0.2
Nonbank financing	18	-4	26	0	0	0	0	0.2	0.0	0.2	0.0	0.0	0.0	0.0
3. Outstanding operations 3/	-10	6	38	0	0	0	0	-0.1	0.1	0.3	0.0	0.0	0.0	0.0
Memorandum items:														
Defense and security outlays	415	457	477	455	455	433	433	4.5	4.3	4.2	3.6	3.6	3.5	3.1
Revenue from forestry	41	25	49	52	61	40	55	0.4	0.2	0.4	0.4	0.5	0.3	0.4
Total revenue (excl. garment quotas)	881	943	1,251	1,519	1,456	1,417	1,673	9.6	9.0	10.9	12.2	11.7	11.4	12.0
Health, Education, Rural dev., Agriculture	144	165	253	338	289	338	415	1.6	1.6	2.2	2.7	2.3	2.7	3.0
Customs department revenue	486	527	796	880	...	838	935	5.3	5.0	6.9	7.0	...	6.8	6.7
Total demobilization cost 4/	...	...	...	...	...	9	58	...	...	...	...	...	0.1	0.4
o.w. government's expense 5/	...	...	...	...	...	1	9	...	...	...	...	...	0.0	0.1
GDP	9,149	10,531	11,470	12,489	12,489	12,406	13,900	...	...	...	...	...	...	...

Source: Data provided by the Cambodian authorities, and Fund staff estimates and projections.

1/ Cash basis.

2/ Includes a 10 percent base wage increase, effective January 1, 2001. The additional cost for the wage increase is estimated to amount to CR15 billion, formerly budgeted as contingency funds.

3/ Includes expenditure committed but not yet allocated to the accounts of the government agencies that execute the budget.

4/ 1,500 soldiers were discharged in 2000, and 10,000 soldiers will be discharged in 2001. A cost per soldier is US\$1,500.

5/ The government's financial contribution to the demobilization program is US\$240 of cash payment per soldier.

Table 5. Cambodia: Monetary Survey, 1999–2001

	1999	2000					2001				
	Dec.	Mar.	June	July	Aug.	Sept.	Dec. Rev. Prog.	March Prog.	June	Sept.	Dec.
(In billions of riels; end of period)											
Net foreign assets	2,019	2,373	2,510	2,463	2,489	2,448	2,534	2,651	2,765	2,859	2,935
National Bank	1,649	2,006	2,115	2,111	2,126	2,094	2,179	2,296	2,410	2,504	2,580
Deposit money banks	370	367	395	352	363	354	355	355	355	355	355
Net domestic assets	-576	-640	-679	-621	-635	-656	-591	-577	-573	-542	-526
Domestic credit	876	883	909	979	981	942	1,057	1,085	1,118	1,203	1,273
Government (net)	103	94	41	44	44	6	83	51	3	28	58
Public enterprises	10	9	8	8	7	4	9	9	9	9	9
Private sector	763	779	860	927	930	932	965	1,025	1,106	1,166	1,206
Other items (net)	-1,453	-1,523	-1,588	-1,599	-1,616	-1,598	-1,648	-1,662	-1,691	-1,744	-1,799
o.w. capital	-1,638	-1,679	-1,748	-1,745	-1,731	-1,737	...	...	...	...	...
Broad money	1,443	1,733	1,831	1,842	1,855	1,792	1,943	2,075	2,191	2,318	2,409
Narrow money	532	550	546	549	543	540	570	578	584	605	616
Currency in circulation	490	505	505	504	502	496	528	535	540	560	570
Demand deposits	42	45	41	45	40	44	42	43	44	45	46
Quasi-money	911	1,183	1,286	1,293	1,312	1,252	1,373	1,497	1,607	1,713	1,793
Time deposits	32	37	33	36	37	34	35	36	37	38	39
Foreign currency deposits	879	1,146	1,253	1,258	1,275	1,218	1,338	1,461	1,570	1,675	1,755
(12 month percent change)											
Net foreign assets	16.8	26.4	31.5	31.1	28.7	19.8	25.5	11.7	10.1	16.8	15.8
Net domestic assets	15.6	13.9	14.5	6.1	11.4	3.0	2.5	-9.9	-15.5	-17.5	-11.0
Domestic credit	4.4	3.6	13.0	20.0	14.6	8.7	20.6	22.9	23.0	27.7	20.5
Government (net)	-42.3	-43.1	-48.2	-36.8	-49.6	-93.2	-19.4	-46.0	-92.7	339.9	-30.1
Private sector	16.6	14.5	19.5	25.2	21.8	22.4	26.4	31.5	28.6	25.1	25.0
Other items (net)	8.6	7.7	13.6	14.2	13.3	6.3	13.4	9.1	6.5	9.1	9.2
Broad money	17.3	31.8	39.1	42.4	36.0	27.5	34.7	19.7	19.6	29.4	24.0
o.w. currency in circulation	-3.8	3.0	11.3	12.1	11.8	7.8	7.8	6.0	7.0	12.8	8.0
(Contribution to annual growth of broad money; in percent)											
Net foreign assets	23.6	37.7	45.7	45.1	40.8	28.8	35.7	16.0	13.9	22.9	20.7
Net domestic assets	-6.3	-5.9	-6.5	-2.8	-4.7	-1.4	-1.0	3.7	5.7	6.4	3.3
Domestic credit	3.0	2.3	7.9	12.6	9.2	5.4	12.5	11.7	11.4	14.6	11.1
Government (net)	-6.1	-5.4	-2.9	-2.0	-3.2	-6.2	-1.4	-2.5	-2.1	1.2	-1.3
Private sector	8.8	7.5	10.7	14.4	12.2	12.1	14.0	14.2	13.4	13.1	12.4
Other items (net)	-9.4	-8.3	-14.5	-15.4	-13.9	-6.7	-13.5	-8.0	-5.6	-8.1	-7.8
Memorandum items:											
Foreign currency deposits											
In millions of U.S. dollars	233	300	324	324	327	314	343	372	398	421	439
In percent of broad money	61	66	68	68	69	68	69	70	72	72	73
Credit to private sector (In millions of U.S. dollars)	202	204	222	239	238	240	247	261	280	293	302
Gross official reserves (In millions of U.S. dollars)	422	448	464	466	468	491	405	497	504	521	445
Net official reserves (In millions of U.S. dollars)	349	375	393	396	397	411	405	415	425	435	445
Average stock of liquidity	1,354	1,450	1,560	1,605	1,646	1,679	1,778	1,856	1,950	2,132	2,248
Velocity 1/	8.5	8.1	7.7	7.5	7.4	7.3	7.0	6.9	6.7	6.3	6.2
Exchange Rate (Riels per U.S. dollar; end of period)	3,775	3,820	3,865	3,880	3,900	3,880	3,900	3,925	3,950	3,975	4,000

Source: Data provided by the Cambodian authorities; and Fund staff projections.

1/ Nominal GDP divided by the average stock of broad money.

