July 2002
IMF Staff Country Report No. 02/156

Cambodia: Fifth Review Under the Poverty Reduction and Growth Facility and Request for Waiver of a Performance Criterion—Staff Report; News Brief on the Executive Board Discussion; and Statement by the Executive Director for Cambodia

In the context of the Fifth Review Under the Poverty Reduction and Growth Facility and Request for Waiver of a Performance Criterion, the following documents have been released and are included in this package:

- the staff report for the Fifth Review Under the Poverty Reduction and Growth Facility and Request for Waiver of a Performance Criterion, prepared by a staff team of the IMF, following discussions that ended on **May 17, 2002,** 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 July 5, 2002**. 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 News Brief summarizing the **views of the Executive Board as expressed during its July 22, 2002 discussion** of the staff report that completed the review.

- a statement by the Executive Director for Cambodia.

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

Letter of Intent sent to the IMF by the authorities of Cambodia *
Memorandum of Economic and Financial Policies by the authorities of Cambodia *
Technical Memorandum of Understanding *

*May also be included in Staff Report

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

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International Monetary Fund
Washington, D.C.

INTERNATIONAL MONETARY FUND

CAMBODIA

Fifth Review Under the Poverty Reduction and Growth Facility and Request for Waiver of a Performance Criterion

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 Departments)

Approved by Wanda Tseng and Anne McGuirk

July 5, 2002

- A staff team visited Phnom Penh during May 6–17, 2002 to conduct discussions for the fifth review under the PRGF arrangement. The staff team consisted of Messrs. Rumbaugh (Head), Doi, Marciniak, López-Mejía (all APD), and Mr. Adachi (PDR), and was assisted by Mr. Hagemann (Resident Representative). Mr. May (OED) also attended the policy meetings.

- The mission met with Prime Minister Hun Sen, Senior Minister of Economy and Finance Keat Chhon, Senior Minister of the Council of Ministers Sok An, Governor Chea Chanto of the National Bank of Cambodia, Minister of Commerce Cham Prasidh, 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 and the fourth review under the arrangement, together with the 2001 Article IV consultation and presentation of the PRSP Preparation Status Report, was concluded on February 6, 2002.

- The government has agreed to the publication of all Board documents since September 2000, and has also agreed to the publication of this Staff Report and the associated MEFP.

- This report was prepared by a staff team under the direction of Mr. Rumbaugh.

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I. EXECUTIVE SUMMARY

Cambodia's medium-term reform program supported by the PRGF is aimed at sustaining economic growth with low inflation, reducing poverty, and accelerating development. To meet these goals, the program focuses on strengthening fiscal revenues, reorienting expenditure away from defense toward the social sectors, financial sector restructuring, improving public administration, and rural and private sector development.

Performance during the first two years of the PRGF-supported program has generally been positive. Macroeconomic stability has been maintained with economic growth averaging 7 percent and low inflation. Significant structural reforms have included completion of a bank relicensing program, the initiation of comprehensive reforms in tax administration and expenditure management, and the launching of civil service reform and military demobilization. For 2002, output growth is expected to decline to 4½ percent, reflecting a sharp slowing in garment exports in the first half of the year.

Sustained growth and poverty reduction will require strengthened efforts to implement reforms underway. Improvements in governance have been central to the program, and further efforts—often in the face of entrenched interests—will be necessary to achieve program objectives. The government remains committed to the program, and to global economic integration, as evidenced by their active pursuit of WTO accession. But their commitment will be particularly tested in the run up to national elections in 2003.

The macroeconomic program for 2002 concentrates on a continued reorientation of fiscal policy. Achieving the PRGF revenue target of 12¾ percent of GDP will require implementing measures to strengthen tax and customs administration and to improve nontax revenue collection. In particular, further improvements in anti-smuggling efforts, and in collecting revenue from telecommunications, tourist services, and the use of assets leased to the private sector will be important. Continued efforts are also needed to improve cash management and the expenditure process. Full independence in the operations of the National Audit Authority will help to begin the process of improving fiscal transparency.

Other structural reforms for the remainder of 2002 focus on bank supervision, restructuring of the Foreign Trade Bank, trade reform, and public sector accounting. The World Bank is taking the lead on forestry policy, military demobilization, civil service reform, and the implementation of the governance action plan, and close collaboration in these areas will continue.

Progress has been made in establishing a participatory process for the PRSP, aimed at completing the PRSP by the October 2002 target date. Parallel work is underway on developing a poverty assessment and monitoring framework and linking trade policy to poverty reduction.

II. Introduction

1. **The political situation has remained stable**. Cambodia held its first-ever commune elections in February 2002. Although there was pre-election violence in some districts, the election results, which produced a substantial majority for the ruling Cambodia People's Party (CPP) of Prime Minister Hun Sen, were widely accepted by opposition parties and international observers. National elections are scheduled for July 2003.

2. **In concluding the 2001 Article IV consultation and the fourth PRGF review,** Executive Directors commended the authorities for the maintenance of macroeconomic stability, but stressed the need to implement the reform program with renewed energy in view of an uncertain global economic environment. Directors emphasized the importance of further improvements in tax administration and expenditure management, as well as the need to pursue reforms in the areas of bank restructuring, forestry policy, and civil service reform. Directors also encouraged the authorities to resolve outstanding external debt reschedulings with key bilateral creditors on highly concessional terms.

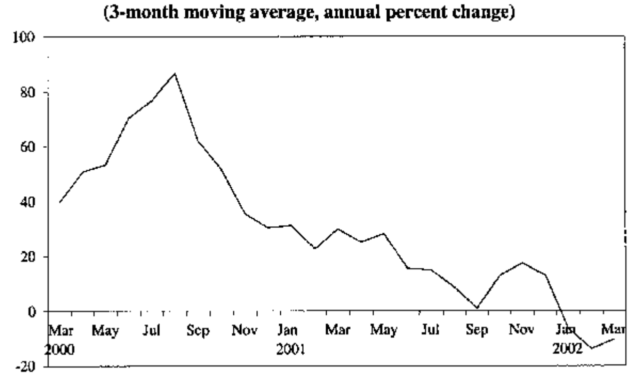
3. **At the Consultative Group meeting (June 19–21 in Phnom Penh), donors were supportive of Cambodia's ongoing efforts**, but also urged the authorities to strengthen reforms to reduce poverty and improve governance. They attached particular importance to legal and judicial reform, social sector spending, the management of natural resources, and private sector development.

4. **In the attached letter to the Managing Director**, the authorities request completion of the fifth PRGF review and a waiver for a missed structural performance criterion for end-May 2002. In support of this request, the accompanying Memorandum of Economic and Financial Policies (MEFP) reviews progress made under the third-year program, and sets out policies for the remainder of the year, including performance criteria and benchmarks for the sixth review.

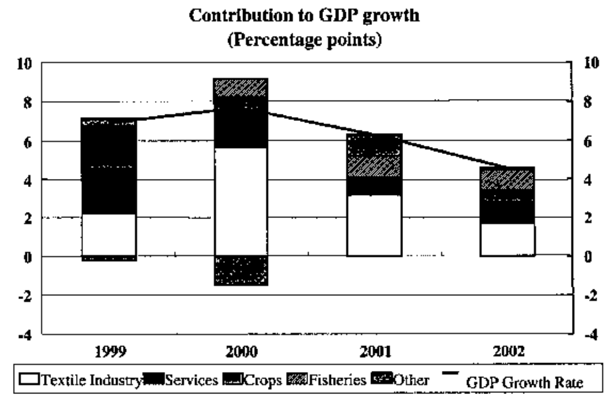
III. Recent Performance Under The 2002 Program

5. **Macroeconomic developments and policy implementation through mid-2002 were broadly consistent with the program.** Economic growth for 2001 is estimated at 6¼ percent, slightly above the program target (Table 1, and Charts 1 and 2). Garment production, the key driver of growth over the last several years, has leveled off since mid 2001 due to slower external demand (Box 1). However, growth in the tourism sector has been maintained, with arrivals increasing by 22 percent in the first quarter of 2002. Inflation was subdued at 0.7 percent for 2001, but rebounded

Garment Exports, 2000 - 02
(3-month moving average, annual percent change)



to 3.9 percent as of end-May 2002. The exchange rate has been stable and international reserves have increased, reaching $617 million (3½ months of imports) as of June 27, 2002.



6. **All quantitative benchmarks for December 2001 and quantitative performance criteria for end-March 2002 were observed** (Table 2). However, one of the two structural performance criteria for the fifth review was not observed (see Paragraph 9 below). Progress in the implementation of other structural reforms has been broadly satisfactory; most structural benchmarks were met, some with minor delays (Table 3).

7. **The implementation of the 2001 budget was consistent with the financing targets under the program, and fiscal performance to date has been broadly in line with expectations.** Revenue reached 11¾ percent of GDP in 2001 and total expenditure remained within budget limits, while the current surplus reached 1¼ percent of GDP and the overall deficit was limited to 6 percent of GDP.[1] However, spending rose sharply in December to meet budget targets, reflecting the persistence of inefficient cash management procedures and slow disbursements to line ministries at the national and provincial levels earlier in the year. The 2002 budget aims at increasing revenue to 12¾ percent of GDP, and restructuring expenditure to achieve a further increase in priority spending for the social sectors, while keeping the overall deficit (excluding grants) at 6 percent of GDP.[2] In the first four months of 2002, while higher revenue has been generated by increased taxes on petroleum products and beer, performance was largely boosted by nontax revenue from the auction of garment quotas and the annual transfer of profits from the central bank. On the expenditure side, total spending was well within budget targets, and the disbursement of funds for the social sectors was higher than in previous years, but will still need to be accelerated to meet annual targets.

[1] Fiscal performance in 2001 and the program for 2002 are described in more detail in EBS/02/13. Ratios to GDP have changed because of the revisions to the national accounts, but the underlying revenue effort is the same.

[2] Total grants amount to about 3 percent of GDP, and primarily fund development projects with a relatively small amount of general budget support in the form of commodity aid (Table 4).

Box 1. Cambodia: Revisions to the National Accounts and Sources of Growth

Revisions to the National Accounts

With assistance from the Asian Development Bank and the IMF resident statistics advisor, the National Institute of Statistics (NIS) recently released new national accounts estimates covering the period 1993–2001. The revisions led to an increase in the level of GDP by about 10 percent and higher growth rates for 1999–2000. The economic sectors that had major revisions were:

- ***Fishing:*** The revised estimates use new data from the Ministry of Agriculture, Forestry and Fisheries as well as surveys conducted by the Mekong River Commission. In constant prices, fisheries now represent 16.9 percent of GDP over 1993–2000, compared to 9.6 percent of GDP in the old series.
- ***Tourism:*** Using new methodology developed by the Ministry of Tourism, value added from tourism was revised downward slightly. For example, in constant prices, hotels and restaurants now represent 3.5 percent of GDP over 1993–2000, compared to 4 percent of GDP in the old series.

Sources of Growth

- **During 1999–2001:** the garment sector was the main engine of growth accounting for 50 percent of total growth; services, mostly related to the tourist sector, explained 25 percent of total growth. Fisheries increased significantly in 2000–01, representing 14 percent of total growth in those years.
- **In 2002:** the sources of growth are expected to be more balanced than in previous years, reflecting a decline in the growth rates of the garment sector. Crop production is expected to increase following flooding experienced during 2000-01.

Medium-Term Prospects and Constraints

Over the medium term, the sources of growth will need to be diversified, as the growth in the garment and tourist sectors experienced during 1999–2001 is not expected to be maintained. Sustained growth would require giving high priority to removing the following constraints:

- **Inadequate infrastructure**, primarily the lack of and poor quality of roads, hampers market access and results in high transportation costs. Deficiencies in port management and electricity and water shortages are also major impediments to growth.
- **Agricultural productivity**, especially for rice, is lower than in neighboring countries with similar soil conditions. Agricultural output could be raised markedly in the medium term without costly investments.
- **The lack of a modern legal and judicial system** is a serious deficiency that hampers the implementation of the governance reform and anti-corruption agenda.
- **Access to financial services** remains poor, especially in rural areas, and intermediation costs are high.
- **High trade facilitation costs** are a significant barrier to trade-driven growth, as highlighted in the pilot study on the Integrated Framework for trade.

Downside Risks to Growth

Cambodia's medium-term vulnerability is derived from external and domestic risks. External shocks could stem primarily from: (i) higher oil prices; and (ii) a lengthier and deeper global slowdown that would further affect garment exports and tourism receipts. Domestic risks are related to the potential for natural disasters (e.g., widespread flooding or drought) and further political and social unrest despite recent progress toward democratization.

8. **Monetary and external developments have also been broadly in line with the program.** Broad money growth for 2001 was 20½ percent, slightly lower than expected, due to a slowing of private sector credit growth, which partly reflects the ongoing bank restructuring process. During the first four months of 2002, the increase in broad money has been larger than programmed, reflecting higher net foreign assets (Tables 5 and 6). While growth in private sector credit continued to be modest, it is expected to regain momentum as the bank relicensing process has been completed and economic activity is expected to increase in the latter half of the year. The current account deficit for 2001, reaching 9½ percent of GDP (2 percent of GDP including official transfers) (Table 7), was smaller than originally programmed, reflecting buoyant exports in the first three quarters of 2001. Gross international reserves increased to $617 million (about 3½ months of imports) as of June 27, 2002, higher than program projections, as the authorities were able to take advantage of an increased demand for local currency to boost international reserves. The exchange rate has remained stable against the U.S. dollar, appreciating slightly in nominal and real effective terms.

9. **Progress in structural reform has been broadly satisfactory, although there have been delays in some areas.** The structural performance criterion (SPC) relating to the closing and consolidation of government accounts was observed. The SPC relating to completing an unqualified audit of the government-owned Foreign Trade Bank by end-May was not observed for technical reasons. An external audit was completed in early May and, according to the auditor, accurately reflected the bank's financial position. However, the audit was qualified because of the provisions made in 2001 for losses that could have been recorded in earlier years. These provisions would not affect future audits and an unqualified audit of the March 2002 accounts was completed on June 19. On this basis, the authorities have requested a waiver for the missed performance criterion. Other structural reforms have proceeded largely as envisaged, albeit with some delays (Table 3 and Box 2).

IV. Policy Discussions For The Remainder Of 2002

A. Short-Term Outlook

10. **Growth is expected to pick up in the second half of the year**. While the authorities expect a rebound in garment exports, the very high growth rates experienced in 2000–01 are not likely to be repeated. The recent performance of the garment industry appears to be related to a decline in external demand, as well as the impact of quota and tariff restrictions to major export markets, rather than a decline in competitiveness (see Annex I). The tourism sector is expected to continue to grow, and value added in the agriculture sector, which still accounts for some 37 percent of GDP, is projected to increase by about 3 percent. While the government is projecting GDP growth of 5½ percent for 2002, staff estimates that 4½ percent is more realistic, given the substantial slowing in the garment sector. Inflation is expected to remain below 5 percent.

Box 2. Cambodia: Structural Conditionality

Coverage of Structural Conditionality for 2002

The structural conditions for 2002 were originally set out in EBS/02/13 and the December 26, 2001 MEFP. These conditions focused on completing the bank restructuring program, reforming the Foreign Trade Bank (FTB), payments system development, improving tax and customs administration, trade reform, and public sector accounting and expenditure management. Reforms in these areas lie in the Fund's areas of expertise, and are viewed as essential for supporting financial stability and enhancing prospects for sustained growth and poverty reduction.

The structural program for 2002 has been maintained, with progress in implementing measures for the fifth review described in Table 3, and structural conditions for the sixth review described in Table 2 of the attached June 21, 2002 MEFP. The only change in structural conditionality for the sixth review is an additional structural benchmark related to improvements in public accounting in the National Treasury.

Status of Structural Conditionality from Earlier Programs

As mentioned in earlier staff reports, progress has been made in all of the structural reform areas identified at the outset of the PRGF arrangement in October 1999, although some have experienced significant delays. In addition, new structural measures were added as the program has evolved—including in the areas of tax and customs administration, expenditure management, and public accounting. The main areas that experienced delays were the military demobilization program, civil service reform, revisions to the Law on Investment, and the privatization of the FTB. Substantial reforms to forestry policy have been implemented, but have not experienced their full effectiveness because of deficiencies in monitoring.

Reforms in all of the areas that had experienced earlier delays are now moving forward or have been completed. Revisions to the Law on Investment—a second tranche release condition for the World Bank SAC—were completed in March 2002. The discharge of 15,000 soldiers under the military demobilization program was completed in late 2001, and the discharge of the last group of 15,000 soldiers is expected in the last quarter of 2002. A civil service reform program has been framed within fiscal constraints, and is being implemented in consultation with the World Bank. The privatization of the FTB was originally envisaged for end-2001, but this was later seen to be an unrealistic target in view of the substantial financial and organizational restructuring needed in the bank.

Structural Areas Covered by the World Bank

The current World Bank SAC program, approved in February 2000, has conditionality in the areas of forestry policy, military demobilization, public expenditure management, and the investment regime. Despite delays in some areas, the Bank views overall performance as satisfactory and second tranche release is expected by September 2002.

The World Bank is also supporting military demobilization through a demobilization and reintegration project, and forestry policy through a Learning and Innovation Loan (LIL). Civil service reform and the Governance Action Plan are being addressed through an Economic and Public Sector Capacity Building project, and a Policy and Human Resource Development Grant. In support of the full PRSP, an updated Country Assistance Strategy and a Poverty Reduction Support Credit (PRSC) are expected to be in place in 2003. The World Bank also has a Legal and Judicial Reform Project and a Land Management Project. Other priority areas with active involvement of the AsDB and other donors include natural resource management, land reform, and legal and judicial reform. Public expenditure management is an overlapping area of assistance involving the Bank, AsDB, WHO, bilateral donors, and the Fund, and has required careful coordination to ensure that assistance is complimentary.

B. Medium-Term Prospects

11. **The program's medium-term objectives for growth and poverty reduction remain achievable provided that the reform agenda continues to be implemented (Table 8)**. Medium-term growth of 6 percent with low inflation is predicated on sustained development in agriculture, tourism-related services, and construction. In addition, legal, judicial and administrative reform, plus measures to facilitate trade, should encourage foreign direct investment and boost economic activity. The overall budget deficit (excluding grants) is expected to be gradually reduced to below 5 percent of GDP, and the external current account deficit would decline to about 8 percent of GDP in 2006, with international reserves reaching 4 months of import coverage.

C. Fiscal Policy

12. **The budget for 2002 aims at achieving a current surplus of 1¼ percent of GDP with both revenue and expenditure increasing in line with medium-term fiscal objectives**. The overall deficit is projected at 6 percent of GDP (3 percent of GDP including grants), roughly the same as in 2001. Recently introduced revenue measures, supplemented by ongoing efforts to broaden the tax base and strengthen customs and tax administration, will contribute to increasing revenue, in line with medium-term objectives. The budget also provides for further expenditure restructuring with military and security spending reduced and significant increases in social spending. As in previous years, expenditure will be kept within financing constraints. Accordingly, in the event of shortfalls in revenue or external financing, the domestic financing target would be met (while protecting social spending) through adjustments in locally financed development spending, with contingency and reserve funds providing additional flexibility.