Table 6. Cambodia: Summary Accounts of the National Bank of Cambodia, 1999–2001

	1999	2000					2001				
	Dec.	March	June	July	Aug.	Sept.	Dec. Rev. Prog.	March	June	Sept. Prog.	Dec.
(In billions of riel; end of period)											
Net foreign assets	1,649	2,006	2,115	2,111	2,126	2,094	2,179	2,296	2,410	2,504	2,580
Foreign assets	1,924	2,279	2,379	2,371	2,386	2,389	2,486	2,617	2,722	2,848	2,916
Foreign liabilities	-275	-273	-264	-260	-259	-295	-307	-321	-313	-344	-336
Net Domestic Assets	-719	-794	-899	-892	-901	-933	-861	-904	-968	-959	-952
Claims on central government (net)	107	95	42	44	45	7	84	52	4	29	59
Claims on deposit money banks (net)	-77	-78	-80	-81	-82	-81	-90	-92	-94	-96	-100
o.w. restricted deposits	-76	-77	-79	-80	-81	-80	-90	-92	-94	-96	-100
Claims on public enterprises (net)	0	0	0	0	0	0	0	0	0	0	0
Claims on private sector (net)	0	0	0	0	0	0	0	0	0	0	0
Other items (net)	-749	-811	-861	-855	-864	-859	-854	-863	-877	-891	-910
o.w. capital	-870	-923	-971	-965	-972	-976	...	...	...	...	...
Reserve money	930	1,212	1,216	1,219	1,225	1,161	1,317	1,392	1,442	1,545	1,628
Currency outside banks	490	505	505	504	502	496	528	535	540	560	570
Currency in banks	20	18	28	31	28	30	32	33	34	35	36
Reserve deposits	420	690	683	685	695	635	757	824	868	950	1,022
(12 month percent change)											
Net Foreign Assets	15.7	30.5	37.0	40.0	37.7	29.0	32.1	14.5	13.9	19.6	18.4
Net Domestic Assets	15.5	26.4	29.4	26.8	28.8	21.1	19.8	13.9	7.7	2.8	10.5
Reserve Money (12 month percent change)	15.9	33.4	43.1	51.6	45.0	35.6	41.7	14.8	18.6	33.1	23.6
o.w. currency outside banks	-3.8	3.0	11.3	12.1	11.8	7.8	7.8	6.0	7.0	12.8	8.0
(Contribution to annual reserve money growth; in percent)											
Net foreign assets	27.9	51.6	67.2	74.9	68.8	54.6	57.0	23.9	24.2	35.3	30.5
Net Domestic Assets	-12.0	-18.2	-24.0	-23.4	-23.8	-19.0	-15.3	-9.1	-5.7	-2.2	-6.9
Net credit to government	-9.4	-8.2	-4.9	-3.6	-5.6	-10.6	-2.5	-3.6	-3.1	1.9	-1.9
Net claims on banks	-1.2	-0.6	-1.0	-1.0	-0.7	-0.4	-1.5	-1.2	-1.2	-1.4	-0.8
Other items (net)	-1.4	-9.4	-18.1	-18.8	-17.6	-8.0	-11.3	-4.3	-1.3	-2.7	-4.2
Memorandum items:											
Money multiplier (Broad Money / Reserve Money)	1.6	1.4	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5

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

Table 7. Cambodia: Balance of Payments, 1997–2001
(In millions of U.S. dollars)

	1997	1998	1999	2000		2001
				Prog.	Rev. Prog.	
Current account (excluding official transfers)	-246	-246	-281	-448	-408	-437
Current account (including official transfers)	-37	-52	-60	-231	-164	-192
Trade balance	-263	-227	-273	-398	-398	-431
Exports	786	867	948	913	1,140	1,207
Domestic exports	534	604	715	608	939	1,002
<i>Of which</i> : Garments	279	392	567	473	851	902
Forestry 1/	224	178	111	89	47	55
Re-exports	252	263	233	305	200	205
Imports, f.o.b.	-1,050	-1,094	-1,221	-1,311	-1,538	-1,638
Retained imports, f.o.b.	-798	-831	-988	-1,005	-1,337	-1,433
Garments sector	-195	-275	-397	-331	-587	-622
Petroleum	-91	-111	-131	-166	-271	-279
Other retained imports	-511	-445	-460	-508	-479	-532
Imports for re-export, f.o.b.	-252	-263	-233	-305	-200	-205
Services (net)	-43	-79	-77	-123	-82	-80
Receipts	205	168	195	229	251	279
<i>Of which</i> : Tourism	68	44	55	80	72	93
Payments	-248	-247	-272	-352	-332	-358
<i>Of which</i> : Interest	-17	-18	-15	-38	-28	-31
Private transfers	60	60	70	72	72	74
Official transfers	210	194	220	217	243	244
Capital account	-53	-53	-37	95	100	192
Medium- and long-term loans	-81	-69	-65	-35	-59	57
Disbursements	35	46	56	86	61	96
Amortization	-115	-115	-121	-121	-121	-39
Foreign direct investment	168	121	129	130	130	135
Short-term flows and errors and omissions	-141	-105	-102	0	29	0
Overall balance	-90	-105	-98	-136	-65	0
Financing	90	105	98	136	65	0
Change in gross official reserves	-28	-11	-32	-60	-62	-45
Use of Fund credit	0	-1	8	15	4	10
Debt rescheduling 2/	0	0	0	117	0	1,358
Change in arrears (- = reduction)	118	117	122	0	122	-1,322
Financing Gap	0	0	0	64	0	0
Memorandum items:						
Trade balance (in percent of GDP)	-8.5	-8.1	-9.1	-11.6	-12.4	-12.3
Current account balance (in percent of GDP)						
Excluding official transfers	-7.9	-8.8	-9.3	-13.1	-12.7	-12.4
Including official transfers	-1.2	-1.9	-2.0	-6.8	-5.1	-5.5
Gross official reserves 3/	262	390	422	486	484	529
In months of imports of goods and services	2.4	3.5	3.4	3.5	3.1	3.2
In months of core imports of goods and services 4/	3.7	3.9	5.9	5.5	5.4	5.7
Net international reserves	197	323	349	399	405	445

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

1/ Includes estimates for unrecorded forestry exports.

2/ Assumes the implementation of the 1995 Paris Club flow rescheduling on Naples terms (67 percent NPV reduction) and a hypothetical stock-of-debt operation in 2001. As to the debt to Russia, after an up-front discount of 70 percent is applied, pre-cutoff date debt is assumed to be subject to the stock of debt operation on Naples terms (67 percent NPV reduction), while the pre-cutoff date arrears and debt service due during 2001 is assumed to be subject to nonconsensual deferral with two year grace period, ten year repayments and the commercial interest rate. Outstanding debt and arrears to Russia are valued at the Gosbank exchange rate of US\$1 = SUR0.6, where "SUR" denotes the former Soviet Union ruble. Debt figures are based on the Cambodian authorities' records.

3/ Includes US\$117 million associated with the return of Cambodian gold holdings by the BIS in 1998.

4/ Imports excluding imports for re-export and imports for garment sector.

Table 8. Cambodia: Medium-Term Macroeconomic Framework, 1997–2005

(In percent of GDP, unless otherwise indicated)

	1997	1998	1999	2000	2001	2002	2003	2004	2005
	Projections								
Real Sector									
Real GDP (percent change)	3.7	1.8	5.0	4.0	6.0	6.0	6.0	6.0	6.5
CPI Inflation (end-period; percent change)	9.2	13.3	-0.5	8.4	1.8	3.7	3.7	3.7	3.7
GDP deflator (percent change)	6.0	13.1	3.8	4.0	5.7	3.7	3.5	3.5	2.0
Per capita GDP (in U.S. dollars)	282	249	257	270	289	308	331	356	375
National saving	11.8	11.1	13.8	12.4	12.0	12.9	12.8	13.9	14.4
o.w. Government saving	0.6	-0.3	1.8	1.3	1.4	1.4	1.2	1.2	1.2
Domestic investment	13.0	12.9	15.8	17.5	17.5	18.0	18.0	18.5	18.7
Fiscal Sector									
Revenue	9.6	9.0	11.5	11.6	12.1	13.0	13.5	13.5	13.7
o.w. tax revenue	6.5	6.5	8.3	8.6	8.7	9.7	10.2	10.3	10.5
o.w. non-tax revenue	3.0	2.2	3.1	2.9	3.2	3.2	3.1	3.1	3.1
Expenditure (cash basis)	13.8	14.9	15.9	17.3	17.9	18.3	18.4	18.3	18.2
Current	8.9	8.9	9.6	10.2	10.5	11.5	12.1	12.1	12.3
Capital	4.9	6.0	6.3	7.1	7.4	6.7	6.3	6.2	5.9
Current balance	0.6	-0.3	1.8	1.3	1.4	1.4	1.2	1.2	1.2
Overall balance	-4.2	-6.0	-4.4	-5.7	-5.8	-5.2	-4.9	-4.8	-4.6
Domestic financing	-0.5	1.1	-0.4	-0.2	-0.2	-0.1	-0.1	-0.1	-0.1
Monetary Sector									
Broad money (percent change)	16.6	15.7	17.3	34.7	24.0	20.0	20.0	20.0	16.0
Velocity (GDP/M2)	9.7	9.5	8.5	7.3	6.4	5.8	5.3	4.8	4.4
External Sector									
Domestic exports (percent change)	81.0	13.0	18.4	31.4	6.7	7.2	5.0	7.3	9.2
Retained imports (percent change)	3.5	4.2	19.0	35.3	7.2	5.6	4.5	5.3	7.7
Current account balance (excluding transfers)	-7.9	-8.8	-9.3	-12.7	-12.4	-11.7	-10.9	-10.1	-9.9
Current account balance (including transfers)	-1.2	-1.9	-2.0	-5.1	-5.5	-5.1	-5.2	-4.6	-4.3
Overall balance	-2.9	-3.7	-3.3	-2.0	0.0	0.1	-0.3	0.4	0.2
Financing gap (in millions of U.S. dollars)	...	...	...	0	0	23	40	40	40
Gross official reserves (in millions of U.S. dollars)	262	390	422	484	529	599	659	741	819
(in months of imports)	2.4	3.5	3.4	3.1	3.2	3.4	3.6	3.8	3.9
External debt 1/	66	73	68	66	38	38	38	36	35
External debt (NPV) 1/	...	62	59	57	22	22	22	22	21
Debt service ratio 2/	17.8	16.1	14.5	2.4	4.1	3.9	3.9	4.4	4.8

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

1/ Figures include bilateral debt with former CMEA countries and the United States that is assumed to be rescheduled in 2001.

2/ The decline in 2000 reflects the end of a large part of the scheduled payments to the Russian Federation.

Table 9. Cambodia: Indicators of Fund Credit, 1998–2013

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
	Projections															
(In millions of SDRs)																
Outstanding Fund Credit	47.2	53.1	56.2	63.5	70.8	69.7	62.7	56.8	52.6	45.1	34.3	22.6	12.5	5.0	0.8	0.0
GRA	5.2	4.2	3.1	2.1	1.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
SAF/PRGF	42.0	49.0	53.1	61.4	69.7	69.7	62.7	56.8	52.6	45.1	34.3	22.6	12.5	5.0	0.8	0.0
PRGF loan disbursements	0.0	8.4	8.4	16.7	16.7	8.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total debt service to the Fund	1.5	2.9	5.9	10.6	10.5	10.3	7.8	6.7	5.0	8.3	11.6	12.4	10.7	8.2	4.9	1.5
Repurchases of GRA	1.0	1.0	1.0	1.0	1.0	1.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repayments of SAF/PRGF	0.0	1.4	4.2	8.4	8.4	8.4	7.0	5.9	4.2	7.5	10.9	11.7	10.0	7.5	4.2	0.8
Charges	0.5	0.4	0.6	1.1	1.0	0.9	0.8	0.8	0.8	0.8	0.7	0.7	0.7	0.7	0.7	0.7
(In percent)																
Fund credit outstanding																
In percent of total public external debt	3.1	3.5	3.5	6.3	6.4	5.9	5.0	4.4	3.9	3.1	2.2	1.4	0.7	0.3	0.0	0.0
In percent of quota	72.6	60.7	64.3	72.6	80.9	79.7	71.7	64.9	60.2	51.6	39.2	25.8	14.3	5.7	1.0	0.0
Debt service to the Fund																
In percent of total public external debt service	1.7	3.0	26.8	26.6	25.9	24.6	15.2	11.0	8.4	13.2	16.4	16.5	14.0	10.6	6.5	2.1
In percent of exports of goods and services	0.3	0.4	0.7	1.1	1.0	1.0	0.7	0.5	0.4	0.6	0.7	0.7	0.6	0.4	0.2	0.1
(In millions of SDRs; unless otherwise indicated)																
Memorandum items:																
Cambodia's quota in the Fund	65.0	87.5	87.5	87.5	87.5	87.5	87.5	87.5	87.5	87.5	87.5	87.5	87.5	87.5	87.5	87.5
Total public external debt	1,507	1,506	1,607	1,013	1,098	1,182	1,242	1,293	1,357	1,438	1,524	1,622	1,738	1,890	2,059	2,252
Total public external debt service	91	96	22	40	40	42	51	61	59	63	71	75	77	77	75	75
Total exports of goods and services	569	665	897	969	1,039	1,087	1,166	1,249	1,364	1,479	1,603	1,738	1,884	2,029	2,186	2,355
Total debt service ratio (in percent of exports of goods and services)	16.1	14.5	2.4	4.1	3.9	3.9	4.4	4.8	4.3	4.2	4.4	4.3	4.1	3.8	3.4	3.2

Source: IMF Treasurer's Department; and Fund staff estimates and projections.

Table 10. Cambodia: Proposed Schedule of Remaining Disbursements
Under the PRGF Arrangement, 2000–2002

Amount	Available Date	Conditions for Disbursement
SDR 8,357,000 (9.6 percent of quota)	December 15, 2000	Observance of the end-September 2000 quantitative performance criteria, relevant structural performance criteria, and completion of the second review.
SDR 8,357,000 (9.6 percent of quota)	June 15, 2001	Observance of the end-March 2001 quantitative performance criteria, relevant structural performance criteria, and completion of the third review.
SDR 8,357,000 (9.6 percent of quota)	December 15, 2001	Observance of the end-September 2001 quantitative performance criteria, relevant structural performance criteria, and completion of the fourth review.
SDR 8,357,000 (9.6 percent of quota)	June 15, 2002	Observance of the end-March 2002 quantitative performance criteria, relevant structural performance criteria, and completion of the fifth review.
SDR 8,358,000 (9.6 percent of quota)	December 15, 2002	Observance of the end-September 2002 quantitative performance criteria, relevant structural performance criteria, and completion of the sixth review.