13. **Ongoing efforts to improve tax and customs administration will be key in achieving the revenue target for 2002**. Staff expressed concern that revenue performance in the first four months was partly due to once-off payments of nontax revenue. The authorities noted that recent measures have had a positive impact on revenue, and reaffirmed their commitment to take other steps as outlined in the MEFP. Some initial success in improving collection of tax arrears and reducing pervasive smuggling has been achieved, but stronger efforts will be required in the months ahead. However, the application of VAT to airport departure fees—a revenue measure previously agreed for 2002—will not be implemented because it was found to be inconsistent with the exemptions granted under the service contract with a private company for the operation of the airport.

14. **Upgrading the enforcement capabilities of the Customs and Excise Department continues to be crucial**. The staff noted the initial success in anti-smuggling operations, but stressed that further efforts will be needed. Following the recent establishment of an anti-smuggling unit in Phnom Penh, similar units will be established in key border provinces in coming months and inter-agency cooperation will continue to be strengthened. The staff stressed that more work is needed to facilitate trade through increased transparency in customs procedures and more effective use of preshipment inspection (PSI). The authorities

are currently holding discussions with the PSI company with a view to extending the current contract, which expires in October 2002.

15. **Meeting revenue targets also hinges upon improved collection of nontax revenue.** Some initial progress has been made. The proportion of garment export quotas subject to auction has increased, contract terms regarding the sale of entrance tickets at the Angkor temple complex have been revised to improve revenue transfer to the government, and an assessment of the operation of the international telecommunications gateway has been conducted. In addition, the collection of revenue from the issuance of visas has been strengthened, and a preliminary inventory of state assets will be completed by end-July. The staff urged more transparency and public disclosure regarding the financial terms governing the use of state assets, particularly regarding telecommunications services and the administration of the airports. This issue is likely to become more important in the future in view of ongoing discussions regarding oil and gas exploration.

16. **Implementation of the expenditure program will continue to focus on improving cash management procedures.** In line with ongoing reforms of the National Treasury, recent steps taken include: (i) establishing a Cash Management Unit that has strengthened coordination between the treasury and budget departments; (ii) initial steps taken to centralize government deposit accounts; and (iii) improved monitoring of outstanding claims on government by the private sector, including limiting the issuance of new payment orders to projected cash availability. Further efforts to standardize government accounting procedures and methodology will continue, as agreed under the 2002 program. These reforms are crucial for alleviating cash constraints to ensure a more even pattern of expenditure for the priority social sectors. The staff welcomed the recent implementation of procurement regulations for four key ministries, but called for extending coverage of procurement procedures to include additional line ministries and goods and services. The authorities indicated that coverage would be extended over time in line with administrative capacity and improvements in overall expenditure management.

17. **The framework underlying the 2003 budget under preparation is in line with the medium-term objectives.** The key parameters are: (i) maintenance of the current surplus at about 1½ percent of GDP; (ii) limiting the overall deficit (excluding grants) to 5½ percent of GDP, consistent with available concessional financing; (iii) a further improvement of revenue to 13¼ percent of GDP; (iv) a slight increase in current expenditure to 11¾ percent of GDP, including higher provisions for debt service; and (v) further increases in social spending. For the first time, the 2003 budget will be framed in a medium-term expenditure framework under preparation with AsDB support. Moreover, in collaboration with the World Bank, the design of the expenditure plan for 2003 will take into account the findings of the World Bank Public Expenditure Review (PER) recently initiated. A new financial framework for communes with the national and provincial treasuries will be effective by 2003, and will need to be implemented cautiously so that overall expenditure control is maintained.

D. Monetary Policy and Bank Restructuring

18. **The monetary program has been revised to reflect a larger increase in net foreign assets than previously programmed.** Broad money is now targeted to increase by 22½ percent in 2002, with a continued trend decline in velocity. Although broad money growth reached 32 percent as of end-April, the accumulation of net foreign assets is projected to slow down and offset an expected pickup in the growth of private credit to 15 percent, largely financed by lower foreign currency deposits at the central bank. The staff urged the authorities to monitor credit developments closely and improve overall bank supervision. As the use of traditional monetary instruments is constrained by the highly dollarized environment, the most important priority would be to avoid bank financing of the budget, as provided for in the program. If there is a need to tighten monetary policy in the future, other options include an increase in the interest rate paid on commercial bank excess reserves at the central bank, or higher reserve requirements.

19. **Bank restructuring and payments system reform are proceeding largely as envisaged.** Following the completion of bank relicensing, efforts are being directed at improving bank supervision, and restructuring the Foreign Trade Bank (FTB). A standard chart of accounts for banks in compliance with IAS has been developed and is under discussion with the Banker's Association; full implementation is expected from January 2003. Banking supervision procedures and regulations are being strengthened with technical assistance from the Fund and AsDB. The restructuring of the FTB in preparation for future privatization is also moving forward despite the delay in securing an unqualified audit (Box 3). In view of the change in the majority shareholder from the NBC to the MEF, the mission emphasized the importance of not losing momentum in the restructuring process.

E. External Sector Policies

20. **The existing flexible exchange rate policy has served Cambodia well and is expected to be maintained in the period ahead.** The authorities reaffirmed their commitment to limit the spread between official and market rates to no more than 1 percent, and gradually move toward full unification of the foreign exchange market. They also reiterated their commitment to avoid any sustained intervention to resist downward pressure on the exchange rate.

21. **The external current account deficit is expected to weaken slightly in 2002,** largely owing to the slowing of garment exports in the first half of the year. Nevertheless, a turnaround in garment exports is anticipated in the second semester, based on a global recovery, as well as a 15 percent increase in garment quotas to the U.S. market recently granted for 2002. Continued tourism growth would help limit the current account deficit (excluding official transfers) to 9½ percent of GDP. While official transfers are projected to be largely maintained at about $268 million, the expected surplus in the capital and financial

Box 3. Cambodia: Bank Restructuring

Bank restructuring in Cambodia has three main components: (i) relicensing of privately owned banks; (ii) reforming and eventually privatizing the government-owned Foreign Trade Bank (FTB); and (iii) improving bank supervision.

The Relicensing Process

The relicensing process of privately owned commercial banks has been completed. On March 19, 2002, two banks that were operating under conditional licenses were liquidated and permanent licenses were granted to those that had taken remedial actions to be in full compliance with the Law on Banking and Financial Institutions (LBFI). On April 4, an additional bank that failed to meet the requirements of the LBFI was liquidated. During the relicensing process:

- 15 banks were closed;
- 14 banks were awarded full banking licenses in accordance with the LBFI. However, one of these banks recently downgraded its operations in Cambodia to a representative office, and the activities of another bank are expected to be voluntarily liquidated.
- Four banks were granted a license to operate as specialized banks. New licenses for specialized banks are expected to follow guidelines and regulations recently completed by the National Bank of Cambodia (NBC).

The Reform of FTB

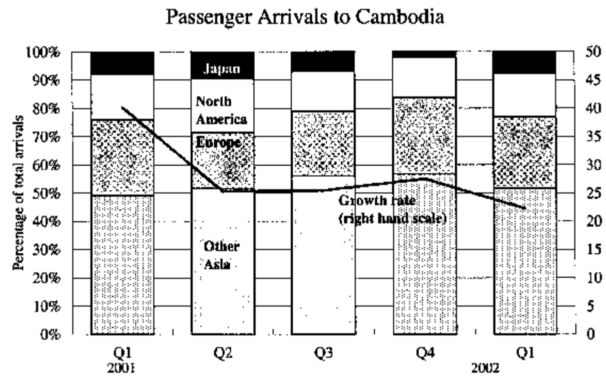
The reform of the FTB is continuing:

- According to an external audit, FTB's accounts accurately reflect the bank's financial position as of end-December 2001. However, the audit was qualified because provisions were made in 2001 for losses that could have been recorded in earlier years. This was a historical qualification that would not to be repeated in the future, and an unqualified audit of the March 2002 accounts was completed on June 19.
- In April 2002, the Ministry of Economy and Finance became the major shareholder of the FTB by issuing a recapitalization bond (CR 40 billion at an interest rate of 3 percent) that replaced bridge financing previously provided by the NBC.
- With technical assistance from Australia, a draft reorganization plan is being implemented. Under the PRGF-supported program, a public announcement to privatize the bank is expected by end-November 2002.

Improvements in Bank Supervision

With technical support from the Fund and the ADB's financial sector program, the framework for effective bank supervision is being improved. In particular:

- A new set of prudential regulations was adopted in December 2001 and new prudential regulations on lending by connected parties were adopted in June 2002. In addition, an onsite inspection unit in NBC was established in March 2002.
- Progress to modernize the payments system has continued. In this regard, the Law on Negotiable Instruments and Payments Transactions was submitted to the Council of Ministers in June 2002.
- CAMEL and prompt corrective action systems, surveillance and inspection procedures, prudential regulations on risk management and risk control, and anti-money laundering regulations are expected to be adopted by September, 2002. Moreover, implementation of a uniform chart of accounts is expected to be accelerated so that banks are using the new chart of accounts from the beginning of 2003.



Source: Ministry of Tourism and IMF estimates.

account has strengthened somewhat as projected concessional lending from the World Bank, the AsDB, and bilateral donors has been revised upward to $172 million, more than compensating for a decline in foreign direct investment. Accordingly, gross official reserves are expected to be maintained at about 3½ months of imports of goods and services, and Cambodia is expected to be able to continue servicing its obligations to the Fund in a timely manner (Tables 9 and 10).

22. **Further strides have been made in the trade reform agenda and with WTO accession.** The staff welcomed the government's intention to complete plans for the next phase of tariff restructuring to reduce the average tariff rate below 15 percent by October 2002 with implementation in 2003. A new Customs Law has also been prepared and is scheduled to be submitted to the Council of Ministers in July. The staff welcomed the further progress in meeting WTO requirements, and agreed with the authorities on the importance of accelerating work on establishing a sound legal framework, especially for key aspects of commercial legislation, as part of the WTO accession process.

23. **Additional steps have been taken toward the resolution of outstanding debt issues with the Russian Federation and the United States.** Technical discussions have taken place with a view to reconciling outstanding issues, and additional documentation from the United States was received by the government in April 2002 and is currently under review.[3] The staff assisted the authorities in technical preparations for an eventual rescheduling in the context of the Paris Club and encouraged the authorities to maintain the current momentum toward resolving these issues in the near future. The authorities reiterated their commitment to reach agreement with both creditors in 2002 but expressed concern about the potential impact of additional debt servicing on the budget and poverty reduction goals. Given Cambodia's limited revenue capacity, they stressed the need to reach rescheduled agreements on highly concessional terms.

F. Other Structural Reforms

24. **Significant steps have been taken over the last several years to reform forestry policy, but efforts need to be strengthened to establish sustainable practice.** The logging suspension announced in January 2002 is still in force, but there have been problems in

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[3] A full debt sustainability analysis is contained in EBS/02/13. Given the ongoing rescheduling discussions, the corresponding claims do not constitute arrears for program purposes.

monitoring and responding to reports of illegal activity. The staff expressed concern with reports of inadequate government cooperation with the external monitor in the Forest Crime Monitoring Unit (FCMU), and especially with an apparent failure to fully transfer royalty payments to the budget. The authorities stressed their commitment to implement a sustainable and transparent forestry policy. In this regard, several additional concessions have now been canceled, and to further control illegal logging during this transition period, all log transportation has been suspended with effect from May 23. Moreover, legal action has been initiated and financial regulations strengthened based on irregularities discovered during a recently completed internal audit of the forestry revenue system. Meanwhile, the government has started the process of evaluating management plans and environmental impact assessments with a view to complete restructuring agreements, or cancel further concessions, by September 2002.

25. **Military demobilization and civil service reform are proceeding, albeit with some delays.** The discharge of the first group of 15,000 soldiers was completed in December 2001. The authorities reiterated their commitment to proceed with the next (and final) stage by discharging an additional 15,000 soldiers in the last quarter of 2002, given that external financing for the reintegration packages is expected in the near future. With regard to civil service reform, the staff welcomed the recent implementation of a new system for remuneration and job classification, and plans to implement the Priority Mission Group scheme in the second half of 2002.[4] The size of the civil service will continue to be kept constant, with normal attrition used to offset the hiring of new teachers. Under a recent agreement between the government and the World Bank, the civil service reform process would not provide for any further retrenchment until after the national elections slated for mid-2003. In the interim, key studies would be prepared on: (i) the labor market; (ii) design of a social safety net; (iii) possible financing options, and (iv) a functional analysis. These studies would serve as a basis for designing the next steps of civil service reform after the national elections. The staff indicated that, based on these studies, more aggressive reductions in non-education personnel would provide room for larger increases in wages.

26. **Governance issues remain high on the reform agenda**. Specific governance issues are being addressed in the areas of forestry policy (see paragraph 24) and fiscal management (see paragraph 15). The staff also commended the authorities for having recently made operational the independent National Audit Authority (NAA) and welcomed the forthcoming audit on the implementation of the 2001 budget, which will be submitted to the National Assembly. The authorities reiterated their commitment to fully comply with the requirements under the IMF's safeguards assessment, by publishing NBC's 2001 audited accounts and reporting on the status of the recommendations made during the Fund's safeguards assessment in the near future. During the Consultative Group Meeting, the authorities submitted a progress report on the implementation of the Governance Action Plan (GAP),

[4] For more details on the government's civil service reform strategy see Box 4 of EBS/02/13 (1/24/02).

and stressed their commitment to continue implementing the program. Donors urged the authorities to speed up implementation, especially with respect to legal and judicial reform.

27. **Efforts are continuing to improve the statistical framework.** The staff welcomed the authorities' decision to adopt the IMF's General Data Dissemination System (GDDS) as a framework for future statistical development, and the latest improvements in national accounts and consumer price statistics. Despite this initial progress, there is a substantial need for further capacity building efforts at the NIS and line ministries. A draft law on statistics providing for increased independence of NIS will be finalized shortly, and a workplan in support of the authorities' request for continued donor support has been prepared.

G. PRSP and Social Impact of Reforms

28. **Preparations for the full PRSP are advancing steadily.** In recent months, line ministries have been better integrated into the PRSP process, with the Council for Social Development maintaining a coordinating role. A national PRSP workshop was held in May, and the draft PRSP outline and sectoral matrices prepared by key line ministries were discussed as part of a broad participatory process. In parallel, work for developing poverty assessment and monitoring frameworks, framing policy actions in a medium-term perspective, and linking trade policy to poverty reduction are all underway. The PRSP is expected to be completed by October 2002.

29. **Reforms under the program are generally believed to be conducive to poverty reduction.** A preliminary assessment of the main social impact of reforms shows a wide range of positive impacts (Box 4). A quantitative assessment is not possible in view of data limitations, but efforts are underway with donor support to strengthen poverty analysis and monitoring capabilities, and will be reflected in the forthcoming PRSP.

H. Program Monitoring

30. **The program for the remainder of 2002 will continue to be monitored through quantitative and structural performance criteria and benchmarks, as defined in Tables 1 and 2 of the MEFP**. The coverage of quantitative benchmarks and performance criteria is unchanged from the previous review. However, targets for June–December have been slightly modified to reflect upward revisions in the floor for international reserves and revised estimates of available budget financing. The scope of structural conditionality for the remainder of the year has been expanded to include one additional benchmark on the centralization of government accounts under the supervision of the national treasury. A single structural performance criterion on the issuance of the final report on government accounting procedures and methodology is provided for under the final review.

31. **Cambodia has been a recipient of wide-ranging technical assistance in support of the reform effort.** The Fund's assistance has been broad-based under the Technical Cooperation Action Plan (Box 5), especially in the fiscal area and for economic statistics.

Box 4. Cambodia: Main Social Impacts of Reform

Severe data limitations prevent the staff from conducting a quantitative Poverty and Social Impact Analysis (PSIA) at this stage. This box summarizes available information.

Impact of changes in the macroeconomic framework

Over the last three years, economic growth averaged about 7 percent annually (4½ percent in per capita terms) and inflation was contained below 3 percent. Sustained growth has created additional income and job opportunities to a wide range of the population, including the poor, and low inflation has protected their standard of living. Continued fiscal restraint in tandem with prudent monetary and exchange rate policy under the program has been instrumental in maintaining a stable economic environment. Nevertheless, despite such growth, many stakeholders feel that it has not yet contributed sufficiently to poverty reduction. Translating growth more effectively into poverty reduction will be addressed in the forthcoming PRSP.

Impact of changes in taxation

Gradual *tax system reform* has been undertaken to increase revenue while minimizing distortions for producers and consumers. The reform aims at moving from direct taxation of trade and incomes to indirect taxation relying on a value-added tax system. While a full tax incidence analysis is not feasible, the increased reliance on indirect taxation is not expected to have reduced household's aggregate disposable income, as it is largely the counterpart of a reduction in trade taxes. Moreover, while recent increases in petroleum taxes and excises on cigarettes and beer have directly affected all social groups, revenue has been increased mostly through broadening of the tax base rather than through increases in overall tax rates. The income tax thresholds are very high and the VAT base excludes most small businesses and products used by the poor. In addition, any deterioration of household incomes that result from revenue enhancing measures would need to be balanced against the increased transfers toward priority social sectors.

Impact of government expenditure allocation

Expenditure reform has affected the level and composition of government spending. As a result of the ongoing demobilization program, military and security expenditure has been curtailed from 3.8 percent of GDP in 1999 to 3.0 percent in 2001, while at the same time priority social spending (i.e., education, health, agriculture and rural development) was raised from 1.8 percent of GDP to 2.9 percent. A comprehensive social safety net is supporting the demobilization effort and preparations are underway to cushion the temporary adverse impact of the ongoing civil service reform. Plans to strengthen procurement procedures and expenditure monitoring will also improve the efficiency of public spending.

Impact of key structural reforms

Trade reform involving a gradual elimination of trade barriers is aimed at broadening Cambodia's regional integration under the AFTA arrangement and at expanding market access further through WTO accession. As a result, cheaper imported goods will be available and Cambodia's potential as a production base for exports will be enhanced. Strengthening the linkage between trade—both domestic and external—and poverty reduction was a key focus of the pilot study under the *Integrated Framework for Trade*, and is a theme being developed as part of the PRSP process.

Forestry reform, particularly efforts to establish a local community-based framework for sound forestry management could make a substantial contribution to reducing rural poverty in the future. Both governance and service delivery are also expected to be strengthened as a result of the ongoing *administrative reform* and implementation of the GAP.

Banking reform, including bank restructuring and payments system reform, has largely safeguarded small depositors during bank liquidations and established the ground for improved intermediation and savings mobilization. Further development of banking operations in rural areas would support agricultural development and poverty reduction.

Progress toward enhancing the analytical framework

The authorities are in the process of conducting a new household survey and poverty assessment. Countrywide poverty mapping should allow comparison with maps describing access to social services. A comprehensive poverty analysis and monitoring exercise sponsored by UNDP is also being conducted.

Box 5. Cambodia: Technical Cooperation Action Plan (TCAP)

The TCAP program is aimed at strengthening the government's capabilities to formulate, implement, and monitor sound fiscal and monetary policies supportive of Cambodia's poverty reduction strategy, and improving the institutional capacity of selected key government agencies through broad training and upgraded information and management systems. Some $6.3 million has been earmarked for about 50 individual technical assistance projects within a 3-year time frame.[1]

The program calls for annual reviews to assess the progress of implementation and, where needed, to adjust planned activities to reflect changed government priorities. In consultation with the government and participating donors, these changes, together with the related budget adjustments, have been reflected in a revised program document. The revisions took into account a progress report prepared by the national program management unit and inputs provided by an FAD review mission held in Phnom Penh during April 8–12. The program adjustments focus on the following areas:

- **National program management**. To strengthen management, a full-time national program manager was approved in June 2002. This will be important for coordinating the activities of several donors including the World Bank, AsDB, UNDP, WHO and bilateral donors.

- **Overall TCAP coordination**. To strengthen coordination between the team of resident technical advisors and the government, monthly steering committee meetings will be held from July 2002. These meetings will include the resident advisors, the national program management, and representatives of each government department, UNDP, IMF, and other participating donors.

- **Assistance under the budget component**. The government has requested that advisory services to modernize and strengthen budget formulation be provided on a resident basis instead of the current peripatetic arrangement. Accordingly, a budget resident advisor will be in place in July for an initial period of six months. The appointment will coincide with an FAD mission that will also review the scope of future technical assistance to the National Treasury.

- **Multisector Statistical Advisor**. The resident multisector statistical advisor currently in place was not envisaged as part of the original TCAP document. The program has been adjusted to include this component.

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[1] The original TCAP program approved in May 2001 was summarized in EBS/01/02.

Other multilateral agencies, including the World Bank, the AsDB, and the UNDP have also provided considerable support to Cambodia. The main challenge is to ensure that technical assistance support is fully complimentary and geared toward capacity building.

V. Staff Appraisal

32. **Cambodia's economy continued to perform relatively well under the third year of the PRGF-supported program, despite a decline in external demand.** Macroeconomic stability has been maintained, international reserves have increased, government revenue and social sector spending have improved, and further steps were taken across a broad range of structural reforms. Completion of the bank relicensing process, preparation of the Law on Negotiable Instruments and Payment Transactions, centralization of government accounts and improvements in cash management, steps to improve tax and customs administration, and initial pay increases as part of a comprehensive civil service reform strategy have been noteworthy accomplishments. Nevertheless, the reform process needs to be strengthened in key areas if growth is to be sustained and contribute to lasting poverty reduction.

33. **Further fiscal reform is required.** Government revenue has increased significantly under the PRGF arrangement, but still remains low compared to other countries. Overall expenditure control has been maintained despite additional election expenses in early 2002. Moreover, there has been a welcome shift in the composition of spending with a sharp decline in defense and security spending and an increase in social sector spending. However, there is a need to further improve the execution of government expenditure and overall fiscal transparency. The staff welcomes the work under way to implement a new financial framework for local governments and urges that this decentralization effort be undertaken gradually to ensure that effective control on overall spending and financial stability is maintained.

34. **Following significant tax measures in recent years, the key to further improvements in revenue performance is through better administration.** It is most critical that initial steps to improve customs administration and address pervasive smuggling be strengthened. In this regard, the recently established anti-smuggling units need to be extended to key border provinces. More generally, tax administration needs to focus on improving compliance through the large taxpayers unit, and on a systematic monitoring and collection of outstanding tax arrears. For nontax revenue, improvements have been made with respect to the auction of garment export quotas, in compiling an inventory of state assets, and in improving financial payments associated with the Ankor temple complex. However, concrete and observable institutional reforms are needed to enhance transparency of the financial terms under government contracts, to minimize revenue losses, and to ensure effective tax compliance. Given the need to improve overall transparency, a fiscal ROSC should be considered in the future.

35. **More remains to be done to improve the timeliness and efficiency of increased government expenditure for the priority social sectors.** Recent improvements in cash management have provided a useful start, and this effort should be extended to ensure timely

disbursement of funds for the priority sectors. The staff also welcomes the government decision to apply specific regulations on government procurement to four important ministries, and strongly urges that this be extended to additional ministries and goods and services in the near future.

36. **Progress on other key structural reforms also needs to be reinforced.** The staff welcomes the completion of the bank relicensing program and steps taken to restructure the Foreign Trade Bank (FTB) and secure an unqualified audit of the bank's financial position. The emphasis in the period ahead needs to be on strengthening bank supervision, and continuing to prepare the FTB for privatization. Completing the discharge of 30,000 soldiers by end-2002 will be important for freeing funds for other budget priorities. The implementation of civil service reform will also need to continue to be in line with fiscal constraints. Priority Mission Groups need to be introduced in a transparent way to improve the ability of the government to retain senior staff, and close consultation with the World Bank and other donors will continue to be important. Once a suitable safety net has been established, the staff continues to urge the government to make further reductions in non-education personnel to allow for larger wage increases and greater decompression.

37. **For forestry policy the objective is to establish a system based on sustainable management.** In this regard, the staff continues to emphasize the importance of completing the restructuring of concession agreements and to cancel further concessions that do not meet required standards by September 2002, as called for in the program. The government also needs to ensure the transfer of all royalty payments to the budget and to improve the monitoring and transparency of the forestry system. Furthermore, it will be important for the government to work closely with all stakeholders to follow community forestry practices to improve the standard of living of the rural poor.

38. **Cambodia's external position is expected to remain manageable over the medium term, provided that the reform effort is sustained.** However, the viability of the program will continue to depend on donor support and the completion of outstanding rescheduling agreements on concessional terms consistent with Cambodia's limited fiscal capacity. In this regard, the staff continues to encourage the completion of outstanding debt rescheduling agreements with the United States and the Russian Federation. The staff supports the maintenance of the flexible exchange rate policy, and efforts being made to pursue membership in the WTO. In this context, further trade reform through lower import duties and reduced tariff dispersion will continue to be important for supporting medium-term growth objectives. The staff encourages the government to include a comprehensive analysis of the linkages between trade policy and poverty reduction in developing its PRSP.

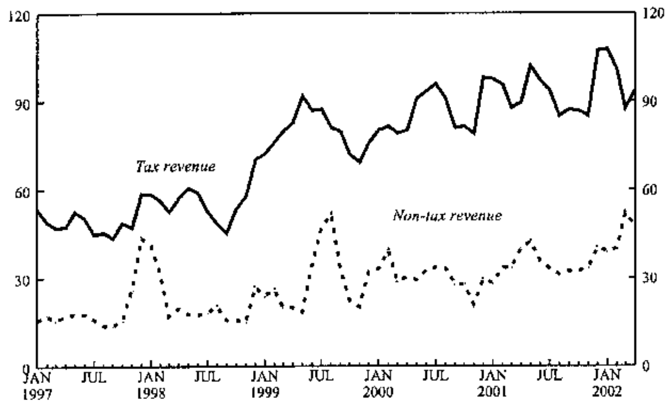
39. **The staff welcomes the recent progress that has been made in developing a full participatory process for the PRSP.** The staff urges the government to continue this effort, and to combine ongoing work with respect to the Integrated Framework for trade and the World Bank's Public Expenditure Review with the PRSP process in view of the existing timetable of completing the PRSP by end-October 2002.

40. **Effective use of technical assistance will continue to be important in all reform efforts**. The staff welcomes the recent steps taken by the government to strengthen the internal coordination of technical assistance, as well as Cambodia's participation in the GDDS system, and recent improvements made in economic statistics. There is, however, scope for further upgrading, particularly with respect to government finance and balance of payments statistics.

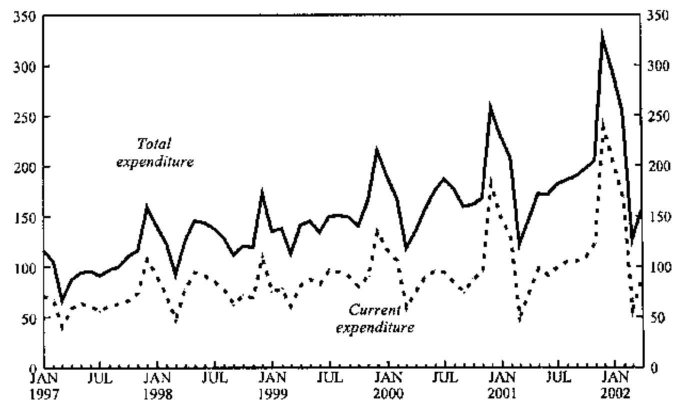
41. **Based on the authorities' record of performance under the third-year program, and the strength of their commitments for the remainder of 2002**, the staff recommends completion of the fifth review under the PRGF arrangement. The staff also supports the authorities' request for a waiver for the nonobservance of one structural performance criterion in view of the progress made in restructuring FTB, the nature of the qualification to the 2001 audit, and the completion of an unqualified audit of the March 2002 accounts. The program's vulnerability continues to reside primarily in the potential social and political uncertainty, weak governance environment, and capacity constraints. However, Cambodia's overall program performance and the authorities' strong commitment to press ahead with the reform agenda mitigate the above risks. Accordingly, the staff recommends that the Executive Board complete the fifth review under the PRGF.

Chart 1. Cambodia: Selected Economic Indicators, 1997-2002

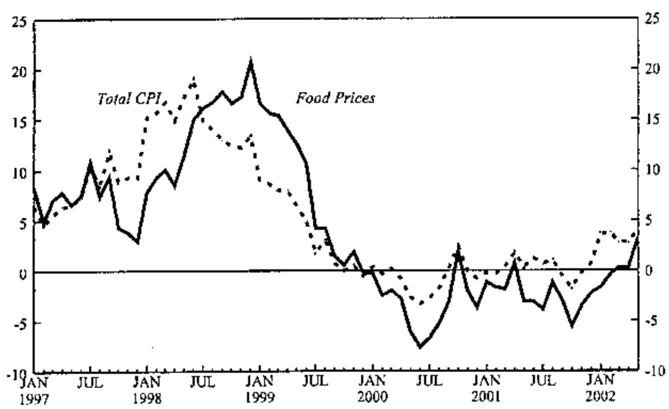
General Government Revenue
(3-month moving average, in billions of riel)



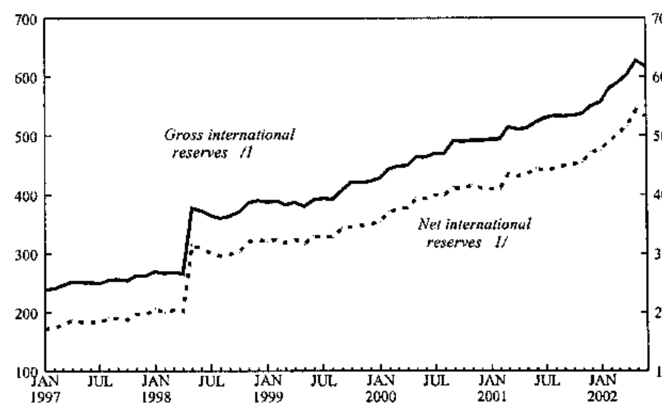
General Government Expenditure
(3-month moving average, in billions of riel)



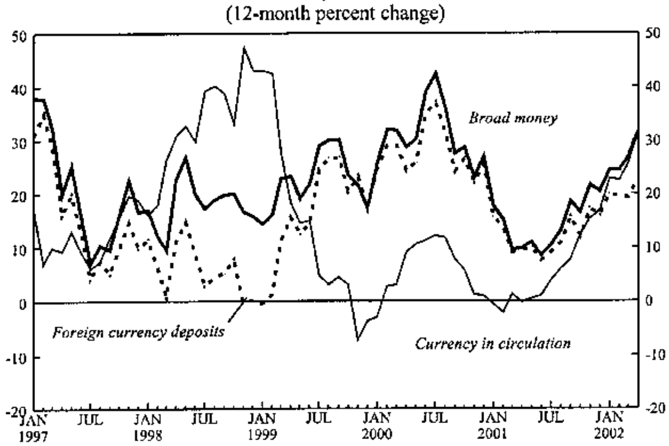
Consumer Price Index
(12-month percent change)



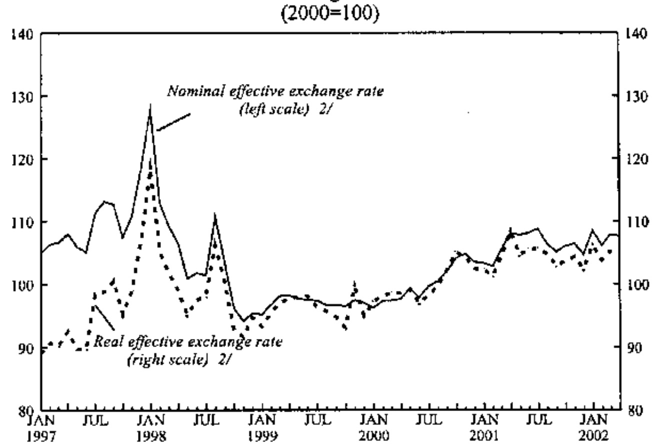
International Reserves
(In millions of U.S. dollars)



Monetary Indicators
(12-month percent change)



Exchange Rate
(2000=100)

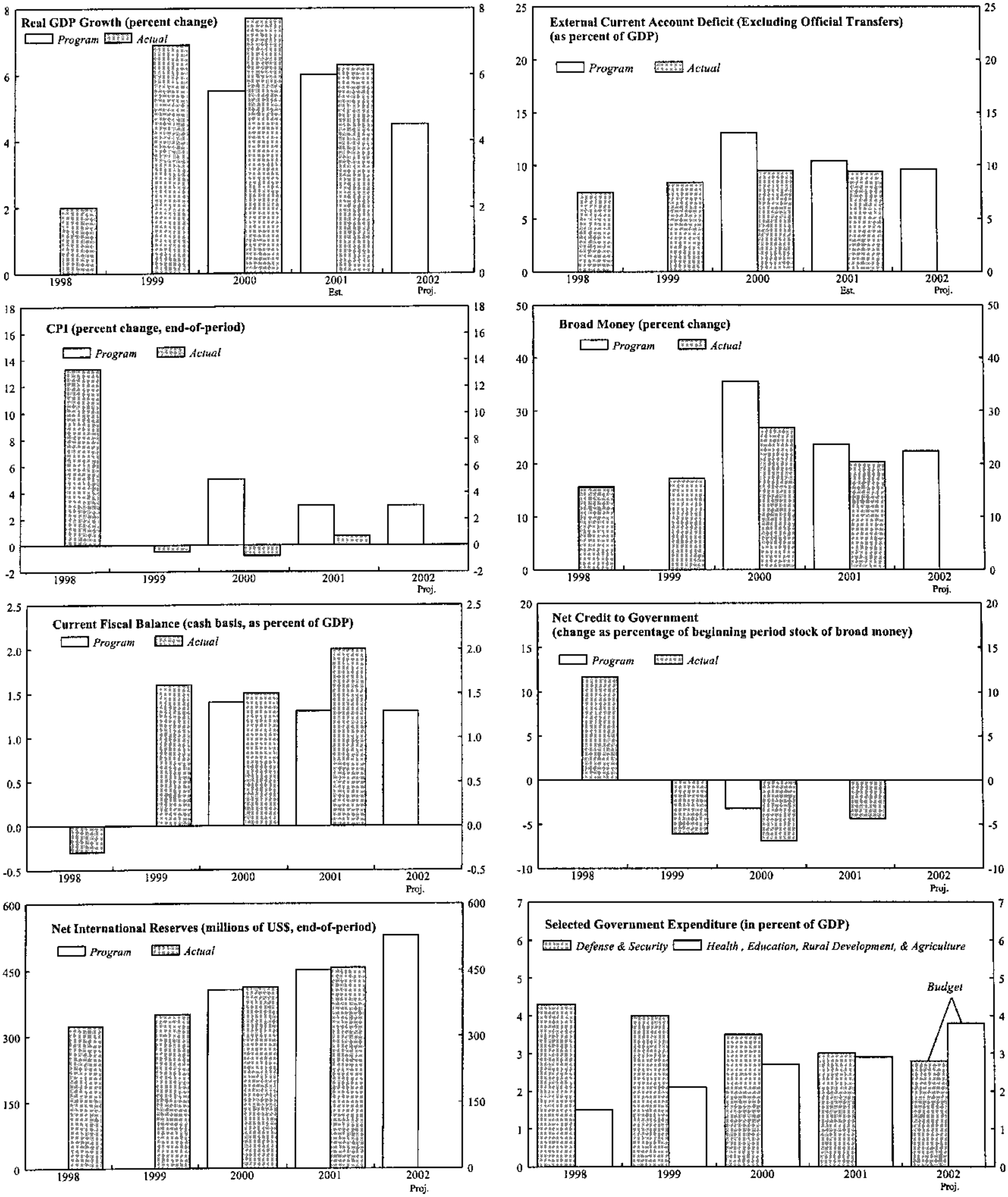


Source: Data provided by the Cambodian authorities.