Cambodia: Fund Relations

As of November 30, 2000

I. Membership Status: Joined: 12/31/1969; Article XIV

II. General Resources Account:	SDR Million	Percent Quota
Quota	87.50	100.0
Fund Holdings of Currency	90.63	103.6

III. SDR Department:	SDR Million	Percent Allocation
Net cumulative allocation	15.42	100.0
Holdings	0.27	1.7

IV. Outstanding Purchases and Loans:	SDR Million	Percent Quota
Systemic Transformation	3.13	3.6
PRGF arrangements	53.11	60.7

V. Financial Arrangements:

<u>Type</u>	<u>Approval Date</u>	<u>Expiration Date</u>	<u>Amount Approved (SDR Million)</u>	<u>Amount Drawn (SDR Million)</u>
ESAF/PRGF	10/22/1999	10/21/2002	58.50	16.71
ESAF	05/06/1994	08/31/1997	84.00	42.00

VI. Projected Obligations to Fund: (SDR Million; based on existing use of resources and present holdings of SDRs):

	Overdue	Forthcoming				
	<u>11/30/2000</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
Principal	---	--	9.4	9.4	9.4	7.0
Charges/Interest	---	<u>0.1</u>	<u>1.1</u>	<u>1.0</u>	<u>0.9</u>	<u>0.8</u>
Total	---	0.1	10.5	10.4	10.3	7.9

VII. Exchange Rate Arrangement:

Since November 8, 1992, the exchange rate of the riel has consisted of the following two rates. First, the official exchange rate, which is expressed in riels per U.S. dollar, applies to all official external transactions conducted by the government and state enterprises. Second, the market rate, which is determined freely through interactions of foreign exchange traders in the private sector, applies to all other transactions. The official exchange rate is adjusted so as to limit the spread between the official rate and the riel-U.S. dollar rate prevailing in the market. From the beginning of 1994, the spread between the official and market exchange rates was limited to no more than 2 percent on a daily basis and, from March 1994, to no

more than 1 percent on a daily basis.¹ On December 14, 2000, the official exchange rate was CR 3,905 per U.S. dollar and the private market rate CR 3,908 per U.S. dollar.

VIII. Article IV Consultation:

Cambodia is on a 12-month consultation cycle. The Executive Board concluded the last Article IV consultation on September 15, 2000 (EBS/00/186, 8/31/00).

IX. Technical Assistance:

In addition to the formulation of the Technical Cooperation Action Plan (Annex IV), the following technical assistance has been provided during the last year:

(i) An FAD mission on tax policy and customs administration took place in September 1999. A resident custom advisor was installed at the Ministry of Finance in early February 2000, but he resigned for personal reasons in early March. His replacement was installed in September 2000. A budget advisor began an initial 3-month assignment in December 2000. A tax policy and administration mission will visit Phnom Penh in February 2001 to develop a reform strategy to improve the tax system and its administration.

(ii) The principal advisor post (MAE) at the National Bank of Cambodia has been extended for another year and several missions have taken place to support the bank restructuring process.

(iii) A STA mission on balance of payments compilation visited Phnom Penh in February 2000. A GFS mission is planned for February 2001.

(iv) A LEG mission to advise on corporate insolvency legislation took place in November 2000.

X. Resident Representative:

The resident representative office was closed in October 1997, but it was re-opened at end-October 1999. Mr. de Zamaróczy is currently the Resident Representative.

¹The spread exceeded 4 percent on a few occasions in August 1998 as the authorities supported the official rate through intervention when the parallel market depreciated.

Cambodia: Relations with the World Bank Group¹

Cambodia became a member of the World Bank on July 22, 1970 but did not borrow from the Bank until 1993. Relations between Cambodia and the Bank were interrupted between 1975 and 1992. In September 1992, Cambodia decided to resume active participation in the Bank, appointing a representative on the Bank Board of Governors and designating the National Bank of Cambodia as the depository institution for Bank assets in Cambodia. In February 2000, the World Bank approved a Country Assistance Strategy for fiscal years 2000-2003, focusing on alleviation of poverty, enhancing governance, and advocating stronger partnership with other donors and nongovernmental organizations in the delivery of projects, policy advice and services. At the same time, the Bank Board also approved a Structural Adjustment Credit for US\$30 million which focuses on fiscal and governance issues. In January 1997, an office was opened in Phnom Penh, that has recently been upgraded to Resident Office, to assist in the implementation of the Bank's assistance program and facilitate communication with the government and other donors.

To date, 15 projects have been approved for Cambodia (US\$385 million). Recent projects have focused in the following areas:

- In 1996, a Disease Control and Health Development Project was approved to support rehabilitation and expansion of the public health system, with a focus on control of communicable diseases, tuberculosis, malaria and HIV/AIDS.
- In 1997, an Agricultural Productivity Improvement Project was approved, focusing on institutional development at the Ministry of Agriculture, including rehabilitation of training facilities, retraining of staff, and sponsoring pilot field activities.
- In 1998, an Urban Water Supply Project was approved to improve water facilities in both Phnom Penh and Sihanoukville.
- In 1999, four IDA projects were approved: a Social Fund II Project to finance small scale social-infrastructure projects at the local level, basically inheriting and extending the objectives from the previous Social Fund Project, a Road Rehabilitation Project to improve accesses to rural areas, a North East Rural Development Project, and an Education Quality Improvement Project.
- In 2000, a Biodiversity and Protected Areas Project, Structural Adjustment Credit and a Forest Concession Management and Control Pilot Project were approved.

Cambodia became a member of the IFC in March 1997. The IFC is expected to provide entrepreneur training and business services for small and medium enterprises under the Mekong Project Development Facility. In addition, the IFC has approved an investment in

¹Prepared by the Fund staff based on information provided by the World Bank, as of December 11, 2000.

a Cambodian power project. The IFC is also providing technical assistance to transform a Cambodian microfinance NGO into a commercial bank.

With regard to recent analytical work, the Bank prepared a Forest Policy Assessment report in June 1996 jointly with the UNDP and the FAO, a Public Expenditure Review in February 1999, and more recently a poverty assessment and strategy report, and a power sector strategy. A diagnostic study on governance and corruption was also prepared.

IDA: Commitments and Disbursements to Cambodia, 1993-2000
(In millions of U.S. dollars, as of December 11, 2000)

Project	Date of approval	Committee	Disbursed
Emergency Rehabilitation	Oct.26, 1993	62.70	64.86
Technical Assistance	Dec.6, 1994	17.00	15.78
Social Fund	Jun.8, 1995	20.00	18.42
Economic Rehabilitation Credit	Sep.28, 1995	40.00	36.91
Phnom Penh Power Rehabilitation	Sep.28, 1995	40.00	32.02
Disease Control and Health	Dec.24, 1996	30.40	15.56
Agricultural Productivity Improvement	Feb.28, 1997	27.00	4.18
Urban Water Supply	Feb. 17, 1998	30.96	9.00
Social Fund II	Mar.23, 1999	25.00	11.76
Road Rehabilitation	Mar.23,1999	45.31	0.76
North East Village	May 18, 1999	5.00	0.47
Education Quality Improvement	Aug. 31, 1999	5.00	0.81
Biodiversity and Protected Areas LIL	Feb. 8, 2000	1.90	0.11
Structural Adjustment Credit	Feb. 29, 2000	30.00	9.61
Forest Concession Management and Control LIL	Jun. 5, 2000	4.80	0.00
Total		385.07	220.25

Cambodia: Relations with the Asian Development Bank

From 1992 through October 31, 2000, the AsDB approved US\$410 million in low-interest loans from the Asian Development Fund to Cambodia to finance thirteen projects and one structural reform program. Only the first project (the US\$68 million Special Rehabilitation Assistance Project, approved in 1992) has been completed. Of the remaining project and program loans, US\$151 million is for economic infrastructure, US\$100 million for social infrastructure, and US\$91 million for agriculture.

The AsDB also designed and administered 74 technical assistance projects during this period. These were financed through US\$51 million in grants from the AsDB (US\$20 million), the Japanese Special Fund (US\$23 million), UNDP (US\$2 million), Sweden (US\$6 million), Denmark (US\$1 million), Australia (US\$1 million), and the Netherlands (US\$0.3 million).

The AsDB completed a new Country Operational Strategy in July 2000 that emphasizes poverty reduction through interventions in four areas: rural economic development, social development, governance, and improvement of the conditions for private investment. The AsDB will place particular emphasis on facilitating government leadership of sector development initiatives in water resource management, education and transportation. This will be accomplished through efforts to coordinate the activities of aid agencies, build local capacity to finance and manage development programs, and fund priority investments.