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

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

Chart 2. Cambodia: Indicators of Program Performance, 1998-2002



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

Table 1. Cambodia: Selected Economic Indicators, 1998–2002

Nominal GDP (2001):	$3,404 million
Population (2001):	13 million
GDP per capita (2001):	$259
Fund Quota:	SDR87.5 million

	1998	1999	2000	2001	2002		
				Est.	Prog.	Rev. Prog.	Most Recent
	(Percent change; unless otherwise indicated)						
Real economy							
Real GDP	2.1	6.9	7.7	6.3	4.5	4.5	...
GDP deflator	13.8	3.7	-4.6	-2.9	3.0	3.0	...
Consumer prices (end of period)	13.3	-0.5	-0.8	0.7	3.0	3.0	3.9 7/
(annual average)	14.8	4.0	-0.8	0.2	1.4	1.4	1.5 7/
Money and credit							
Broad money	15.7	17.3	26.9	20.4	19.4	22.4	31.6 8/
Of which: riels in circulation	43.0	-3.8	1.0	16.8	13.5	20.2	31.2 8/
Net credit to the government 1/	11.7	-6.1	-6.9	-4.3	0.0	0.0	-5.0 8/
Velocity of money 2/	10.3	9.3	7.3	6.6	5.8	5.8	...
	(In percent of GDP)						
Government budget							
Revenue (incl. capital revenue)	8.3	10.6	11.2	11.7	12.8	12.8	11.5 9/
Of which: tax revenue	6.0	7.7	8.2	8.4	8.9	8.9	7.5 9/
nontax revenue	2.0	2.8	2.8	3.2	3.7	3.7	3.6 9/
Expenditure 3/	13.8	14.7	16.4	17.7	18.5	18.7	14.2 9/
Current expenditure 3/	8.3	8.9	9.5	10.4	11.3	11.3	7.9 9/
Capital expenditure	5.5	5.8	6.9	7.3	7.2	7.4	6.0 9/
Current budget balance	-0.3	1.6	1.5	1.2	1.3	1.3	3.0 9/
Overall budget balance	-5.5	-4.0	-5.2	-6.0	-5.8	-5.9	-2.7 9/
Overall budget balance (incl. grants)	-2.5	-1.3	-2.3	-3.1	-2.8	-2.6	1.3 9/
Foreign financing	4.5	4.4	5.5	5.7	5.8	6.2	6.9 9/
Domestic financing	1.0	-0.6	-0.1	0.1	0.0	-0.3	-3.1 9/
Outstanding operations 4/	0.1	0.3	-0.2	0.2	0.0	0.0	-1.0 9/
Domestic investment	11.3	15.9	13.5	17.9	15.0	16.2	...
Government investment	5.3	5.7	6.7	7.2	7.0	7.2	6.0 9/
Nongovernment investment	6.1	10.2	6.8	10.7	8.0	9.0	...
Of which: change in inventories	-0.9	1.4	-1.7	2.0	...	...	...
National saving	10.3	14.1	12.0	16.2	13.0	13.8	...
Government saving	-0.3	1.6	1.5	1.2	1.3	1.3	3.0 9/
Nongovernment saving	10.6	12.5	10.5	15.0	11.8	12.5	...
	(In millions of U.S. dollars; unless otherwise indicated)						
Balance of payments							
Exports 5/	685	921	1,205	1,288	1,402	1,358	...
Imports 5/	-919	-1,201	-1,570	-1,647	-1,718	-1,752	...
Current account (excl. official transfers)	-226	-277	-318	-320	-358	-356	...
(in percent of GDP)	-7.5	-8.4	-9.5	-9.4	-9.7	-9.6	...
Current account (incl. official transfers)	-32	-56	-50	-57	-72	-87	...
(in percent of GDP)	-1.0	-1.7	-1.5	-1.7	-2.0	-2.4	...
Capital account	-65	-30	3	86	78	116	...
Overall balance	-96	-86	-47	29	5	28	...
Gross official reserves	390	422	485	551	604	629	617 10/
(In months of imports of goods and services)	3.7	3.2	2.9	3.2	3.2	3.4	3.3 10/
Net official reserves	323	349	411	470	516	537	533 10/
External debt 6/	2,044	2,233	2,229	2,218	1,529	1,552	...
(in percent of GDP)	67.9	67.7	66.5	65.2	41.5	42.1	...
Debt service	124	125	129	55	20	20	...
(In percent of domestic exports of goods and services)	18.4	11.1	8.6	3.3	1.1	1.1	...
Memorandum items:							
Nominal GDP (in billions of riels) 11/	11,364	12,587	12,932	13,357	14,377	14,377	...
(in millions of U.S. dollars)	3,011	3,300	3,351	3,404	3,686	3,686	...
Exchange rate (riels per dollar, end of period)	3,780	3,775	3,910	3,900	3,900	3,900	3,920 12/

Sources: 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 cash adjustments.
4/ Includes expenditure committed but not yet allocated to the accounts of the government agencies that execute the budget, and exchange rate adjustments.
5/ Excludes re-exports.
6/ A Paris Club rescheduling under Naples terms (67 percent NPV reduction) is assumed in 2002.
7/ As of May 2002
8/ As of April 2002.
9/ As of April 2002. These data include estimates of provincial finances and is not seasonally adjusted.
10/ As of June 27, 2002. Gold and foreign liabilities are evaluated at the end-2001 gold price and $/SDR exchange rate respectively.
11/ GDP figures have been revised to reflect new estimates provided by the National Institute of Statistics and officially released in May 2002.
12/ As of end-June 2002.

Table 2. Cambodia: Quantitative Performance Criteria and Benchmarks, December 2001–March 2002

	2000	2001			2002		
	Stock at End -Dec.	End-Dec.			End-March 1/		
	Actual	Rev. Prog.	Adj. Prog.	Actual	Prog.	Adj. Prog.	Actual
	(Cumulative change from beginning of year)						
Net domestic assets of the central bank (in billions of riels) 2/3/	-941	-57	-18	-171	18	-49	-110
Net credit to the government from the banking system (in billions of riels) 3/	3	0	39	-78	20	-47	-77
Net domestic financing of the budget (in billions of riels) 3/	...	0	39	13	20	-47	-138
Contracting or guaranteeing of external debt by the public sector 4/							
Up to one-year maturity 5/	...	...	...	...	...	...	...
1-5 year's maturity	...	...	...	...	...	...	...
Medium-and long-term nonconcessional debt 6/	...	...	...	...	...	...	...
External payments arrears 7/	...	...	...	...	...	...	...
Net official international reserves (in millions of U.S. dollars) 8/	411	40	30	56	4	7	32
Memorandum items:							
Foreign currency nonproject budget/BOP support (in millions of U.S. dollars)	...	20	...	5	0	2	2
Total nonproject budget support (in billions of riels)	...	144	...	54	0	67	67
Exchange rate (riels per U.S. dollar; end of period)	3,910	4,000	...	3,900	3,900	3,900	3,900

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

1/ Performance criteria.

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

3/ For purposes of verifying compliance with the program, the program ceiling for net domestic assets of the central bank, net credit to the government from the banking system, and net domestic financing of the budget were adjusted upward by CR 39 billion in December 2001 due to shortfalls in total nonproject budget support. In March 2002, these items were adjusted downward by CR 67 billion, reflecting an excess in total 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 $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 $15.4 million in December 2001. In March 2002, the floor on net international reserves was adjusted upward by $2.3 million.

Table 3. Cambodia: Structural Benchmarks and Performance Criteria Assessed During the Fifth Review

	Policy Action	Program Monitoring	Status
1.	Suspend all logging activity by concessionaires with effect from January 1, 2002 until sustainable management plans have been approved.	Structural benchmark (continuous)	Partially observed. Enforcement capabilities need to be upgraded.
2.	Issue government regulation (Prakas) detailing a specific format for cash management procedures as a basis for improving the operations of the Cash Management Unit and establishing better coordination between the National Treasury and the Foreign Currency Unit by end-January 2001.	Structural benchmark	Observed.
3.	Revoke banking licenses for banks that have not met the requirements under their MOU, including additional closures if necessary, by end-February 2002.	Structural benchmark	Completed. Final decisions were announced on March 19.
4.	Submit the Law on Negotiable Instruments and Payments Transactions to the Council of Ministers by end-May 2002.	Structural benchmark	Completed. The law was submitted to the Council of Ministers on June 4.
5.	Reduce the number of accounts by integrating revenue accounts held by line ministries (as specified in the Technical Memorandum of Understanding) with the National Treasury single account by end-March 2002.	Structural performance criterion	Observed.
6.	Submit a new Customs Law (in line with WTO requirements) to the Council of Ministers by end-March 2002.	Structural benchmark	More comprehensive revision of the law than previously envisaged is being undertaken and should be submitted to the Council of Ministers by end-July.
7.	Complete an unqualified audit of the 2001 accounts of the Foreign Trade Bank by end-May 2002.	Structural performance criterion	An audit was completed, but was qualified. An unqualified audit of the March 2002 accounts was completed on June 19.
8.	Establish anti-smuggling unit in key border provinces with clear definition of roles and responsibilities by end-April 2002.	Structural benchmark	A strengthened unit in Phnom Penh, and provisional units in border provinces have been established.

Table 4. Cambodia: General Government Operations, 2000–02

	2000	2001	2002			2000	2001	2002		
		Est.	Budget	Prog.	Rev. Prog.		Est.	Budget	Prog.	Rev. Prog.
			(In billion of riels)					(In percent of GDP)		
Total revenue	1,442	1,561	1,860	1,834	1,834	11.2	11.7	13.4	12.8	12.8
Of which : central government	1,408	1,520	1,816	1,790	1,790	10.9	11.4	13.0	12.5	12.5
Tax revenue	1,055	1,128	1,285	1,279	1,279	8.2	8.4	9.2	8.9	8.9
Direct taxes	136	140	138	127	127	1.0	1.0	1.0	0.9	0.9
Of which : Profit taxes	101	113	108	96	96	0.8	0.8	0.8	0.7	0.7
Of which : Minimum tax refunds (-)	…	…	…	-36	-36	…	…	…	-0.3	-0.3
Indirect taxes	500	571	681	686	686	3.9	4.3	4.9	4.8	4.8
Of which : Excise taxes	113	155	165	220	220	0.9	1.2	1.2	1.5	1.5
Domestic	19	20	35	35	35	0.1	0.2	0.3	0.2	0.2
Import	94	135	130	185	185	0.7	1.0	0.9	1.3	1.3
VAT (net VAT refunds)	371	403	502	452	452	2.9	3.0	3.6	3.1	3.1
Domestic	73	85	112	112	112	0.6	0.6	0.8	0.8	0.8
Import	313	327	390	370	370	2.4	2.4	2.8	2.6	2.6
Refund (-)	-14	-9	…	-30	-30	-0.1	…	…	-0.2	-0.2
Trade taxes	390	376	430	430	430	3.0	2.8	3.1	3.0	3.0
Tax revenue from provinces	29	41	36	36	36	0.2	0.3	0.3	0.3	0.3
Nontax revenue	356	424	550	530	530	2.8	3.2	4.0	3.7	3.7
Of which : Timber Royalties	41	29	46	20	20	0.3	0.2	0.3	0.1	0.1
Enterprises and immobil	27	28	36	36	36	0.2	0.2	0.3	0.3	0.3
PTT	92	122	133	130	130	0.7	0.9	1.0	0.9	0.9
Passports and visa	20	36	43	43	43	0.2	0.3	0.3	0.3	0.3
Quota Auction	22	32	35	75	75	0.2	0.2	0.3	0.5	0.5
Garment licenses	43	39	45	45	45	0.3	0.3	0.3	0.3	0.3
Capital revenue	31	9	25	25	25	0.2	0.1	0.2	0.2	0.2
Total expenditure 1/	2,119	2,367	2,655	2,662	2,682	16.4	17.7	19.1	18.5	18.7
Current expenditure	1,223	1,391	1,620	1,620	1,620	9.5	10.4	11.6	11.3	11.3
Wages	512	488	524	524	524	4.0	3.7	3.8	3.6	3.6
Civil administration	211	214	259	259	259	1.6	1.6	1.9	1.8	1.8
Defense and security	301	274	265	265	265	2.3	2.1	1.9	1.8	1.8
Nonwage	677	866	1,052	1,052	1,052	5.2	6.5	7.6	7.3	7.3
Of which : Operating expenditures	497	602	676	676	676	3.8	4.5	4.9	4.7	4.7
Interest	21	22	25	25	25	0.2	0.2	0.2	0.2	0.2
Unexpected. Expenses (	0	14	15	15	15	0.0	0.1	0.1	0.1	0.1
Reserve funds (Chapter	13	63	111	110	110	0.1	0.5	0.8	0.8	0.8
Of which: Election	…	…	…	10	10	…	…	…	0.1	0.1
Civil service reform	…	…	…	30	30	…	…	…	0.2	0.2
Demobilization	…	…	…	14	14	…	…	…	0.1	0.1
Provincial expenditure (net subsidy)	33	37	44	44	44	0.3	0.3	0.3	0.3	0.3
Capital expenditure	896	975	1,035	1,042	1,062	6.9	7.3	7.4	7.2	7.4
Locally financed	303	283	335	342	362	2.3	2.1	2.4	2.4	2.5
Externally financed	592	692	700	700	700	4.6	5.2	5.0	4.9	4.9
Current balance	188	160	215	189	189	1.5	1.2	1.5	1.3	1.3
Overall balance	-677	-806	-795	-828	-848	-5.2	-6.0	-5.7	-5.8	-5.9
Overall balance (including grants)	-293	-410	-395	-404	-369	-2.3	-3.1	-2.8	-2.8	-2.6
Financing	677	806	795	828	848	5.2	6.0	5.7	5.8	5.9
Foreign financing (net)	708	763	808	828	894	5.5	5.7	5.8	5.8	6.2
Of which : Budget support (grant)	24	36	0	24	79	0.2	0.3	0.0	0.2	0.5
Budget support (loans)	89	18	120	113	124	0.7	0.1	0.9	0.8	0.9
Project grants	360	360	400	400	400	2.8	2.7	2.9	2.8	2.8
Project loans	234	353	300	300	300	1.8	2.6	2.2	2.1	2.1
Domestic financing (net)	-11	13	-13	0	-46	-0.1	0.1	-0.1	0.0	-0.3
Of which : Central bank financing (net)	-103	-78	-5	0	0	-0.8	…	0.0	0.0	0.0
Private sector accounts	103	73	-8	0	-46	0.8	…	-0.1	0.0	-0.3
Exchange rate adjustments	-7	-2	0	0	0	-0.1	0.0	0.0	0.0	0.0
Outstanding operations 2/	-12	32	0	0	0	-0.1	0.2	0.0	0.0	0.0
Memorandum items:										
Defense and security outlays	446	400	390	390	390	3.5	3.0	2.8	2.7	2.7
Health, education, rural development, agriculture	299	382	518	518	518	2.3	2.9	3.7	3.6	3.6
Tax department revenue	229	249	299	258	258	1.8	1.9	2.1	1.8	1.8
Customs department revenue	797	838	950	985	985	6.2	6.3	6.8	6.9	6.9
Total demobilization cost 3/	9	…	88	88	88	0.1	…	0.6	0.6	0.6
Of which : government's expense 3/	1	…	14	14	14	0.0	…	0.1	0.1	0.1
GDP 4/	12,932	13,357	13,919	14,377	14,377	…	…	…	…	…

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

1/ Includes interests on the bond issued in April 2002 to recapitalize the Foreign Trade Bank, but excludes the principal amount.

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

3/ 1,500 soldiers were discharged in 2000, 15,000 in 2001, and an additional 15,000 are expected in 2002. Cost per soldier is US$1,500. The government's financial contribution to the demobilization program is US$240 per soldier.

4/ GDP figures reflect new estimates released in May 2002.

Table 5. Cambodia: Monetary Survey, 1999-2002 1/

	1999	2000	2001		2002							
	Dec.	Dec.	Dec.		Jan.	Feb.	Mar.		April	June	Sept.	Dec.
			Actual	Prog.			Actual	Prog.		Revised Program		
	(In billions of riels; end of period)											
Net foreign assets	2,019	2,588	3,080	2,995	3,249	3,354	3,366	3,157	3,417	3,416	3,483	3,518
National Bank	1,649	2,102	2,428	2,450	2,521	2,552	2,680	2,481	2,789	2,716	2,759	2,769
Deposit money banks	370	486	651	545	729	802	686	676	628	700	725	749
Net domestic assets	-576	-758	-876	-732	-921	-955	-959	-908	-896	-913	-876	-821
Domestic credit	876	904	868	1,041	866	857	829	853	867	915	950	1,006
Government (net)	103	3	-75	3	-75	-105	-152	-122	-150	-95	-95	-75
Public enterprises	10	3	7	4	6	5	5	4	5	4	4	4
Private sector	763	898	936	1,033	935	957	976	971	1,013	1,006	1,041	1,077
Other items (net)	-1,453	-1,662	-1,743	-1,772	-1,787	-1,813	-1,788	-1,761	-1,763	-1,828	-1,826	-1,827
Of which: capital	-1,638	-1,791	-1,959	...	-1,967	-1,971	-1,971	...	-1,909	...	...	...
National Bank	-870	-1,000	-1,035	...	-1,048	-1,048	-1,067	...	-1,078	...	...	...
Deposit money banks	-767	-791	-924	...	-919	-923	-904	...	-832	...	...	...
Broad money	1,443	1,831	2,204	2,263	2,328	2,398	2,408	2,249	2,521	2,504	2,608	2,697
Narrow money	532	540	610	581	638	649	676	648	709	679	710	741
Currency in circulation	490	495	578	535	604	615	641	607	673	636	665	694
Demand deposits	42	45	32	46	34	35	35	41	36	43	45	47
Quasi-money	911	1,291	1,594	1,682	1,690	1,749	1,731	1,601	1,812	1,825	1,898	1,956
Time deposits	32	46	56	54	54	63	62	58	61	61	64	67
Foreign currency deposits	879	1,245	1,539	1,629	1,637	1,686	1,670	1,543	1,751	1,763	1,833	1,888
	(12 - month percent change)											
Net foreign assets	16.8	28.2	19.0	15.7	24.2	23.8	23.2	15.5	25.0	21.7	18.0	14.2
Net domestic assets (+ decrease)	15.7	31.5	15.6	-3.5	23.7	22.4	14.9	8.8	9.7	11.1	5.8	-6.3
Private sector	16.6	17.7	4.2	15.0	4.2	7.0	7.9	7.3	10.8	6.3	5.0	15.0
Broad money	17.3	26.9	20.4	23.7	24.3	24.4	26.8	18.4	31.6	26.1	22.8	22.4
Of which: currency in circulation	-3.8	1.0	16.8	8.2	22.7	22.5	25.6	18.8	31.2	24.8	24.3	20.2
	(Contribution to annual growth of broad money; in percent)											
Net foreign assets	23.6	39.5	26.8	22.2	33.8	33.4	33.3	22.3	35.7	30.7	25.1	19.9
Net domestic assets	-6.3	-12.6	-6.4	1.4	-9.4	-9.1	-6.6	-3.9	-4.1	-4.6	-2.3	2.5
Domestic credit	3.0	2.0	-2.0	7.4	-2.6	-2.7	-0.4	0.8	0.4	2.5	1.1	6.3
Government (net)	-6.1	-6.9	-4.3	0.0	-4.8	-6.1	-4.4	-2.8	-5.0	-0.7	-1.0	0.0
Private sector	8.8	9.4	2.1	7.4	2.0	3.2	3.7	3.5	5.1	3.0	2.3	6.4
Other items (net)	-9.4	-14.5	-4.4	-6.0	-6.8	-6.4	-6.1	-4.7	-4.5	-7.1	-3.4	-3.8
Memorandum items:												
Foreign currency deposits (in millions of dollars)	233	318	395	407	420	431	428	396	449	452	470	484
Foreign currency deposits (in percent of broad money)	61	68	70	72	70	70	69	69	69	70	70	70
Credit to the private sector (in millions of dollars)	202	230	240	258	240	245	250	249	259	258	267	276
Velocity 2/	9.3	7.3	6.6	7.2	6.5	6.4	6.3	6.6	6.2	6.1	6.0	5.8

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

1/ The coverage of the monetary survey takes into account the closing of banks during the relicensing process.

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

Table 6. Cambodia: Summary Accounts of the National Bank of Cambodia, 1999-2002

	1999	2000	2001		2002					
	Dec.	Dec.	Dec.		Mar.		April	June	Sept.	Dec.
			Actual	Prog.	Actual	Prog.		Revised Program		
	(In billions of riels; end of period)									
Net foreign assets	1,649	2,102	2,428	2,450	2,680	2,481	2,789	2,716	2,759	2,769
Foreign assets	1,924	2,389	2,740	2,768	3,016	2,824	3,129	3,049	3,120	3,121
Foreign liabilities	-275	-286	-312	-318	-335	-343	-339	-334	-361	-352
Net domestic assets	-719	-941	-1,069	-998	-1,180	-1,119	-1,192	-1,115	-1,117	-1,099
Claims on central government (net)	107	4	-75	3	-152	-122	-150	-95	-95	-75
Claims	283	272	271	...	269	...	269	...	...	...
Deposits	176	268	346	...	421	...	419	...	...	...
Claims on deposit money banks (net)	-77	-69	-85	-106	-82	-81	-88	-83	-85	-87
Claims on public enterprises (net)	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
Other items (net)	-749	-877	-909	-895	-947	-916	-953	-937	-937	-937
Assets	121	124	127	...	168	...	173	...	...	...
Liabilities	870	1,000	1,035	...	1,115	...	1,126	...	...	...
Of which : capital	-870	-1,000	-1,035	...	-1,067	...	-1,078	...	...	...
Reserve money	930	1,161	1,360	1,452	1,500	1,362	1,597	1,601	1,642	1,670
Currency outside banks	490	495	578	535	641	607	673	636	665	694
Currency in banks	20	34	36	42	34	41	45	44	48	52
Reserve deposits	420	633	746	875	824	715	880	920	929	924
	(12-month percent change)									
Net foreign assets	15.7	27.5	15.5	16.5	20.2	12.9	25.7	20.3	19.3	14.0
Net domestic assets (+ decrease)	15.6	31.0	13.5	6.0	20.0	9.5	19.0	5.9	3.0	2.8
Reserve money	15.9	24.9	17.1	25.0	20.3	15.8	31.2	32.9	33.7	22.8
Of which : currency outside banks	-3.8	1.0	16.8	8.2	25.8	18.8	31.2	24.8	24.3	20.2
	(Contribution to annual reserve money growth; in percent)									
Net foreign assets	27.9	48.8	28.1	29.9	36.0	24.1	46.9	38.1	36.3	25.1
Net domestic assets	-12.1	-23.9	-11.0	-4.9	-15.8	-8.2	-15.7	-5.2	-2.6	-2.2
Net credit to government	-9.4	-11.1	-6.8	-0.1	-5.6	-4.5	-7.8	-1.1	-1.8	0.0
Net claims on banks	-1.2	0.9	-1.4	-3.3	0.4	0.0	-1.9	-1.2	-0.7	-0.6
Other items (net)	-1.4	-13.7	-2.8	-1.5	-10.5	-3.7	-5.9	-2.9	-0.1	-2.1
Memorandum item:										
Money multiplier (Broad Money/Reserve Money)	1.6	1.6	1.6	1.6	1.6	1.7	1.6	1.6	1.6	1.6

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

Table 7.Cambodia: Balance of Payments, 1998-2003
(In millions of U.S. dollars)

	1998	1999	2000	2001	2002		2003
			Prog.	Est.	Prog.	Rev. Prog.	Prog.
Current account (excluding official transfers)	**-226**	**-277**	**-318**	**-320**	**-358**	**-356**	**-368**
Current account (including official transfers)	**-32**	**-56**	**-50**	**-57**	**-72**	**-87**	**-89**
Trade balance 1/	-228	-274	-359	-354	-316	-389	-403
Exports	863	1,099	1,383	1,451	1,663	1,529	1,627
Domestic exports	685	921	1,205	1,288	1,402	1,358	1,448
Of which: GSP (incl. garments)	392	679	1,013	1,142	1,353	1,221	1,270
Forestry	167	111	58	33	12	12	38
Re-exports	178	178	178	163	261	171	179
Imports, f.o.b.	-1,091	-1,373	-1,742	-1,806	-1,979	-1,918	-2,030
Retained imports, f.o.b.	-919	-1,201	-1,570	-1,647	-1,718	-1,752	-1,856
Garments	-267	-406	-606	-683	-879	-730	-760
Petroleum	-181	-194	-300	-295	-281	-292	-296
Other retained imports	-471	-601	-664	-670	-558	-729	-800
Imports for re-export, f.o.b	-172	-172	-172	-158	-261	-166	-173
Services and Income (net)	-57	-73	-29	-41	-118	-43	-46
Services (net)	-9	4	52	77	40	102	115
Of which: Tourism (credit)	66	133	199	235	218	282	302
Income (net)	-48	-76	-82	-118	-158	-145	-161
Of which: Interest (debit)	-18	-11	-11	-11	-32	-18	-42
Private transfers (net)	60	70	70	76	77	77	80
Official transfers (net)	194	220	268	263	285	268	279
Capital and financial account	**-65**	**-30**	**3**	**86**	**78**	**116**	**140**
Medium- and long-term loans	-69	-57	-23	85	96	137	149
Disbursements	46	57	91	119	131	172	194
Amortization	-115	-114	-114	-35	-35	-35	-45
Foreign direct investment	121	146	134	96	75	75	90
Short-term flows and errors and omissions	-116	-118	-108	-95	-94	-96	-98
Overall balance	**-96**	**-86**	**-47**	**29**	**5**	**28**	**51**
Financing	**96**	**86**	**47**	**-29**	**-5**	**-28**	**-51**
Change in gross official reserves	-11	-32	-63	-66	-55	-78	-78
Use of Fund credit	-1	8	4	9	9	9	-1
Debt restructuring 2/	0	0	0	16	1,435	1,435	27
Debt forgiveness	0	0	0	15	800	800	19
Debt rescheduling	0	0	0	1	636	636	8
Change in arrears (- = reduction)	108	110	105	11	-1,395	-1,395	0
Memorandum items:							
Trade balance (in percent of GDP)	-7.6	-8.3	-10.7	-10.4	-8.6	-10.6	-10.1
Current account balance							
Excluding official transfers (in percent of GDP)	-7.5	-8.4	-9.5	-9.4	-9.7	-9.6	-9.3
Including official transfers (in percent of GDP)	-1.0	-1.7	-1.5	-1.7	-2.0	-2.4	-2.2
Gross official reserves 3/	390	422	485	551	604	629	707
In months of imports of goods & services	3.7	3.2	2.9	3.2	3.2	3.4	3.6
In months of core imports of goods & services 4/	3.8	5.3	5.0	6.0	5.8	6.0	6.3
Net international reserves	323	349	411	470	516	537	617
Debt service (cash basis)	7	9	9	11	17	18	61
Nominal GDP (in millions of U.S. dollars)	3,011	3,300	3,351	3,404	3,686	3,686	3,978

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

1/ Includes estimates for unrecorded forestry exports and unrecorded petroleum imports. Data on exports and imports have been revised from earlier estimates based on improved statistics.

2/ Assumes a Paris Club rescheduling under Naples terms (67 percent NPV reduction) in 2002. Bilateral rescheduling agreements were reached with the Czech and Slovak Republics in 2001.

3/ Includes $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, 1999–2006
(In percent of GDP, unless otherwise indicated)

	1999	2000	2001	2002	2003	2004	2005	2006
				Projections				
Real sector								
Real GDP (percent change)	6.9	7.7	6.3	4.5	6.0	6.0	6.5	6.5
Real Per capita GDP (in riels; percent change)	4.2	5.0	3.7	2.5	3.9	3.9	3.4	3.4
CPI Inflation (end-period; percent change)	-0.5	-0.8	0.7	3.0	3.0	3.0	3.0	3.0
CPI Inflation (average; percent change)	4.0	-0.8	0.2	1.8	3.0	3.0	3.0	3.0
GDP deflator (percent change)	3.7	-4.6	-2.9	3.0	3.1	3.1	3.0	3.0
National saving	14.1	12.0	16.2	13.8	14.4	14.8	15.2	15.5
Government saving	1.6	1.5	1.2	1.3	1.3	1.3	1.3	1.3
Private saving	12.5	10.5	15.0	12.5	13.1	13.5	13.9	14.2
Domestic investment	15.9	13.5	17.9	16.2	16.6	17.0	17.4	17.8
Government investment	5.7	6.7	7.2	7.2	6.9	6.6	6.5	6.2
Private investment	10.2	6.8	10.7	9.0	9.7	10.4	10.9	11.6
Of which: changes in inventories	1.4	-1.7	2.0	...	...	...	...	...
Fiscal sector								
Revenue	10.6	11.2	11.7	12.8	13.2	13.9	14.0	14.4
Of which : Tax revenue	7.7	8.2	8.4	8.9	9.3	9.7	10.1	10.5
Nontax revenue	2.8	2.8	3.2	3.7	3.7	4.0	3.6	3.6
Expenditure (cash basis)	14.7	16.4	17.7	18.7	18.8	19.2	19.3	19.4
Current	8.9	9.5	10.4	11.3	11.7	12.4	12.5	12.8
Of which: interest payments	0.1	0.1	0.2	0.5	1.1	1.0	1.0	0.9
Capital	5.8	6.9	7.3	7.4	7.1	6.8	6.8	6.5
Current balance	1.6	1.5	1.2	1.3	1.3	1.3	1.3	1.3
Overall balance	-4.0	-5.2	-6.0	-5.9	-5.6	-5.3	-5.2	-4.9
Overall balance (including grants)	-1.3	-2.3	-3.1	-2.6	-2.3	-2.0	-1.9	-1.9
Domestic financing	-0.3	-0.1	0.1	-0.2	0.0	0.0	0.0	0.0
External financing	4.4	5.3	5.9	6.1	5.6	5.2	5.0	4.8
Disbursements	4.4	5.3	6.0	7.1	6.7	6.3	6.0	5.7
Amortization	0.0	0.0	0.0	0.9	1.1	1.1	1.0	0.9
Monetary sector								
Broad money (percent change)	17.3	26.9	20.4	22.4	20.0	17.5	16.7	16.4
Velocity (GDP/M2)	9.3	7.3	6.6	5.8	5.3	4.9	4.6	4.3
Private sector credit (percent change)	16.6	17.7	4.2	15.0	15.0	15.0	15.0	15.0
External sector								
Domestic exports (percent change)	34.5	30.8	6.9	5.4	6.7	6.4	9.5	7.5
Retained imports (percent change)	30.7	30.7	5.0	6.4	6.0	6.0	7.0	7.5
Current account balance (excluding transfers)	-8.4	-9.5	-9.4	-9.6	-9.3	-9.0	-8.6	-8.4
Current account balance (including transfers)	-1.7	-1.5	-1.7	-2.4	-2.2	-2.2	-2.2	-2.3
Overall balance	-2.6	-1.4	0.9	0.8	1.3	0.3	0.2	0.2
Financing gap (in millions of US$)	0	0	0	0	0	38	41	43
Gross official reserves (in millions of US$)	422	485	551	629	707	778	851	926
(in months of imports of goods and services)	3.2	2.9	3.2	3.4	3.6	3.8	3.8	3.9
External debt 1/	68	67	65	42	43	43	42	41
Of which: Central government 1/	65	64	63	40	42	42	42	41
External debt (NPV) 1/	56	56	56	27	27	26	26	25
Debt-service ratio 2/	11.1	8.6	3.3	1.1	3.6	3.4	3.3	3.0

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

1/ Figures include bilateral debt with the Russian Federation and the United States and reflect the impact of completing rescheduling agreements on Naples terms with these creditors in 2002.

2/ As percent of domestic exports of goods and services. The declines in 2000 and 2001 reflect the end of the large part of the scheduled payments to the Russian Federation.

Table 9. Cambodia: Indicators of Fund Credit, 1998–2011

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
				Projections										
				(In millions of SDRs)										
Outstanding Fund Credit	47.2	53.1	56.2	63.6	73.7	72.6	65.6	59.7	55.5	48.0	37.1	25.4	15.4	7.9
GRA	5.2	4.2	3.1	2.1	1.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
SAF/PRGF	42.0	49.0	53.1	61.4	72.5	72.5	65.5	59.6	55.4	47.9	37.0	25.3	15.3	7.8
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
Total debt service to the Fund	1.5	2.9	5.7	9.6	7.2	10.1	7.6	6.5	4.7	8.0	11.4	12.1	10.4	7.9
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
Repayments of SAF/PRGF	0.0	1.4	4.2	8.4	5.6	8.4	7.0	5.9	4.2	7.5	10.9	11.7	10.0	7.5
Charges	0.5	0.4	0.4	0.2	0.6	0.7	0.6	0.6	0.5	0.5	0.5	0.4	0.4	0.4
				(In percent)										
Fund credit outstanding														
In percent of total public external debt	3.1	3.3	3.3	3.6	6.0	5.3	4.4	3.7	3.3	2.7	2.0	1.3	0.7	0.3
In percent of quota	72.6	60.7	64.3	72.6	84.2	83.0	75.0	68.2	63.4	54.8	42.4	29.0	17.6	9.0
Debt service to the Fund														
In percent of total public external debt service	1.7	3.1	5.7	22.2	44.8	18.7	14.0	11.7	8.5	13.2	13.5	14.1	12.1	9.2
In percent of exports of goods and services	0.3	0.3	0.5	0.7	0.5	0.7	0.5	0.4	0.3	0.4	0.5	0.5	0.4	0.3
				(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
Total public external debt	1,507	1,627	1,711	1,765	1,235	1,376	1,485	1,592	1,697	1,793	1,883	2,000	2,161	2,352
Total public external debt service	91	91	99	43	16	54	54	55	55	61	84	86	86	85
Total exports of goods and services	498	823	1,160	1,311	1,401	1,495	1,588	1,698	1,821	1,951	2,087	2,232	2,389	2,554
Total debt-service ratio														
(in percent of exports of goods and services)	18.4	11.1	8.6	3.3	1.1	3.6	3.4	3.3	3.0	3.1	4.0	3.9	3.6	3.3

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

Table 10. Cambodia: Proposed Schedule of Remaining Disbursements
Under the PRGF Arrangement, 2001–02

Amount	Available Date	Conditions for Disbursement
SDR 8,357,000 (9.6 percent of quota)	Upon completion of the fifth review.	Observance of the end-March 2002 quantitative performance criteria, and relevant structural performance criteria.
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: Recent Performance of the Garment Industry

Overview

1. Cambodia's garment industry has witnessed a dramatic increase in its exports over the past few years (Chart). The U.S. government granted Cambodia Most Favored Nation (MFN) status in 1996 and subsequently designated Cambodia as a beneficiary of the Generalized System of Preferences (GSP) program in 1997.[1] While the GSP scheme specifically excluded textiles and garments from the list of goods that enjoy the zero tariff access to the U.S. market, the average tariff rate of 17 percent under the MFN was sufficient for Cambodia to increase its garment exports by as much as 70–190 percent per annum during 1996–98. In 1999, faced with a rapid increase in imports from Cambodia, the U.S. government imposed quotas on 12 categories of garment products.[2] Nevertheless, garment exports grew by 13–75 percent during 1999–2001. In the aftermath of the U.S. economic slowdown, however, the growth in Cambodia's garment exports have shown a marked decline since the last quarter of 2001. In the first quarter of 2002, total exports recorded negative growth for the first time since the country received the preferential trade arrangement in 1996.

Competitiveness of the Industry

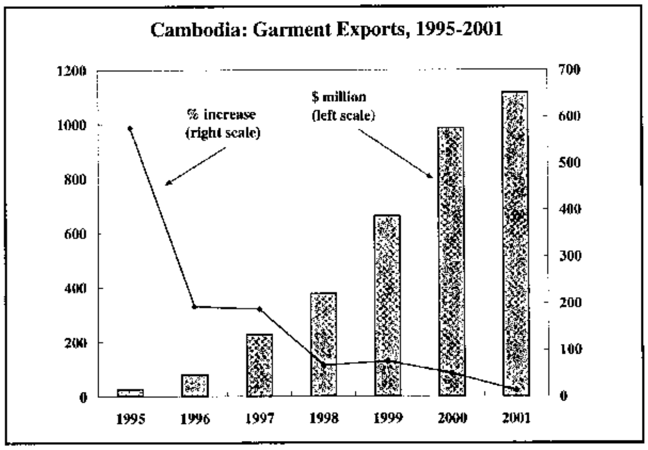
2. Cambodia is a highly dollarized economy with around 70 percent of broad money accounted for by U.S. dollar denominated deposits.[3] The garment industry is almost completely dollarized. An industry study shows that for every $100 worth of garments exported, $63 was spent on imported raw materials, and $17 spent on labor costs with the

[1] In 1999, the EU signed a textile and garment trade agreement with Cambodia, under which Cambodian garments enter the EU market with no duty and quotas imposed. Since the U.S. accounts for more than 70 percent of total garment exports (2001), this annex focuses on Cambodia's performance in the U.S. market.

[2] According to the U.S.-Cambodia textile agreement, which covered the period 1999–2001, the relaxation of the quotas consisted of an automatic increase of 6 percent and an additional bonus of up to 14 percent that would be approved on the basis of the U.S. recognition of Cambodia's compliance with internationally recognized labor standards. In both 2000 and 2001, the United States granted a quota increase of 15 percent (6 percent automatic plus 9 percent bonus components). In late 2001, both governments reached agreement to extend their bilateral textile agreement for an additional three years, through December 2004. The quota for most textile exports in 2002 was 15 percent higher than in 2001, a 9 percent bonus in addition to the normal increase of 6 percent.

[3] de Zamaroczy, Mario and Sopanha Sa, "*Macroeconomic Adjustment in a Highly Dollarized Economy---The Case of Cambodia*," IMF Working Paper (WP/02/92)

wages specified in dollars (the minimum wage in the industry is currently $45 per month).[4] Given this production structure, changes in the domestic exchange rate do not affect the external competitiveness of the industry, although changes in the exchange rates of competing countries would still have an impact.



3. One indication of Cambodia's continued competitiveness is the rapid expansion of nonquota exports. Faced with quota restrictions in 12 categories, Cambodian garment producers have increasingly focused on exports of garment types that are not subject to quotas. In fact, in 2001, nonquota exports increased by 44 percent, accounting for 39 percent of total garment exports to the U.S. market, compared to 30 percent in 2000.[5] Moreover, exports to the non-U.S. market, mainly the EU which is quota free, continue to be robust. They increased by 17 percent in the first quarter of 2002 after growing by 37 percent in 2001.