In October–November 2000, the AsDB conducted an assessment of the flood damage to prepare a proposal for loan assistance to meet Cambodia's rehabilitation requirements. The AsDB is currently preparing an Emergency Flood Rehabilitation Project, expected to amount to US\$55 million. The project will cover rehabilitation of national transport network, irrigation, education and health facilities, and rural livelihood restoration.

AsDB: Loan Commitments and Disbursements to Cambodia
(In millions of U.S. dollars)
(as of October 31, 2000)

	Loan Approvals	Contract Awards/ Commitments	Disbursements
1994	28.2	35.9	12.2
1995	45.1	28.1	35.9
1996	105.0	15.3	32.1
1997	0.0	41.5	10.7
1998	40.0	29.1	29.3
1999	88.4	17.0	26.2
2000 (through October)	36.0	110.6	41.8
Total	342.7	277.5	188.2

Cambodia: Technical Assistance and Technical Cooperation Action Plan (TCAP)

The TCAP program was formulated between April and September 2000, and the program document is expected to be finalized in January 2001. The program is primarily aimed at strengthening the government's capabilities to formulate, implement and monitor sound fiscal and monetary policies supportive of Cambodia's poverty reduction strategy, as set forth in the Interim PRSP. Actions scheduled under the TCAP are also part of a broad effort aimed at establishing an efficient governance framework and building the institutional capacity of selected key government agencies through broad training and upgraded information and management systems. The TCAP reflects concerted efforts by the IMF, the AsDB, the UNDP and several bilateral donors to achieve the above goals. Some US\$6.3 million has been earmarked under the TCAP for implementing about 50 individual technical assistance projects within a three-year time frame.

Background

In view of Cambodia's extremely limited implementation capacity, a substantial amount of technical assistance would be required to meet reform objectives. To this end, the Government of Cambodia has requested IMF assistance in designing a comprehensive program of technical assistance covering principle areas of reform related to macroeconomic policy, including fiscal reform (tax administration and policy, customs administration, and budget management), banking reform, statistics, and the legal framework. Following discussions between the government, the IMF, UNDP, and other interested multilateral and bilateral donors a comprehensive program has been prepared.

A program of technical assistance was previously provided during 1994–97 (Attachment I). Assistance provided during this period achieved notable successes, including the preparation of the 1997 Tax Law, setting up a legislative framework for the banking system, and improvements in economic statistics. This broad success was undermined, however, by a serious deterioration in governance, and the expected benefits of improved administrative capacity—for example, with respect to enhanced revenue mobilization—did not materialize. The failure to build local capacity led to some further slippage in progress in all of these areas during 1997–98.

A comprehensive review of this assistance was conducted in early 1997 and concluded that crucial factors behind the progress that was achieved were well-defined and limited goals, and strong commitment by the authorities at the highest levels (at least in the initial stages). Shortfalls from the program's original objectives largely stemmed from: (i) overly ambitious objectives in the original project; and (ii) less than full collaboration between local staff and project advisors, including with respect to training. The Cambodian government has agreed with this assessment and emphasized that the two main impediments to successful implementation of previous technical assistance were: (i) the inability of the government to coordinate external assistance; and (ii) a lack of commitment to ensure sustainability of projects through the designation of counterparts and appropriate use of trained staff.

Key Components of the TCAP

In response to this past experience, the current TCAP program has set realistic and specific objectives in the context of strong government ownership. In addition, inter-ministerial coordination of the program will be carried out by a Government Steering Committee, chaired by the Ministry of Economy and Finance, and consisting of senior officials of the National Bank of Cambodia, government agencies and departments involved in the implementation of the TCAP, as well as representatives of other concerned ministries. The program is divided into four main areas each of which is further divided into operative components (Attachment II):

1. **Fiscal Sector Reform:** To improve capacity in tax policy and administration, customs administration, and overall budget management.
2. **Banking System Reform:** To strengthen the banking system by supporting the following objectives: (i) relicensing of commercial banks; (ii) strengthening NBC supervision capacity; (iii) restructuring the Foreign Trade Bank; and (iv) reform of the payments system.
3. **Economic Statistics:** To strengthen the government's capacity to collect, compile, analyze, and disseminate broad economic statistics through reform of the statistical institutional framework.
4. **Legal Framework:** This program, as part of the overall legal reform program for Cambodia, will strengthen the government's capacity to improve the overall legal framework, a precondition for further private sector development, by contributing to the formulation and implementation of a comprehensive legal reform strategy, with specific follow-up technical assistance from the Fund in the areas of corporate insolvency and secured transactions.

Cambodia: Summary of Technical Assistance Provided by the Fund, 1994-2000

Purpose	Assistance and timing (person-months)	Funding Sources
Tax Policy and Tax Administration		
• Establish economic forecasting unit, including medium-term programming and flash reporting	24, from January 1994	IMF/UNDP
• Reform of tax administration (advisor)	24, from March 1994	IMF/UNDP
• Tax policy mission	2, September 1994	IMF
• Long-term fiscal advisor	24, from July 1995	IMF
• Inspection mission	1/2, June 1996	IMF
• Reform of tax administration	1½, January 1997	IMF
• Tax policy and customs administration	2, September 1999	IMF
• Technical Cooperation Action Plan (TCAP) mission	3¾, March-April 2000	IMF
• Customs administration (advisor)	5, February 2000	IMF
Monetary Policy and Central Bank Operations		
• Cash management and currency reform	4, from October 1994	IMF/UNDP
• Implement accounting system for the NBC	44, from November 1994	IMF/UNDP
• Develop NBC's bank inspection and supervisory capacity	32, from November 1994	IMF/UNDP
• Foreign exchange management	20, from November 1994	IMF/UNDP
• Development of research and analysis capability	24, from February 1994	IMF/AsDB/UNDP
• Reform of financial institutions legislation	6, from March 1994	IMF/AsDB/UNDP
• Assist the NBC in implementing monetary policy	12, from February 1995	IMF
• Monetary operations and banking supervision	1, May 1996	IMF
• Central bank operations	12, January 1997	IMF
• Long-term advisor	36, from January 1998	IMF
• Banking system reform	4, March and June 2000	IMF
• Banking system restructuring and central bank development	2, October 2000	IMF
Statistics		
• Establishment of reporting procedures and format for GFS	18, from April 1994	IMF/UNDP
• Development of balance of payments statistics	24, from May 1995	IMF/UNDP
• Development of monetary statistics	2, from May 1995	IMF/UNDP
• Improvement of consumer price indices	2, from June 1995	IMF
• Balance of payments compilation	1/2, December 1998	IMF
• Balance of payments compilation	1/2, February 2000	IMF
Legal Framework		
• Review of technical assistance needs	1/2, April 2000	IMF
• Bankruptcy Law	1/2, November 2000	IMF

Cambodia: Summary of the Technical Cooperation Action Plan (TCAP): 2000-02¹

Purpose	Assistance (in person-months)	Budget (in U.S.dollars)
Fiscal Reform	342.4	4,993,000
Tax policy and administration	108.3	910,000
Customs administration	125.3	922,000
Budget management	108.8	3,161,000
Banking System Reform	36.5	657,000
Central bank	30.0	540,000
Commercial banks	6.5	117,000
Economic Statistics	22.5	415,000
Legal Reform	2.0	36,000
Program Administration	52.0	226,000
Total TCAP	455.4	6,327,000
Of which:		
IMF		1,242,000
AsDB		1,625,000
UNDP and others		3,460,000

¹Status as of end-November 2000.

Cambodia—Statistical Issues

At the start of Cambodia's reform program in 1993, the statistical base was largely nonexistent. Substantial improvements have been made since then, and an *IFS* page for Cambodia was published in April 1996. Nevertheless, significant problems remain, even though a considerable amount of technical assistance has been provided by the Fund, the UNDP, the AsDB, and the World Bank. Core data are generally provided on a timely basis (Attachment I).

National accounts

The National Institute of Statistics (NIS) of the Ministry of Planning provides official estimates of the components of GDP. The available statistical base on which the national accounts are estimated is extremely weak and fragmentary, and data for most sectors are not collected on a systematic basis. GDP deflators are estimated mainly from CPI data, as most other price data are not available. For several years, the AsDB has been providing technical assistance and financial support to improve the quality of the national accounts. Surveys of the main economic sectors need to be strengthened, and significant improvement of the national accounts database will take a number of years. The latest edition of the national accounts shows revised estimates for 1993–1999.

Prices

The NIS provides official estimates of the CPI on a monthly basis with a lag of five weeks. In 1995, an STA mission made recommendations to improve the reliability of the statistics, and since then significant improvements have been made. However, problems relating to price collection procedures and the compilation of CPI remain, and the index covers only Phnom Penh. The NIS is currently revising the weights of the CPI basket to reflect upgraded patterns of household consumption and broadening the coverage to include five major provincial cities. No producer or wholesale price indices are available yet.

Government finance statistics

The MEF provides monthly fiscal data on a timely basis with a four-week lag. The quality of fiscal data, compiled on the basis of GFS methodology, has improved during the last three years, owing to substantial technical assistance mostly financed by the World Bank. However, the authorities have not yet provided any data for publication in *IFS* and the *GFS Yearbook*. There are still weaknesses as regards the coverage and the economic classification of expenditure. Information on external financing of the budget has improved significantly, but detailed donor-specific data on investments financed by project aid are available only with considerable lags. The authorities are committed to provide fiscal data for *IFS* and the *GFS Yearbook* by end-2001. To assist the authorities, an STA mission on government finance statistics has been scheduled for the first quarter of 2001.

Monetary statistics

The NBC provides data on the monetary authorities and deposit money banks on a monthly basis with a lag of four weeks. Substantial improvements have been made in the past few years, particularly with the adoption of the new plan of accounts by the NBC in January 1996, and the introduction of an *IFS* page for Cambodia in April 1996. Monetary statistics in Cambodia cover riels in circulation and domestic bank deposits in riel and foreign currencies. However, data on the large amount of foreign currency in circulation in Cambodia are not available. As a result, the effective money stock in Cambodia is underestimated by the amount of foreign currency in circulation, which leads to overestimates of the income velocity of money.

Mr. Khay Phousnith, Director of the Economic Research Department of the NBC, is currently on secondment to STA as a Special Appointee.

External sector statistics

The NBC provides official estimates of balance of payments statistics. While a significant improvement has been made in compiling the statistics, aided in large part by a previous long-term advisor, weaknesses remain in several areas. Customs data have substantial coverage and valuation problems arising from the nonrecording of nondutiable imports and the weakness of customs controls. In addition, the bulk of reexports to neighboring countries are included under customs' import data but may be under-reported in total exports. Estimates of the trade balance are therefore subject to considerable uncertainty. While efforts have been made to compile better data on foreign direct investment, private capital flows are likely to be large and not fully captured by official data. A range of international transactions by enterprises, such as payments for imported services, income payments, and portfolio investment abroad are not included in the data.

An STA mission which visited Phnom Penh in February 2000 made recommendations to address these issues. The mission worked out an arrangement for a stronger collaboration between the NBC and the Customs Department to ensure a timely submission of foreign trade statistics, but lack of expertise and logistical difficulties have hampered implementation of direct investment surveys. A follow-up STA mission on balance of payment statistics has been scheduled for the first quarter of 2001, which will focus on foreign direct investment.

Cambodia: Core Statistical Indicators as of December 15, 2000

	Exchange Rates	International Reserves	Central Bank Balance Sheet	Reserve/Base Money	Broad Money	Interest Rates	Consumer Price Index	Exports/Imports	Current Account Balance	Overall Government Balance	GDP/GNP	External Public Debt/Debt Service
Date of Latest Observation	December 15 2000	November 30 2000	October 2000	December 8 2000	October 2000	October 2000	October 2000	June 2000	1999	November 2000	1999	1999
Date Received	December 15 2000	December 5 2000	December 8 2000	December 15 2000	December 8 2000	December 8 2000	December 8 2000	October 2000	April 2000	December 15 2000	April 2000	April 2000
Frequency of Data	Daily	Daily	Monthly	Weekly	Monthly	Monthly	Monthly	Monthly	Quarterly	Monthly	Annual	Annually
Frequency of Reporting	Daily	Weekly with one week lag	Monthly with five weeks lag	Weekly with one week lag	Monthly with five weeks lag	Monthly with five weeks lag	Monthly with five weeks lag	During missions	During missions	Monthly with one month lag	Annual	Annually
Source of Data	NBC	NBC	NBC	NBC	NBC	NBC	NIS	NBC and MEF	NBC	MEF	NIS	NBC
Mode of Reporting	Fax or Email	Fax or Email	Fax or Email	Fax or Email	Fax or Email	Fax or Email	Fax or Email	During missions	During missions	Fax	During missions	During missions
Confidentiality	No	Yes	No	No	No	No	No	No	No	No	No	Yes
Frequency of Publication	Daily	N/A	Monthly	Monthly	Monthly	Monthly	Monthly	Annually	Annually	Annually	Annually	N/A

Statement by the IMF Staff Representative
January 19, 2001

1. The following information has become available since the issuance of the staff report for Cambodia (EBS/01/2, 1/4/01). The information does not change the thrust of the staff appraisal.
2. Donor aid, and existing rice stocks, have so far prevented the expected increase in food prices following the severe flooding in the second half of 2000. As a result, the 12-month change in the CPI has stayed well below the program target of 5 percent; at end-December 2000 it was minus 0.8 percent. However, food prices are still expected to rise, and inflation is anticipated to increase in the near term before declining later in 2001, as envisaged in the staff report.
3. Information provided by the authorities indicates that the quantitative benchmarks for end-December 2000 for net domestic assets of the central bank and net official international reserves were observed. Preliminary data also indicate that the quantitative benchmark for net credit to the government from the banking system is also likely to have been observed by a comfortable margin.
4. The National Bank of Cambodia established on January 2, 2001 a dollar clearing and settlement system (which is a structural benchmark under the 2001 program). The formation of a working committee to prepare a recapitalization bond for the Foreign Trade Bank is expected to be completed by end-January 2001, instead of by end-December 2000 as noted in Box 5 of the staff report.

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IMF Completes Second Review of Cambodia's PRGF Arrangement and Approves in Principle US\$11 Million Credit

The Executive Board of the International Monetary Fund (IMF) today completed in principle the second review of Cambodia's performance under the program supported by a three-year, SDR 58.5 million (about US\$81.6 million) Poverty Reduction and Growth Facility (PRGF)¹ credit (see Press Release No. 99/51). The Board also approved in principle the release of a further SDR 8.36 million (about US\$11 million) from the PRGF arrangement, which would bring total disbursements under the IMF-supported program to SDR 25.1 million (about US\$33 million).