4. Therefore, rather than any change in competitiveness per se, exogenous factors are a better explanation of the recent deceleration in Cambodia's garment exports. Preferential trade arrangements granted to some of Cambodia's competitors is one of these factors.[6] In 2000, the United States signed into law a historic trade and development act (African Growth and Opportunity Act) that granted sub-Saharan African producers (including textiles and garments producers) quota/duty free access to the U.S. market. In the same year, the U.S. government also signed a Bilateral Trade Agreement with Vietnam which paved the

[4] Cambodia Development Resource Institute, *Cambodia's Annual Economic Review 2001.*

[5] In terms of quantity, the increase in nonquota items is even more marked. In 2001, nonquota exports increased by 72 percent and accounted for 59 percent of total exports to the United States, compared to 44 percent in 2000.

[6] Cambodian government officials and industry representatives point to competition from ASEAN producers (Indonesia, Thailand and Vietnam), South Asia (India, Bangladesh and Sri Lanka) and African countries (Mozambique and Madagascar).

way for Vietnamese garment producers to export to the U.S. market at MFN tariff rates and without quota restrictions.[7] The product lines of these countries compete directly with those of Cambodia, as they specialize, among other things, in cotton apparels and man-made-fiber apparels.

5. The effect of these institutional arrangements in promoting exports is clearly visible for both Vietnam and sub-Saharan countries in the midst of a global economic slowdown. In 2001, sub-Saharan countries' exports increased by 26 percent while world exports to the U.S. experienced a slight decline of 2 percent. In the first quarter of 2002, Vietnam and sub-Saharan countries increased their exports by 178 percent and 28 percent, respectively, while world total exports to the United States declined by 10 percent. During this period, Cambodia did relatively better than most of its ASEAN and South Asian competitors. Its exports grew by 17 percent in 2001 and the decline of 11 percent in the first quarter of 2002 was in line with the global slowdown. On the other hand, ASEAN producers experienced a deeper decline of 16 percent in the first quarter of 2002 while South Asian producers saw their exports fall by 2–13 percent.

U.S. Textiles and Apparels Imports from the Rest of the World

	2000	2001	Percent Change	1Q/2001	1Q/2002	Percent Change
Total imports	71,691.5	70,238.1	-2.0	17,504.8	15,765.9	-9.9
of which						
ASEAN	9,797.8	9,998.5	2.0	2,586.4	2,176.2	-15.9
Cambodia	815.8	952.5	16.8	260.4	231.1	-11.2
Vietnam	49.9	49.3	-1.1	13.7	38.0	177.8
Indonesia	2,380.2	2,552.8	7.3	664.3	563.9	-15.1
Thailand	2,447.1	2,441.4	-0.2	593.1	507.6	-14.4
Sub-Sahara	776.4	975.0	25.6	213.1	263.9	23.8
Madagascar	109.7	178.1	62.4	33.7	36.5	8.5
South Asia						
India	2,740.7	2,633.3	-3.9	757.4	740.1	-2.3
Bangladesh	2,204.7	2,205.0	0.0	596.1	519.8	-12.8
Sri Lanka	1,677.4	1,698.3	1.2	468.9	419.0	-10.6

Source: The Office of Textiles and Apparel, U.S. Department of Commerce.

[7] A World Bank study predicts that the exports of Vietnamese clothing could increase as much as fifteen-fold as tariff reductions to the MFN level is particularly large for this export category at more than 40 percent. See Fukase, Emiko and Will Martin, "*The Effects of the United States Granting MFN Status to Vietnam*," 1999.

Institutional rigidities

6. Looking forward, Cambodia's long-term competitiveness is clouded by concerns about its institutional rigidity. The garment industry faces minimum wage restrictions imposed in 1999 as part of the Textile and Apparel Agreement. While the minimum wage in Cambodia is not particularly high in comparison with other competing countries, the dollar-based minimum wage may deprive the industry of flexible adjustments to external shocks. Restrictions on work shifts are another institutional rigidity that could undermine Cambodia's long-term competitiveness. Garment factories are currently only permitted to operate two shifts per day with a night shift requiring doubling of the wage rate. Moreover, industry representatives complain about the poor quality of the labor force, a large number of public holidays, and frequent strikes and other disruptions to the production process. Finally, there are substantial unofficial fees and regulatory compliance costs in exporting garments. For example, the Integrated Framework study estimated the informal costs as much as $150 per container consisting of $30,000 worth of garment exports.[8]

Minimum Wages in Garment Industry in Selected Countries

	Year	Hours of Work	Minimum Wage	Average Salary
Cambodia	2000	48	45	61
Vietnam	2000	48	45	60
Indonesia	2000	40	43	46
Thailand	1999	48	93–109	106
India	1999	48	6–54	57
Bangladesh	1996	48	12–76	40
Sri Lanka	1998	45	29–37	63

Source: Integration and Competitiveness Study

Conclusion

7. The recent slowing of Cambodia's garment exports is more related to the global economic slowdown and the preferential trade arrangements granted to competing countries than its loss of competitiveness. However, institutional rigidities embodied in the current labor market, if not addressed, could undermine Cambodia's competitiveness in the long run.

[8] *Cambodia: Integration and Competitiveness Study*, 2001, ITC, World Bank, UNCTAD, IMF, UNDP and WTO.

Cambodia: Fund Relations
As of May 31, 2002

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

		SDR Million	Percent Quota
II.	**General Resources Account**:	**SDR Million**	**Percent Quota**
	Quota	87.50	100.0
	Fund Holdings of Currency	89.06	101.8
III.	**SDR Department**:	**SDR Million**	**Percent Allocation**
	Net cumulative allocation	15.42	100.00
	Holdings	0.49	3.21
IV.	**Outstanding Purchases and Loans**:	**SDR Million**	**Percent Quota**
	Systemic Transformation	1.56	1.8
	PRGF arrangements	65.58	75.0

V. **Financial Arrangements**:

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
ESAF/PRGF	10/22/1999	02/28/2003	58.50	41.79
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				
	12/31/2001	2002	2003	2004	2005	2006
Principal	--	4.7	9.4	7.0	5.9	4.2
Charges/Interest	--	0.5	0.7	0.6	0.6	0.5
Total	--	5.2	10.1	7.6	6.5	4.7

VII. **Implementation of HIPC Initiative**: Not applicable.

VIII. **Safeguards Assessment**:

Under its current arrangement with the Fund, Cambodia is subject to the transitional procedures governing safeguards assessments, which require a review of the external audit mechanism of the National Bank of Cambodia (NBC). Staff reviewed the documentation provided by the central bank and concluded that NBC has made considerable progress in updating its external audit mechanism and financial reporting framework in the past year. In particular, the NBC appointed a high quality international accounting firm to audit its financial statements in accordance with International Standards on Auditing and adopted International Accounting Standards.

In addition, staff identified certain weaknesses in other areas of the safeguards framework, notably in NBC's financial reporting framework. Following staff advice, the NBC has agreed to the following measures: (i) the contract of the external auditor has been extended for another five years; (ii) the monitoring of the external audit mechanism (by the Fund) will be adhered to for the duration of the Fund arrangement; and (iii) NBC staff will provide periodic updates to the Fund on the status of the other recommendations made by the auditor. An external audit of NBC's 2001 accounts was recently completed. As done with the 2000 accounts, the NBC will publish its audited financial statements and related audit opinion for 2001, in accordance with safeguards policy.

IX. **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 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 to no more than 1 percent on a daily basis. On May 30, 2002, the official exchange rate was CR 3,910 per U.S. dollar and the private market rate CR 3,912 per U.S. dollar. Cambodia accepted the obligations of Article VIII, Sections 2, 3, and 4 on January 1, 2002. Cambodia maintains an exchange system that is free of restrictions on payments and transfers for current international transactions.

X. **Article IV Consultation**:

Cambodia is on a 12-month consultation cycle. The Executive Board concluded the last Article IV consultation on February 6, 2002 (EBS/02/13, 01/24/02).

XI. **Technical Assistance**:

Following discussions between the Government, the IMF, UNDP, and other interested multilateral and bilateral donors, a comprehensive Technical Cooperation Action Plan (TCAP) was adopted in May 2001. The TCAP calls for an annual review to assess the progress of implementation and, where needed, to adjust planned activities to reflect changed government priorities. With the agreement of the government and participating donors a revised program document, incorporating these changes and related budget adjustments, was completed in June 2002. An update of recent technical assistance missions is contained in Annex VI.

XII. **Resident Representative**:

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

Cambodia: Relations with the World Bank Group[1]

Cambodia became a member of the World Bank on July 22, 1970 but did not borrow from the Bank until 1993. In February 2000, the World Bank approved a Country Assistance Strategy for fiscal years 2000–03, 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 $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 a Resident Office, to assist in the implementation of the Bank's assistance program and facilitate communication with the Government and other donors.

To date, 19 projects have been approved for Cambodia ($472.8 million). Recent projects have focused in the following areas:

- 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, a Road Rehabilitation Project to improve access 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.

- In March 2001, a Flood Emergency Rehabilitation Project ($35 million) was approved.

- In June 2001, an Emergency Supplementary Credit for Social Fund II ($10 million) was approved.

- In August 2001, a Military Demolization and Reintegration Project ($18 million) was approved.

- In February 2002, a Land Management and Administration Project ($24 million) was approved.

[1] Prepared by the Fund staff based on information provided by the World Bank, as of end-May 2002.

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 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 has prepared a Forest Policy Assessment report, a Public Expenditure Review in February 1999, and more recently a poverty assessment and strategy report, a power sector strategy, a diagnostic study on governance and corruption. A new Public Expenditure Review was initiated in April 2002. Negotiations for a $5.4 million Economic and Public Sector Capacity Building Project were held in May 2002. The Project is awaiting Board approval scheduled for June 25, 2002.

IDA: Commitments and Disbursements to Cambodia, 1993–2002
(In millions of U.S. dollars, as of end-May 2002)

Project	Date of Approval	Committed	Disbursed
Emergency Rehabilitation [Closed]	Oct.26, 1993	62.70	64.86
Technical Assistance [Closed]	Dec.6, 1994	17.00	16.90
Social Fund [Closed]	Jun.8, 1995	20.00	18.42
Economic Rehabilitation Credit [Closed]	Sep.28, 1995	40.00	36.91
Phnom Penh Power Rehabilitation [Closed]	Sep.28, 1995	40.00	32.02
Disease Control and Health	Dec.24, 1996	30.40	23.70
Agricultural Productivity Improvement	Feb.28, 1997	27.00	8.40
Urban Water Supply	Feb. 17, 1998	30.96	20.80
Social Fund II	Mar.23, 1999	25.00	22.50
Emergency Supplementary Credit	Jun 19, 2001	10.00	0.00
Road Rehabilitation	Mar.23, 1999	45.31	7.00
North East Village	May 18, 1999	5.00	1.80
Education Quality Improvement	Aug. 31, 1999	5.00	3.20
Biodiversity and Protected Areas LIL	Feb. 8, 2000	1.90	0.30
Structural Adjustment Credit	Feb. 29, 2000	30.00	14.20
Forest Concession Management and Control LIL	Jun. 5, 2000	4.80	0.50
Flood Emergency Rehabilitation	Mar 13, 2001	35.00	2.30
Military Demobilization and Integration	Aug. 23.2001	18.40	0.00
Land Management and Administration Project	February 26, 2002	24.30	0.00
Total		472.77	273.81

Cambodia: Relations with the Asian Development Bank

From 1992 through April 30, 2002, the AsDB approved $558.8 million in low-interest loans to Cambodia to finance 17 projects and three structural reform programs. To date 3 projects (totaling $122.9 million) have been completed: the Special Rehabilitation Assistance Project (approved in 1992), Power Rehabilitation Project (approved in 1994), and an Agriculture Sector Program (approved in 1996). Of the remaining loan projects, $178.6 million were for economic infrastructure, $98.0 million for social infrastructure, and $156.30 million for agriculture and rural infrastructure.

The AsDB designed and administered 83 technical assistance projects during this period. These were financed through $63.4 million in grants from the AsDB ($21.7 million), the Japanese Special Fund ($30.7 million), and other sources ($11.0 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 is very active in the areas of governance, including public expenditure management and medium-term planning. 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 2000, the AsDB conducted an assessment of the flood damage to prepare a proposal for loan assistance to meet Cambodia's rehabilitation requirements. In December 2000 an Emergency Flood Rehabilitation Project in the amount of $55 million was approved. The Financial Sector Development Program has been approved by the Board and the initial tranche conditions have been met. In 2001, the Board also approved a loan to support structural reform in the education sector along with a complementary investment loan.

AsDB: Loan Commitments and Disbursements to Cambodia
(In millions of U.S. dollars)
(as of April 30, 2002)

	Loan Approvals	Contract Awards/ Commitments	Disbursements
1992	67.7	0.0	0.0
1993	0.0	4.4	5.4
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	88.0	17.0	26.2
2000	109.6	114.2	50.8
2001	75.2	40.7	48.3
Total	558.8	326.2	250.9

Cambodia—Statistical Issues

Extensive technical assistance from the Fund, the UNDP, the AsDB, and the World Bank has contributed to substantial improvements in macroeconomic statistics. In October 2001, a long-term STA advisor was placed in the National Institute of Statistics (NIS) to assist the authorities in upgrading economic and financial statistics. An *IFS* page for Cambodia has been published since April 1996. In March 2002 Cambodia's metadata were posted on the General Data Dissemination System (GDDS) site of the Fund's Dissemination Standards Bulletin Board. Despite significant shortcomings in some areas, core data are generally adequate for program design and monitoring and are provided on a timely basis (Attachment I).

National accounts. Official GDP estimates are provided annually under peripatetic support from the AsDB. Revised national accounts series for 1993–2001 were officially released in May 2002. The quality of GDP estimates remains hampered by the lack of comprehensive and reliable sectoral information.

Prices. The NIS provides a monthly CPI with a five-week lag. NIS has recently updated the CPI for Phnom Penh with new expenditure weights (July–December, 2000 = 100). In addition, the NIS has compiled a monthly CPI for five major provincial cities since the second half of 2001. No producer or wholesale price indices are available yet.

Government finance statistics. The Ministry of Economy and Finance provides monthly fiscal data broadly based on GFS standards on a timely basis with a four-week lag. The authorities have provided monthly fiscal data for publication in IFS since 2001 and are committed to providing data for the *GFS Yearbook* in 2002. There are still weaknesses regarding the reliability of data sources, the coverage and the economic and functional classifications of expenditure and donor-specific data on investments financed by project aid are available only with considerable lags. Recent and envisaged measures to improve expenditure management, including a revision of public accounting to be implemented on January 1, 2003, should significantly help in resolving some of these issues.

Monetary statistics. The NBC provides data on the monetary authorities and deposit money banks on a monthly basis with a four-week lag. A STA mission in April 2002 assisted the authorities in strengthening the framework for compiling monetary statistics.

External sector statistics. The NBC is responsible for compiling balance of payments statistics. Customs data have substantial coverage and valuation problems arising from the nonrecording of nondutiable imports, under reporting of re-exports, and the weakness of customs controls. While efforts have been made to improve the quality of foreign direct investment data, private capital flows are believed 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. Data on external debt are provided by the Ministry of Economy and Finance. A balance of payments technical assistance mission visited Cambodia during April–June 2002 to, among other things, review and recommend improvements to the source data used for compiling the balance of payments, including the need to address deficiencies in the foreign direct investment and external debt data.

Cambodia: Core Statistical Indicators as of May 31, 2002

	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	May 31, 2002	May 31, 2002	April, 2002	May 31, 2002	April 2002	April 2002	April 2002	December 2001	December 2001	April 2002	2001	2001
Date Received	June 3, 2002	June 7, 2002	June 7, 2002	June 7, 2002	June 7, 2002	June 7, 2002	May 2002	May 2002	May 2002	May 2002	May 2002	May 2002
Frequency of Data	Daily	Daily	Monthly	Weekly	Monthly	Monthly	Monthly	Quarterly	Quarterly	Monthly	Annual	Annual
Frequency of Reporting	Daily	Weekly one-week lag	Monthly five-week lag	Weekly one-week lag	Monthly five-week lag	Monthly five-week lag	Monthly five-week lag	During missions	During missions	Monthly one-month lag	Annual	During missions
Source of Data	NBC	NBC	NBC	NBC	NBC	NBC	NIS	NBC	NBC	MEF	NIS	MEF
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

Cambodia—Summary of Technical Assistance Provided by the Fund, 1999–June 2002[1]

Purpose	Assistance and Timing (person-months)
Fiscal Reform	
• Tax policy and customs administration	2, September 1999
• Technical Cooperation Action Plan (TCAP) mission	3¾, March-April 2000
• Customs administration (advisor)	5, February 2000
• Tax administration and policy	1, March 2001
• Public expenditure management	1, April 2001
• Long-term customs advisor	12, April 2001
• Long-term treasury advisor	12, August 2001
• Long-term tax advisor	12, October 2001
Monetary Policy and Central Bank Operations	
• Long-term advisor	36, from January 1998
• Banking system reform	4, March and June 2000
• Banking system restructuring and central bank development	2, October 2000
• Banking system restructuring	1, April 2001
• Banking system restructuring and payments system development	1, August 2001
• Payments system development	1, November 2001
• Law on negotiable instruments and payment transactions	½, March and May 2002
Statistics	
• Balance of payments compilation	½, February 2000
• Balance of payments compilation	1, January 2001
• Government Finance Statistics	1, April 2001
• Long-term mutlisector statistics advisor	12, November 2001
• General Data Dissemination System	1, November-December, 2001
• Monetary Statistics	1, March-April, 2002
• Balance of payments compilation	2, April-June, 2002
Legal	
• Legal Framework Review of technical assistance needs	½, April 2000
• Bankruptcy Law	½, November 2000
• Bankruptcy Law	½, July 2001
• Bankruptcy Law	½, February 2002

[1] A detailed description of the Technical Cooperation Action Plan (TCAP) is contained in EBS/01/02 (01/04/01).

June 21, 2002

Mr. Horst Köhler
Managing Director
International Monetary Fund
Washington D.C. 20431
U.S.A

Dear Mr. Köhler:

1. The attached memorandum summarizes key developments under the PRGF-supported program during 2001 and the first half of 2002, and sets forth the economic, financial, and poverty alleviation policies that the Royal Government of Cambodia intends to implement in the remainder of 2002. It also updates the medium-term macroeconomic framework, in light of the recent global downturn.

2. The Government has received broad support from development partners during the Consultative Group Meeting held in Phnom Penh (June 20-21). Cambodia's economic performance through mid-2002 has shown resilience in the face of a weaker global environment. Growth and inflation performance as well as the fiscal outcome in 2001 have been in line with program targets. All quantitative benchmarks for December 2001 and quantitative performance criteria for end-March 2002 were observed. Progress continued to be made in key structural reforms, especially banking sector rehabilitation, trade policy, fiscal restructuring, and dissemination of a governance and anti-corruption agenda. On this basis, the Government requests completion of the fifth review under the PRGF program and a waiver for the nonobservance of a structural performance criterion which required completing an unqualified audit of the 2001 accounts of the Foreign Trade Bank by end-May 2002.

3. The Government believes that the policies and measures described in the attached memorandum are adequate to achieve the objectives of the program for 2002, and stands ready to take additional measures that may become necessary for this purpose. The Government will consult with the Managing Director, at the initiative of either party, and will provide the IMF with such information as it requests on the progress made in policy implementation and the achievement of program objectives. In any event, Cambodia will conduct with the IMF the sixth and final review of the arrangement no later than end-February 2003.

4. In continuing with our policy of transparency, we consent to the publication, including on the IMF's website, of the attached Memorandum of Economic and Financial Policies and the accompanying Executive Board documents prepared by the IMF staff. In addition, as done with the 2000 accounts, we will publish the audited accounts of the NBC for 2001, in compliance with the requirements under the IMF's Safeguards Assessment.

Sincerely yours,

/s/	/s/
Keat Chhon	Chea Chanto
Senior Minister	Governor
Ministry of Economy and Finance	National Bank of Cambodia

Attachment

CAMBODIA

Supplementary Memorandum of Economic and Financial Policies for 2002

June 21, 2002

I. INTRODUCTION AND RECENT DEVELOPMENTS

1. **The Government's reform program supported by the PRGF aims at sustaining economic growth, reducing poverty, and accelerating development.** To this end, the program has successfully achieved macroeconomic stability, with annual GDP growth during 1999–2001 averaging 7 percent and very low inflation.[1] The program continues to focus on reorienting fiscal policy by increasing revenues and reallocating expenditures toward the social sectors. Achieving fiscal objectives will depend on further improvements in tax and customs administration, as well as in public expenditure management. To sustain growth and support poverty reduction the program also aims to promote a sound business environment by enhancing governance and implementing a comprehensive set of structural reforms in the areas of bank restructuring, trade policy, forestry policy, legal and judicial reform, and improving the provision of public services through civil service reform. This memorandum supplements and extends the government's commitments outlined in the December 26, 2001 Memorandum of Economic and Financial Policies.

2. **Cambodia's economy has shown resilience in the face of a weaker global environment.** Growth in 2001 was driven mainly by a booming tourist sector and strong exports of garments. Inflation has remained low, and for the 12-month period ending March 2002 prices increased by only 3 percent. All quantitative performance criteria for March 2002 were observed. The structural performance criterion (SPC) for end-March on the consolidation of government accounts was observed, but the SPC on completing an unqualified audit of the Foreign Trade Bank (FTB) was only partially observed. Most structural benchmarks were met, some with minor delays, while others were only partially observed.

3. **Budgetary performance continued to improve in 2001.** The overall fiscal deficit (excluding grants) was limited to 6 percent of GDP, while the current surplus was maintained at 1¼ percent of GDP. Despite shortfalls in customs revenue, government revenue was close to 12 percent of GDP, reflecting improved collection of domestic taxes and nontax revenue. Overall expenditure was contained below budget targets, thus contributing to the avoidance of domestic financing. However, spending rose sharply in December reflecting the need for structural change in budget and cash management.

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[1] All growth rates and ratios to GDP reflect the recent upgrading of national accounts estimates by the National Institute of Statistics officially released in May 2002.

4. **Monetary and external developments were broadly in line with the program.** Broad money growth in 2001 was 20½ percent, slightly lower than expected, due to a slowing of private sector credit as some banks reduced large exposures to comply with tightened prudential regulations. The current account deficit was slightly higher than programmed, reaching 9½ percent of GDP (excluding grants). The deterioration of the current account was mainly due to a decline in the growth of garment exports since mid-2001. Gross international reserves were larger than programmed, reaching $551 million (about 3 months of imports of goods and services) at end-2001. The riel continued to be relatively stable in U.S. dollar terms, although it appreciated slightly in nominal and real effective terms.

5. **Progress made in the implementation of structural reforms in 2001 has been continued during the first six months of 2002.** Bank restructuring is proceeding as envisaged, progress has been made in the restructuring of the FTB despite the delay in the completion of an unqualified audit, and the draft Law on Negotiable Instruments and Payments Transactions has been completed and was submitted to the Council of Ministers on June 4, 2002. On expenditure management, initial steps to ensure a more efficient pattern of expenditure were taken, including the closing of several government accounts held by line ministries at end-March. Revisions to the Law on Investment were completed and submitted to the National Assembly in March 2002. On trade reform, a revised Customs Law, in line with WTO requirements, was completed and will be submitted to the Council of Ministers in July. On forestry reform, the suspension of all logging activity has remained in place, but issues surrounding the transport of logs cut in 2001 require a strengthening of the monitoring system.

II. MACROECONOMIC AND STRUCTURAL POLICIES FOR THE REMAINDER OF 2002

6. **In view of the resilience of Cambodia's economy to the deterioration of the world economic environment in 2001, the forecasts under the program for 2002 remain appropriate.** For 2002, the growth in garment production is declining after high growth in earlier years, but continued increases in tourist arrivals and improved agricultural production will sustain growth at 4½ to 5½ percent, accompanied by inflation of about 3 percent. The current budget surplus is expected to remain at about 1¼ percent of GDP, while the overall fiscal deficit (excluding grants) will be contained at less than 6 percent of GDP and financed by external concessional resources. The external current account deficit is projected to remain at about 9 percent of GDP and the increase in gross international reserves is now targeted at $78 million, maintaining gross reserves at about 3½ months of imports of goods and services.

7. **Fiscal performance in the first quarter of 2002 was broadly consistent with budget targets.** However, revenue performance was boosted by several once-off payments of nontax revenue. The Government is committed to meet the 2002 revenue target through strict implementation of the agreed revenue and administrative measures as shown in Annex 1. Expenditure has been implemented cautiously, in line with financing targets, and

actions to strengthen public expenditure management and improve the implementation of the budget throughout the year will be continued as outlined in Annex II.

8. **Several tax and administrative measures have been adopted or are underway.** Taxes on petroleum and beer have been increased, the real regime is being extended to 5 additional provinces, and some initial success in collecting tax arrears has been achieved. However, the collection of VAT on airport departure fees was not feasible because of exemptions granted under the service contract. Efforts to strengthen the tax department will continue and for the remainder of 2002 will focus on the steady collection of outstanding tax arrears from the 100 largest accounts with performance monitored against collection targets. Additional taxpayer accounts will be added to the project on an ongoing basis as the original 100 accounts are closed or collected. Tax auditing strategy and capabilities will be enhanced by a comprehensive program that over the next 12 months will establish: (i) formal manuals and procedures; (ii) a modern management information system with audit operations; and (iii) modern work descriptions with clear roles and responsibilities. In addition, there will be an expanded coverage of tax payers using modern selection techniques. Further to the above, decisions are to be taken by end-June 2002 regarding proposed vision, mission, and roles and responsibilities linked to a revised tax administration structure. Tax collection efforts will also be enhanced by improved coordination between the tax and customs department. Detailed instructions for implementing the Prakas issued on February 23, 2001 that specifies reporting relationships between CED and the Tax Department was finalized on June 6, 2002. A joint review has been carried out by CED and the Tax Department on the taxation of motorcycles and motorcycle parts, and a full assessment report with policy options will be finalized by June 28, 2002.

9. **Strengthening the enforcement capabilities of the Customs and Excise Department (CED) will be key to meeting the 2002 revenue targets and to ensure improvements in revenue over the medium term.** Data from CED indicate that revenue improved somewhat during the first quarter of 2002 compared to previous years, owing to higher tax rates on beer and petroleum, and some initial successes in anti-smuggling operations. Efforts for the remainder of 2002 will focus on the following key measures from the government's anti-smuggling strategy: (i) establishing a strengthened anti-smuggling unit in municipal districts around Phnom Penh in May 2002, and extending these to key border provinces by end-June 2002; (ii) creating an Intelligence Unit in CED by end-July 2002 to collect, analyze, and disseminate information to anti-smuggling teams, and prepare statistics for the newly-established Inter-Ministerial Commission (IMC); and (iii) convening regular quarterly meetings of the IMC and monthly meetings of the anti-smuggling working group, and providing regular reports on the results of anti-smuggling operations to the Council of Ministers. Efforts will also be made to strengthen the preshipment inspection program for imports by using reconciliation procedures to resolve valuation differences, and reducing to no more than 10 percent the number of sealed containers subject to re-inspection by any government agency based on principles of risk management.

10. **To strengthen the performance of nontax revenue, the following actions will be taken.** Contract revisions to increase the share of revenue going to the government from

ticket sales at the Angkor temple complex were completed on May 29, 2002. In response to a joint assessment by the Ministry of Economy and Finance and the Ministry of Posts and Telecommunications in December 2001 on the contract for Gateway II, the government has concluded that some aspects of the contract have been implemented inappropriately and is taking steps to recover outstanding revenue and strengthen contract performance. An initial auction of garment quotas for export to the United States was conducted in January 2002, and an additional auction is expected in July in line with the objective of increasing the proportion of quotas subject to auction to at least 20 percent. To support stronger enforcement activities for the use of state assets, a preliminary inventory covering 70–80 percent of all assets held by line ministries will be completed by end-June 2002. Finally, the revenue monitoring and reporting system for forestry will be strengthened as outlined in paragraph 20 below.

11. **The expenditure program for 2002 was designed to support the poverty reduction strategy and envisaged reforms in expenditure administration.** The government is committed to reorienting expenditure away from defense toward the priority social sectors, and to provide for a more even pattern of expenditure during the year. To meet this goal, the first steps to reform expenditure administration have been taken and further progress in the expenditure reform program will be made during the second semester. In particular, the National Treasury will prepare a report on the stock of outstanding payment orders by mid-July 2002. Based on this report, the cash management committee will ensure the necessary availability of cash. Accordingly, with effect from July 1, 2002 the issuance of government payment orders will be strictly limited to projected cash availability over the subsequent 4 weeks. To support this effort, the centralization of government accounting will be continued as outlined in Annex II. A working group has been established in the National Treasury to prepare a report on standardized accounting procedures and methodology for the public sector in line with international standards by end-October 2002. From January 1, 2002, government procurement was strengthened by applying the provisions of the 1995 decree (No. 60) on Public Procurement to acquisitions of goods, services, and construction activities, except for heavy capital investment in road, bridges, and sewerage construction in four key ministries (Health, Education, Agriculture, and Rural Development). The coverage of procurement procedures will be extended over time to other ministries in line with implementation capacity and cash availability.

12. **The 2003 budget, under preparation, envisages a further improvement in social spending while allowing for increased interest payments arising from the prospective completion of outstanding external debt rescheduling agreements.** A current surplus of about 1½ percent of GDP will be maintained and the overall deficit limited to available concessional assistance, with no domestic financing of the budget. A further improvement in revenue to about 13¼ percent of GDP will be targeted by extending recent improvements in tax and customs administration. In the context of the preparation of the 2003 budget, the Government will inform the IMF on any revenue enhancing measures that could be needed to meet further expenditure pressures. The expenditure program will target a slight increase in current expenditure to 11¾ percent of GDP, in part to address a significant increase in interest payments. The overall deficit is projected at about 5½ percent of GDP and will be

fully financed by concessional resources. The 2003 budget is being formulated within the context of a medium-term expenditure framework that will need to be further developed in the period ahead and linked with the PRSP process.

13. **Progress has been made moving forward with military demobilization and civil service reform.** After the receipt of financing already committed by the World Bank and other donors, and the completion of the delivery of the reintegration package for the first 15,000 discharged soldiers, the government intends to discharge the second group of 15,000 soldiers by end-2002. Implementation of a new salary system, based on the automated payroll, and initial selections for Priority Mission Groups (PMGs) have recently started. Owing to the implementation of the new system for remuneration and classification, the average salary of civil servants has increased by about 38 percent within the 2002 budget framework for civil administration. PMGs will start to be identified in June 2002, and are expected to include 500 people. These reforms are consistent with the agreed resource constraints provided for in the 2002 budget that provides for a maximum increase in the overall wage bill of 8½ percent, inclusive of contingency funds. In line with the medium term reform program, the size of the civil service will be kept constant with normal attrition used to offset any new hiring of teachers. The government and the World Bank have agreed on steps to be taken during 2002–03 to further articulate the next phases of the National Program of Administrative Reform with a view to improving civil service pay and ensuring that the size and the shape of the civil service are financially sustainable and meet organizational requirements. Future staff reductions will be based on a credible policy on social safety nets, to be developed by December 2002 and supported by donors.

14. **The monetary program for 2002 is consistent with growth and inflation objectives.** The program provided for money growth of 19 percent and an expansion of private credit of 13 percent. During the first quarter of 2002, the increase in net foreign assets was larger than programmed, reflecting buoyant foreign exchange inflows from the tourist sector. Reflecting these developments, adjustments to the monetary program have been made. Taking into account expected nonproject balance of payments support, the increase in net international reserves is targeted at $67 million, with broad money growth projected at 22 percent, and private credit growth at 15 percent.

15. **The Government will maintain a flexible exchange rate policy, with the spread between the official exchange and market rates limited to 1 percent.** The NBC will continue adhering to the established intervention policy of using any increased demand for the riel to bolster international reserves and not resisting downward pressure on the exchange rate, except in the event of temporary disorderly market conditions. The NBC will continue to gradually eliminate the spread with the market rate during periods of stability and will proceed gradually toward achieving full unification of the exchange rate.

16. **Trade reform is moving forward and progress has been made toward joining the WTO**. The Government is moving forward with the next phase of tariff restructuring. Taking into account technical assistance to be provided by the Fund, detailed plans for reducing the unweighted average tariff rate to below 15 percent will be completed by end-October 2002,

with implementation in 2003. Regarding accession to WTO, and in line with the Doha declaration, a second working party meeting was held in Geneva in February and a third round of discussions of government's replies to questions raised by other members is expected to take place in July. As part of the Government's poverty reduction strategy, plans for broader trade reform and for improving overall trade facilitation based on the Integrated Framework (IF) for trade are being developed, and will be reflected in the forthcoming Poverty Reduction Strategy Paper (PRSP).

17. **The Government has taken steps to advance discussions on outstanding debt issues with the Russian Federation and the United States.** In February, an official delegation held discussions with both creditors and the Paris Club secretariat. A technical team was subsequently sent to Washington D.C. to discuss documentation issues with the United States. As a result of these efforts, documentation to verify disbursements was transmitted to the Cambodian embassy in Washington in late March and was received in Cambodia on April 21, 2002, and has been under review. The Government also sent an official letter to Moscow to invite a delegation to Phnom Penh for further negotiations on rescheduling terms as well as verification of the outstanding debt amount. Pending reconciliation, the Government remains fully committed to resolving debt issues with a view to reaching agreement in 2002. The review of the documentation received from the United States is underway, and a report on the preliminary conclusions stemming from this review is expected to be completed by end-June, 2002. The Government will continue maintaining a prudent debt-management policy, and in this regard, will refrain from contracting or guaranteeing any nonconcessional debt. The terms of all external borrowing will be promptly reported to the IMF as outlined in the technical memorandum of understanding.

18. **The Government is maintaining the momentum of banking sector reform.** The bank relicensing program has been completed, and the liquidation of nonviable banks is proceeding. Guidelines and regulations for specialized banks have been finalized and will be published in the July 2002 quarterly bulletin of the NBC. With the support of technical assistance, bank supervision is being strengthened further as a new uniform chart of accounts for the banking system consistent with IAS will be finalized by end-July 2002 with implementation to begin thereafter; all banks will be using the new chart of accounts from January 2003. The adequacy and effectiveness of the existing prudential regulations have also been reviewed.

19. **The FTB reconciled most of the discrepancies in their accounts, but failed to achieve an unqualified audit of the 2001 accounts for technical reasons.** The external audit concluded that, notwithstanding the small qualification, FTB's 2001 accounts gave a true and fair view of its financial position. As the qualification was related to historical provisions that will not repeat itself, an unqualified audit of the March 2002 accounts was completed on June 19. As part of the restructuring process, the Ministry of Economy and Finance became the major shareholder in the bank in April 2002 by replacing bridge financing provided by the NBC with its own capital injection. Management assistance is

being provided by external consultants and it is intended that a public announcement to privatize the bank will be issued by end-November 2002.

20. **The Government has maintained a suspension on logging activity, but continues to experience difficulties in the monitoring of log transportation and overall forest crime monitoring.** The Forestry Law is expected to be debated by the National Assembly during the current session, which will end on August 12, 2002. Restructured concession agreements in line with sustainable practice, are still expected to be completed by end-September 2002, but further work will need to be accelerated as concessionaires have made only limited progress toward submitting management plans and inventory assessments that are fully in line with sustainable practice. In view of the need to upgrade the monitoring of previously cut logs, all log transportation by concessions has been suspended from midnight of May 23, 2002, and an internal audit of the transfer of royalties to the budget on logging that took place in 2001 has been conducted, and based on the audit report, remedial actions are being taken. The monitoring of the future transportation of logs by concessions will be improved with the adoption of a new system of log tracking using electronic monitoring through bar code devices expected to be in place by the next logging season (September 2002).

21. **The Government continues to pursue a governance and anti-corruption agenda.** Enhancing governance is important to meet fiscal objectives and sustain poverty reduction. The Governance Action Plan (GAP) has been broadly disseminated at the national and local levels, and an updated GAP is being prepared. The Consultative Group Meeting to be held in Phnom Penh during June 19–21, 2002 will be used to launch external consultation with stakeholders to finalize the revised GAP. The National Audit Authority is now operational and will complete a full report on the implementation of the 2001 budget by November 2002. In accordance with the IMF's safeguards assessment, an external audit of NBC's 2001 accounts was completed on June 19, 2002. The audit report and financial statements of the NBC for 2001 will be published as required by the IMF's safeguards procedures. NBC will also provide an update on the status of recommendations made by the audit report on the 2000 accounts.

22. **Program objectives will continue to be supported by broad-based technical assistance efforts.** As part of the annual review of the TCAP program, the Government produced an assessment report noting that the overall objectives of the program remain sound and that progress has been made. Following the recommendations made during the annual review, management of the program has been strengthened and the appointment of a new national program manager on a full time basis has been approved. To improve TCAP team coordination, monthly steering committee meetings will begin from July 2002.

23. **The upgrading of Cambodia's statistical framework is underway.** A new statistics law will be submitted to the Council of Ministers in the near future. Reflecting the Government's commitment to use the IMF's General Data Dissemination System (GDDS), Cambodia's metadata were posted for the first time on the GDDS site in March 2002. A new CPI for Phnom Penh with updated weights was published in February, and new national

accounts estimates through 2001 were released in May. Annual fiscal data are expected to submitted for publication in the *Government Finance Statistics Yearbook* by August, and the NBC will continue to publish economic and financial data in its monthly bulletin, and will publish banking regulations and other studies in a new quarterly bulletin to be introduced in July. Improvements in social data are also being undertaken in the context of the PRSP process.

24. **The Government is committed to finalize the full PRSP by October 2002.** A draft outline of the PRSP has been prepared, several workshops with NGOs and civil society have been held, and a national PRSP workshop took place during May 28–29. Under the leadership of the Council for Social Development (CSD), line ministries are now actively engaged in the process.