¹ On November 22, 1999, the IMF's concessional facility for low-income countries, the Enhanced Structural Adjustment Facility, was renamed the Poverty Reduction and Growth Facility, and its purposes were redefined. It is intended that PRGF-supported programs will in time be based on country-owned poverty reduction strategies adopted in a participatory process involving civil society and development partners, and articulated in a Poverty Reduction Strategy Paper (PRSP). This is intended to ensure that each PRGF-supported program is consistent with a comprehensive framework for macroeconomic, structural, and social policies to foster growth and reduce poverty. At this time for Cambodia, pending the completion of a PRSP, a preliminary framework has been set out in an interim PRSP (I-PRSP), and a participatory process is underway. It is understood that all policy understandings in the I-PRSP beyond the first year are subject to reexamination and modification in line with the strategy that is to be elaborated in the PRSP. Once completed and broadly endorsed by the Executive Boards of the IMF and World Bank, the PRSP will provide the policy framework for future review under this PRGF arrangement. PRGF loans carry an annual interest rate of 0.5 percent, and are repayable over 10 years with a 5 ½-year grace period on principal payments.

A final decision by the IMF Executive Board is pending discussion of Cambodia's interim Poverty Reduction Strategy Paper by the Executive Board of the World Bank. The World Bank Board discussion is expected to take place on January 23, 2001.

After the IMF Executive Board's discussion on Cambodia, Shigemitsu Sugisaki, Deputy Managing Director and Acting Chairman, made the following statement:

"Cambodia has made a good start in the implementation of economic reforms under its PRGF-supported program. The authorities have achieved progress in economic growth and kept inflation low despite the adverse impact of the floods in 2000. However, the reform agenda remains large, and further strong efforts are needed in the period ahead to build basic economic institutions, protect macroeconomic stability, improve governance, and make progress in reducing poverty.

"The authorities are commended for preparing a comprehensive interim PRSP, which presents a full discussion of the government's poverty reduction strategy. The interim PRSP has involved a broad range of government agencies and external partners, has set a clear agenda for a participatory process for the full PRSP, and provides a sound basis for Fund concessional assistance. The authorities, however, will need to strengthen coordination among government ministries, and with domestic and external development partners, to ensure the preparation of a high quality PRSP by end-2001.

"To build on the progress achieved so far, the program for 2001 provides a coherent framework to consolidate macroeconomic stability, deepen structural reforms, and enhance investor confidence. These are all essential for Cambodia to achieve more durable broad-based economic growth and sustained reductions in poverty.

"To attain the program objectives, it will be important for the authorities to further increase government revenue and improve expenditure composition and budget management. It will also be necessary to continue bank restructuring and deepen other structural reforms that are key to macroeconomic stability and poverty reduction—including civil service reform and military demobilization. Prudent monetary and exchange rate policies will continue to be needed, supported by the avoidance of domestic financing of the budget.

"The authorities are also urged to make good use of technical assistance that has been programmed in key areas to support macroeconomic stability and poverty reduction objectives, and to take the necessary steps to ensure that the envisaged improvements in local capacity will be made to support a sustained implementation of reforms. Continued successful implementation of the program will require close monitoring and further donor support," Mr. Sugisaki said.

**Statement by Dono Iskandar Djojosebroto, Executive Director
for Cambodia
January 19, 2001**

My Cambodian authorities would like to express their appreciation to the staff and management of the Fund for their continuous assistance and strong support in the implementation of the reform program under the Poverty Reduction and Growth Facility (PRGF) arrangement. The authorities have expressed their commitment to use the assistance received from international agencies judiciously towards building a strong base for sustainable economic growth and development in Cambodia. Their commitment has been clearly described in the Memorandum of Economic and Financial Policies and the Interim Poverty Reduction Strategy Paper (I-PRSP). The joint staff assessment and their recommendations will be very helpful in the preparation of the full PRSP.

During the first year of implementation of the PRGF, Cambodia's general performance was encouraging as reflected in the resumption of economic growth, low inflation and improvement in public finances. All quantitative and structural performance criteria under the arrangement were observed. Structural reforms were implemented broadly as programmed with notable progress in the forestry and banking sectors.

Unfortunately, Cambodia's recovery suffered a serious setback due to unusually severe flooding between July and November 2000, the worst in 70 years. The floods affected a fifth of Cambodia's population, three-fourths of its provinces and a third of total agricultural land. Hundreds of people died and thousands were displaced. Major roads and irrigation facilities were washed away and a number of schools and hospitals were damaged. Consequently, the government was confronted with the onerous task of rehabilitating the displaced people by providing them with basic necessities and restoring the damaged infrastructure. The government mobilized all available internal resources and appealed for external assistance to provide immediate relief. The amount of flood relief was estimated at US\$ 105 million. My Cambodian authorities would like to express their gratitude for the timely assistance from donor countries and institutions for immediate flood relief and rehabilitation of the economic infrastructure. With the support and assistance from the international community, in particular the IMF, my Cambodian authorities are determined to overcome these transitional challenges and continue with the structural reforms as outlined in the program.

I. Recent economic developments

Real GDP growth is estimated to slow to 4 percent in 2000, compared with the program target of 5½ percent, due to the flood. Agricultural output declined owing to damage to the rice crop. However, the garment and tourist sectors are expected to expand as

projected. Food prices have not increased as feared, owing to the availability of existing stocks and donor assistance. According to the latest data released by the National Institute of Statistics (NIS), inflation for the year 2000 was minus 0.8 percent. The current account deficit, excluding official transfers, is estimated to remain at 13 percent of GDP as projected, despite higher imports due to higher oil prices. Nonetheless, gross official reserves are expected to increase from US\$ 422 million in 1999 to US\$ 484 million, or equivalent to 3.1 months of imports of goods and services.

In the fiscal area, the government has cautiously managed the budget to prevent a significant deterioration in the fiscal balance despite the impact of the flooding and higher oil prices. The overall budget deficit is expected to rise to 5.75 percent of GDP compared with the program estimate of 4.6 percent, owing to improved implementation of donor-financed capital expenditure. The current budget surplus is estimated at 1.3 percent of GDP, close to the program target of 1.4 percent, as a result of increased spending for flood relief. Revenue collection has improved. This was partly due to the revenue enhancing measures implemented during mid-2000. The revenue from profit tax and VAT was higher than expected. Revenue from trade tax was, however, lower-than-expected owing mainly to the decline in cigarette imports. Total revenue is estimated to reach 11.6 percent of GDP, close to the program target, but expenditure on defense and security is estimated to decline in nominal terms in 2000 for the first time in more than a decade. This will allow an increased flow of budgetary resources of about ½ percentage point of GDP to the social sectors. During the last two months, actual disbursements for education and health increased significantly to offset the slow pace experienced earlier in the year.

Monetary developments have been largely influenced by the fiscal position as well as the high dollarization of the economy. Based on preliminary estimates, broad money rose by 35 percent as targeted, primarily due to an increase in foreign currency deposits. In contrast, domestic currency in circulation rose by only 8 percent, due mainly to continued fiscal restraint. Bank credit to the private sector increased by 26.4 percent, reflecting the increase in credit demand related in part to higher oil prices, as well as an increase in private sector economic activity. The exchange rate remained relatively stable throughout 2000, except for a slight weakening during the second half of 2000 as a result of the stronger U.S. dollar. The National Bank of Cambodia (NBC) has pursued a flexible exchange rate policy to keep any difference between the official and parallel market exchange rate at less than 1 percent, as agreed under the program.

II. Structural policies for 2001

In the banking sector, the government has intensified reforms to increase public confidence and mobilize savings for investment. During 2000, significant progress was made to re-license commercial banks in line with provisions of the Financial Institutions Law. The NBC closed 3 insolvent banks in July 2000 and revoked the licenses of another 8 non-viable banks in December 2000. The NBC will appoint provisional administrators to prevent asset stripping and to ensure the banks are liquidated in an orderly manner. Fourteen potentially viable banks will be re-licensed subject to their signing a Memorandum of Understanding (MOU) that requires the banks to raise their capital to a minimum of

CR 50 billion (about US\$ 13 million) and comply with other regulatory requirements. The implementation of the MOUs will be closely monitored by the Bank Supervision Department. Four banks have been issued new licenses. To avoid any negative impact, the NBC has been in dialogue with lawmakers and government officials to help them better understand the ongoing re-licensing process. The measure is gaining support from the public.

Considerable efforts have been undertaken to prepare for the privatization of the Foreign Trade Bank of Cambodia (FTB). After the privatization of the FTB, the NBC will no longer be involved in the management of FTB, thus enabling the NBC to focus solely on its central banking responsibilities. A separate board of directors has been appointed to restructure the FTB, which will be re-capitalized and placed on the same footing as other commercial banks. The NBC has injected initial capital of CR 10 billion into FTB while the Ministry of Economy and Finance (MEF) will issue government bonds to raise FTB's capital up to the minimum statutory requirement by June 2001. Representatives from the NBC and FTB have been nominated in mid-January 2001 to a working committee to prepare for the issuance of the re-capitalization bonds, with technical assistance from the IMF. The committee is expected to start its work by end of January 2001 when its composition is completed with the appointment of members from the MEF. The FTB will upgrade its management capability and seek private shareholders. Technical assistance from the IFC will start in February 2001 with the primary objective of advising FTB on the approach and methodology to restructure and privatize the FTB. The Cambodian government is seeking further assistance from AsDB to complete the restructuring and privatization process in a timely and orderly manner.

Starting with the year 2001 program, on January 2, 2001, the NBC established the U.S. dollar clearing and settlement system to complement the existing domestic currency-clearing house. By end-June 2001 the NBC will finalize the draft Payments Law that is needed to start a modern payments system.

In the forestry sector, the government has taken firm actions against illegal logging activities. The Forestry Crime Monitoring Unit (FCMU) was established in October 1999 with participation of outside observers. National consultations with relevant stakeholders have been initiated to draft a Forestry Law. The law is expected to be submitted to the National Assembly by end-February 2001. Following the review of concession contracts in May 2000, three concessions were cancelled and other logging activities were restricted.

The government has implemented reforms to rationalize the size of the civil service and military. The civil service census was completed in March 2000, leading to the removal of 6,000 "ghost" workers and irregular cases. To facilitate the rationalization of the civil service, a computerized payroll system is being set up. This was, however, delayed as resources were diverted to the more urgent need for immediate flood relief. A strategy to rationalize the size of the civil service is targeted for completion by end-March 2001 with technical assistance from the World Bank, UNDP and AsDB.

Around 1,500 soldiers were discharged under the pilot military demobilization program. The pilot phase had provided many useful lessons to ensure better preparation for

the full demobilization program to minimize the potentially negative social impact. The government has taken firm but cautious steps to comply with the program target as well as to ensure smooth reintegration of the demobilized soldiers into the local communities. A comprehensive reform strategy will be discussed with the World Bank and other donor partners at a forthcoming workshop. The first phase of the full demobilization program of 10,000 soldiers is planned for mid-2001.

In the trade area, Cambodia has begun to reduce tariff rates in accordance with the requirements of the ASEAN Free-Trade Agreement (AFTA) and has started the process for WTO accession. The authorities have already completed the WTO questionnaires in June and December 2000, and are targeting for the completion of the accession process by 2002. In the 2001 budget, the maximum tariff rate was reduced to 35 percent, the number of tariff bands was reduced to 4, and the average tariff rate was reduced to less than 16½ percent.

III. Poverty reduction strategy

Owing to a long history of internal conflict, Cambodia is one of the poorest countries in the world, with GDP per capita estimated at only US\$ 256 in 1999. The main agenda of government policy as expressed in the Interim Poverty Reduction Strategy Paper (I-PRSP) is to pull Cambodia up from the shackles of poverty. The preparation of the I-PRSP was made with the broad participation of representatives of government bodies, legislative bodies, donor community, and non-governmental organizations. The I-PRSP presents a detailed analysis of the multi-dimensionality of poverty in Cambodia and outlines the measures to reduce the incidence of poverty by promoting opportunities, creating security, strengthening capabilities and generating empowerment. The paper has consolidated the experiences from existing policies for poverty reduction, and formulated the priority actions for the short and medium term to ensure a cohesive and consensus-based development, with equity for all Cambodians. The authorities are committed to complete the full PRSP taking into consideration the comments in the joint staff assessment paper.

IV. Medium-term framework

Under the PRGF-supported program, Cambodia has so far achieved positive results, both in the macroeconomic fields as well as in the structural areas. However, the authorities are aware that there are still many challenges and difficulties to be overcome in the years ahead. The government will take additional macroeconomic policies and measures aimed at raising real GDP growth to 6 percent, keeping inflation low at single digit, containing the current account deficit to a level consistent with available concessional financing and FDI flows, and increasing gross official reserves to an equivalent of four months of imports by the end of the three-year program.

The 2001 budget was programmed to achieve a current surplus of 1.4 percent of GDP, based on enhanced revenue collection through broadening of the tax base and strengthening customs and tax administration with technical assistance from the IMF. In addition to the expansion of the VAT base and other revenue efforts, the government will review the investment law to eliminate any tax distortions. On the expenditure side, the

budget aims to reduce spending for defense and security by ½ percentage point of GDP, and allocate the freed-up resources to the social sectors (health, education), agriculture and rural development projects. The civil service wage bill will be kept at 1.7 percent of GDP, providing room for a 10 percent increase in basic wage after the removal of irregular cases from the payroll. The overall deficit (excluding grants) is budgeted to increase slightly from 5.7 to 5.8 percent of GDP. Domestic financing will remain under tight control. The government's net debt position with the central bank will be reduced. The government will make further efforts to improve budgetary operations in order to channel more resources to the social sectors. The Budget Strategy and Enforcement Center, established in 2000, will be strengthened to improve budget execution. In addition, in 2001, an increase in budget funds, from CR 27 million to CR 68 million will be allocated to the provincial and district budget as part of the government's policy to enhance the de-concentration of the central budget under the Accelerated District Development and Priority Action program.

The success of the reform program will depend on a combination of domestic efforts and technical assistance from international organizations. The government will allocate sufficient resources to the efficient use of technical assistance under the TCAP program. In the statistics area, Cambodia has already expressed its intention to participate in the GDDS, but it will require technical assistance to further improve the quality of its statistics.

V. Conclusion

Over the first year implementation of the PRGF reform program, Cambodia has generally achieved a strong performance, despite the adverse impact of the severe flooding. For the second year of the program, the government remains fully committed to continue the reform program in order to build basic economic institutions, maintain macroeconomic stability, improve governance, promote sustainable growth and fight against poverty. Further actions will be focused on improving tax administration and expenditure management, bank restructuring, military demobilization, civil service reform, and trade liberalization. The other core priorities are to reform the forestry and legal areas. The full Poverty Reduction Strategy Paper will be completed within the targeted time frame in order to provide a clear road map to fight against poverty.

My Cambodian authorities will continue their close cooperation with the Fund and the World Bank to ensure a successful implementation of the program.

With the successful implementation of the program over its first year, my Cambodian authorities request the Board's approval of the completion of the second review under the PRGF arrangement and the release of the third disbursement.

Once again, on behalf of my Cambodian authorities, I would like to express our appreciation to the staff, management and the Board for their strong support for the reform program under the PRGF arrangement as well as for their continuous assistance to Cambodia.