25. **The sixth and final review under the program is expected to be completed by end-February 2003.** It will focus primarily on improved revenue mobilization, budget implementation--including military demobilization and civil service reform, forestry and bank reforms, and progress in resolving outstanding external debt issues. Quantitative performance criteria through end-September 2002 for the sixth review include (Table 1): (i) a ceiling on net domestic assets of the NBC; (ii) a ceiling on net bank credit to the government; (iii) a ceiling on net domestic financing of the budget; (iv) a zero ceiling on publicly contracted or guaranteed nonconcessional foreign currency loans; and (v) a floor on net official international reserves of the NBC. Quantitative benchmarks and performance criteria for June-December have been adjusted slightly to take into account revisions to the targets for international reserves, and revised estimates of nonproject balance of payments and budget support. The only structural performance criterion to be evaluated in the sixth review is the issuance of the final report of the working group on standardized accounting procedures and methodology for the public sector by end-October 2002 (Table 2).

ANNEX I

Cambodia: Main Revenue Measures Affecting the 2002 Budget[2]

I. Revenue Measures Introduced in the First Semester of 2002

A. Tax Measures

- The coverage of the real regime was expanded to five additional provinces.
- The excise tax on beer was increased from 10 percent to 20 percent.
- Additional taxes on petroleum products—2 cents per liter for gasoline and 4 cents per liter for diesel—were introduced with effect from January 1, 2002.
- A joint review was carried out by the Tax Department and the Customs and Excise Department of all aspects of taxation of motorcycles and motorcycle parts. A full assessment report with policy options will be completed by June 28, 2002.

B. Nontax Measures

- In response to a joint assessment by the Ministry of Economy and Finance and the Ministry of Posts and Telecommunications in December 2001 on the contract for international gateway II, the government has concluded that some aspects of the contract have been implemented inappropriately and is taking steps to recover outstanding revenue and strengthen contract performance.
- A preliminary inventory, covering 70-80 percent of state assets held by line ministries, will be completed by end-June 2002.
- The share of garment quotas to be auctioned was increased from 10 percent to 20 percent.
- A contract revision with Sokha Hotel, the managing company for the Angkor monument complex, was signed on May 29, 2002.
- Royalty fees for casinos were increased based on estimated turnover.

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[2] This list provides an update and some revisions to the list of measures attached to the December 26, 2001 MEFP.

C. Tax and Customs Administration Improvements

- The Tax Department reviewed legislation to ensure that appropriate support for collection action exists.

- To ensure coordination between the Customs (CED) and Tax Departments, a Protocol for implementation of the Prakas issued on February 23, 2001 has been signed by the relevant department directors on June 6, 2002 to specify reporting relationships.

- An Inter-Ministerial Commission on anti-smuggling was established. Regular reports are being submitted to the Council of Ministers on the results of anti-smuggling operations with effect from June 2002.

- Anti-smuggling task forces were strengthened in Phnom Penh, and a comprehensive anti-smuggling strategy targeting key revenue sources, high risk items, and prime locations was endorsed by the government in May 2002.

II. Revenue Measures to be Introduced in the Second Semester of 2002

A. Tax Measures

- In response to an assessment report, changes in the taxation of domestically assembled motorcycles and motorcycle parts will be introduced taking into account provisions of the Law on Taxation and the proposed revisions to the Law on Investment.

B. Tax and Customs Administration Improvements

- Continuing to strengthen tax auditing strategies and capabilities.

- Collection action on companies with leases of state assets that are on arrears will be strengthened.

- After having identified the 100 accounts with the largest arrears, the Tax Department will finalize a report on performance on collecting arrears by end-July 2002, including an action plan with collection targets and reports on performance.

- In-depth examination of dutiable non-PSI consignments, and limiting reinspection of PSI consignments to no more than 10 percent, based on principles of risk management, with effect from July 1, 2002.

- An Intelligence Unit will be created in CED by end-July to report on anti-smuggling operations.

ANNEX II

Cambodia: Main Government Expenditure and Budget Management Measures in 2002

I. Expenditures Measures Introduced During the First Semester

- A Prakas was issued in January 2002 establishing a new cash management committee and detailing a specific format for cash management procedures to manage cash management and improve the coordination between the National Treasury and other MEF departments.

- The number of government deposit accounts was reduced in March 2002 by integrating revenue accounts held by line ministries into the Treasury single account.

- The NBC started reporting to the National Treasury transactions for all government accounts on a monthly basis including the following documents: a statistical statement on monthly transactions; the status of account balances, and an account statement of detailed transactions.

- Tax payments by transfer or check to the Treasury single account with NBC, especially for the large taxpayers, have been in effect since November 2001.

- Steps have been taken to strengthen internal auditing capabilities at the Ministry of Economy for key spending ministries.

- Budget preparation has been enhanced by placing the formulation of the 2003 budget circular within the context of a preliminary medium-term revenue and expenditure framework.

- Preparation of monthly cash plans consistent with the annual cash plan, and measuring performance against the monthly plans.

- A provisional report on the amount and composition of domestic debt managed by the National Treasury as of end-2001 was completed in January 2002. An updated version of the debt statement as of end-June 2002 will be completed by mid-July 2002.

II. Expenditures Measures to be Introduced During the Second Semester

- A final report on standardized accounting procedures and methodology for the public sector, in line with international standards will be submitted by end-October 2002. A revised chart of government accounts, based on the actual accounting system and meeting international standards, will be finalized by November, for implementation from January 1, 2003.

- As a first step toward unifying the public accounting system under the National Treasury, from July 1, 2002 accounting for the 8 U.S. dollar accounts managed by the Foreign Currency Unit of the Ministry of Economy and Finance will be centralized in the National Treasury. As a second step, by end-October this procedure of accounting centralization will be extended to all other government accounts held by ministries and public agencies in close cooperation with the National Treasury. The full consolidation of government accounts into the Treasury Single Account will be pursued in 2003.

- Devolution of limited budgetary authority for operations and maintenance expenditure for the Health and Education ministries will be introduced by January 1, 2003.

- Budgetary procedures will be strengthened for the ministries under the Priority Action Program (PAP) to meet the social expenditure targets set forth under the poverty alleviation strategy.

- A new financial framework for communes with the national and provincial treasuries has been developed. Implementation has started and is expected to be fully effective later in the year.

- Continued development of a medium-term expenditure framework (MTEF) linked to the national poverty reduction strategy.

Table 1. Cambodia: Quantitative Performance Criteria and Benchmarks, June 2002-December 2002

	2001	2002					
	End-Dec.	End-June		End-Sept. 1/		End-Dec.	
	Actual	Prog.	Rev. Prog.	Prog.	Rev. Prog.	Prog.	Rev. Prog.
	(Cumulative change from beginning of year)						
Net domestic assets of the central bank (in billions of riels) 2/3/	-1070	-26	-45	-28	-47	-10	-29
Net credit to the government from the banking system (in billions of riels) 3/4/	-75	-20	-20	-20	-20	0	0
Net domestic financing of the budget (in billions of riels) 3/	-23	-20	-62	-20	-81	0	-46
Contracting or guaranteeing of external debt by the public sector 4/							
Up to one-year maturity 5/	...	...	...	...	...	...	...
1-5 year's maturity	...	...	...	...	...	...	...
Medium-and long-term nonconcessional debt 6/	...	...	...	...	...	...	...
External payments arrears 7/	...	...	...	...	...	...	...
Net official international reserves (in millions of U.S. dollars) 8/	470	27	54	36	65	46	67
Memorandum items:							
Foreign currency budget / BOP support (in millions of U.S. dollars)	5	19	13	24	27	29	32
Total nonproject budget support (in billions of riels)	54	74	116	94	175	137	203
	(Stock at end of period)						
Net domestic assets of the central bank (in billions of riels)	-1,070	-1,096	-1,115	-1,098	-1,117	-1,080	-1,099
Net credit to the government from the banking system (in billions of riels)	-75	-95	-95	-95	-95	-75	-75
Net official international reserves (in millions of U.S. dollars)	470	497	524	506	535	516	537
	(At end of period)						
Exchange rate (riels per U.S. dollar, end of period)	3,900	3,900	3,900	3,900	3,900	3,900	3,900

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

1/ Performance criteria.

2/ Net domestic assets are defined as reserve money minus net foreign assets of the central bank, 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 adjusted upward (downward) by any shortfall (excess) in external nonproject budget support from the program estimates. The adjustments for shortfalls in nonproject budget support will not exceed $10 million.

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 $12 million.

7/ Continuous performance criterion.

8/ For purposes of verifying compliance with the program, the floor on net official international reserves will be adjusted downward (upward) by any shortfalls (excess) in external nonproject budget support from the program estimates. The adjustments for shortfalls in budget support will not exceed $10 million. Valuation effects on the stock of gold holdings are excluded, and gold holdings in 2001 and 2002 are evaluated at the end-December 2001 gold price.

Table 2. Cambodia: Structural Benchmarks and Performance Criteria to be Assessed During the Sixth Review

Policy Action	Program Monitoring
1. Identify the 100 largest accounts in the tax department that are in arrears, complete an analysis of the arrears, and establish an action plan with collection targets and reports on performance. The first report to be completed by end-July 2002.	Structural benchmark
2. Pursue further centralization of accounting in the National Treasury by end-October as defined in the technical memorandum of understanding.	Structural benchmark
3. Finalize a new chart of accounts for fully licensed commercial banks based on international standards and begin implementation by end-July 2002.	Structural benchmark
4. Issue final report of the working group in the National Treasury on standardized accounting procedures and methodology for the public sector in line with international standards by October 2002.	Structural performance criterion
5. Taking into account technical assistance recommendations, complete proposal for the next stage of tariff restructuring to reduce the unweighted average rate to below 15 percent by end-October 2002.	Structural benchmark
6. Initiate privatization of the Foreign Trade Bank by issuing a public notice by end-November 2002.	Structural benchmark

Cambodia: Technical Memorandum of Understanding

This memorandum sets out the understandings between the Cambodian authorities and the IMF staff regarding the definitions of the quantitative performance criteria and benchmarks for the program supported by the Poverty Reduction and Growth Facility (PRGF), and the related reporting system of monetary and financial data.

1. **Net official international reserves of the National Bank of Cambodia** (NIR*) is defined as the unencumbered (i.e., readily available) gross official reserves of the National Bank of Cambodia (NBC) less foreign liabilities of the NBC. Under the program, the floor for NIR* will be: (i) decreased (increased) by the amount of a shortfall (excess) in external nonproject support from program estimates—any downward adjustment would not exceed $10 million; and (ii) decreased by any foreign-currency costs associated with bank restructuring. For purposes of monitoring performance against the program target for NIR, valuation effects on the stock of gold holdings will be excluded, and gold holdings will be evaluated at the gold price in effect on December 31st of the previous year[3]. Similarly, the level of foreign assets and liabilities will be evaluated at the U.S. dollar/SDR exchange rate in effect on December 31st of the previous year. NIR* data will be transmitted to the IMF weekly with a lag of no more than one week.

2. **Net Domestic Assets of the National Bank of Cambodia** (NDA*) are defined as reserve money minus net foreign assets of the NBC, adjusted for valuation changes arising from the difference between the program and the actual exchange rates. Reserve money is defined as the sum of notes and coins issued by the NBC, excluding NBC holdings of currency, and deposits of commercial banks and domestic nongovernmental sectors at the NBC. Reserve money excludes all NBC securities. The program ceilings for NDA* will be adjusted upward (downward) for any shortfall (excess) in nonproject external budgetary support from program estimates—any upward adjustment will not exceed $10 million. The ceilings will also be adjusted upward for costs associated with bank restructuring. NDA* data will be transmitted monthly within four weeks.

3. **Net credit to the government from the banking system** (NCG) is defined as claims on the general government by the banking system less deposits of the general government with the banking system. General government is defined to include central government, provinces, and communes. The program ceilings for NCG will be adjusted upward (downward) for any shortfall (excess) in nonproject external budgetary support from program estimates—any upward adjustment would not exceed $10 million. NCG data (as reflected in the monetary survey) will be transmitted monthly within four weeks.

4. **Net domestic financing of the budget** (NDF) is defined as the sum of NCG and any nonbank financing of the general government. The program ceilings for NDF will be

[3] For example, gold holdings in 2002 will be evaluated at the end-December 2001 gold price.

adjusted upward (downward) for any shortfall (excess) in nonproject external budgetary support from program assumptions—any upward adjustment would not exceed $10 million. For purposes of program monitoring, actual levels of NDF will not include any flows associated with "outstanding operations" (committed spending that has not yet been executed) or any "exchange rate adjustment" (valuation effects on government deposits from exchange rate fluctuations). Details on all transactions associated with outstanding operations and exchange rate adjustment will be reported at all test dates. For purposes of program monitoring, any accumulation of domestic payments arrears will be included as part of NDF. NDF data (as reflected in the consolidated report on government operations (TOFE) table) will be transmitted monthly within four weeks.

5. **The contracting or guaranteeing of external debt by the public sector** is defined as foreign currency borrowing contracted or guaranteed by the public sector in Cambodia. Public sector is defined to include the Royal Government of Cambodia, the NBC, publicly-owned enterprises, local governments, or any other agency acting on behalf of the government. The program has ceilings for all debt below five years maturity and all nonconcessional debt for maturities beyond five years (both ceilings are set at zero). The coverage of debt includes financial leases and other instruments giving rise to external liabilities on nonconcessional terms.[4] Details on any such borrowing should be reported within three weeks. Nonconcessional debt is defined as a debt with a grant element (NPV discount relative to face value) of less than 35 percent, based on the currency- and maturity-specific discount rates reported by the OECD (commercial interest reference rates).

6. **External payments arrears** are defined as the stock of external arrears on loans contracted or guaranteed by the public sector (as defined above), excluding debts subject to rescheduling or debt forgiveness.

7. To adhere to **the structural performance criteria** for the sixth review, a final report on standardized accounting procedures and methodology for the public sector in line with international standards will be issued by end-October 2002.

8. **The structural benchmark on government accounting** for end-October 2002 will involve the centralization of accounting in the National Treasury of the 8 U.S. dollar accounts managed by the Foreign Currency Unit, and all other government accounts held by ministries and public agencies.

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[4] This performance criterion applies not only to debt as defined in point No. 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt (August 24, 2000) but also to commitments contracted or guaranteed for which value has not been received. Excluded from this performance criterion are amounts contracted under the government loan agreement with China, dated July 26, 2000, for a maximum loan amount equivalent to $12 million. For purposes of program monitoring, the ceilings on external debt also exclude normal short-term trade-related credits and any borrowing associated with debt rescheduling.

Summary of data reporting requirements

(i) Data on daily average selling and buying exchange rates (official and market rates) to be transmitted daily.

(ii) NIR* to be transmitted weekly with a lag of one week.

(iii) Monetary survey and consolidated balance sheets of the NBC and commercial banks to be transmitted monthly within four weeks.

(iv) Consolidated report of government operations (TOFE) to be transmitted monthly within four weeks.

(v) CPI data to be transmitted monthly within five weeks.

(vi) Flash report of NBC accounts to be transmitted weekly within one week.

(vii) Trade data to be transmitted monthly within ten weeks.

(viii) Any publicly contracted or guaranteed nonconcessional borrowing to be transmitted within three weeks.

(ix) Any external payments arrears to be transmitted monthly within three weeks.

INTERNATIONAL MONETARY FUND

NEWS BRIEF

FOR IMMEDIATE RELEASE

News Brief No. 02/71
FOR IMMEDIATE RELEASE
July 22, 2002

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Completes Fifth Review of Cambodia's PRGF Program and Approves US$11.2 Million Credit

The Executive Board of the International Monetary Fund (IMF) today completed the fifth review of Cambodia's economic performance under the Poverty Reduction and Growth Facility (PRGF) arrangement. This enables the immediate release of a further SDR 8.4 million (about US$11.2 million) from the arrangement, which would bring total disbursements under the IMF-supported program to SDR 50.1 million (about US$ 67.3 million).

Cambodia's arrangement was approved on October 22, 1999, in a total amount equivalent to SDR 58.5 million (about US$78.5 million—see Press Release 99/51).

The PRGF is the IMF's concessional facility for low-income countries. 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. 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.

EXTERNAL RELATIONS DEPARTMENT
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After the IMF Executive Board's discussion, Eduardo Aninat, Deputy Managing Director and Acting Chairman, made the following statement:

"The Cambodian authorities have continued to make good progress in implementing their economic reform program. Inflation remains low and economic growth is being sustained despite a weaker external environment. Progress in the implementation of structural reforms has also been broadly satisfactory, but reform efforts need to be strengthened in key areas, particularly revenue administration, public expenditure management, forestry policy, and civil service reform. Further improvements in governance are also key to meeting program objectives. To minimize the program's vulnerability, it is important that technical assistance be adequate, well coordinated, and well used to build capacity in all levels of government.

"The PRGF-supported program continues to concentrate on a reorientation of fiscal policy. To achieve the revenue targets, strong action is needed to improve tax and customs administration and nontax revenue collection. Enhancing cash management and overall budget execution is also required. To maintain overall financial stability, domestic financing of the budget should continue to be avoided and fiscal decentralization implemented gradually to maintain effective control of overall spending.

"Faster progress in several areas of structural reform would help sustain growth and further reduce poverty. Completing the restructuring of the Foreign Trade Bank and enhancing bank supervision will be important for promoting the sound development of the financial system, while completing the military demobilization by end-2002 will facilitate continued shifting of expenditure away from defense. Civil service reform must be accelerated to improve the efficiency of public service delivery, and further legal and judicial reform is required to improve the investment environment. In addition, it will be important to achieve a sustainable forestry policy, including the adoption of community forestry practices to improve the standard of living of the rural poor. Deepening trade reform and reducing trade facilitation costs will enhance growth prospects. In this regard, the PRSP, expected to be completed by end-October 2002, should highlight the links between trade and poverty reduction.

"Donor support and debt relief will continue to be crucial to determine the program's success. Accordingly, it is important that the authorities and Cambodia's main bilateral creditors continue their good faith efforts to complete outstanding debt rescheduling agreements in the near future, on concessional terms consistent with Cambodia's fiscal constraints. Moreover, nonconcessional borrowing should continue to be avoided," Mr. Aninat said.

Statement by Dono Iskandar Djojosubroto, Executive Director and Tola May, Assistant to the Executive Director for Cambodia
July 22, 2002

Key points:

- *All quantitative and structural performance criteria for the fifth review of the PRGF program was successfully met, except for one structural performance criterion relating to the completion of an unqualified audit of the Foreign Trade Bank. Given that the condition was met with only a slight delay, and the overall progress in restructuring the bank, the authorities believe that their request for a waiver for the missed performance criterion can be justified.*
- *The PRGF program is in its third year and the Cambodian economy continues to perform well with macroeconomic stability providing a sound basis for sustainable and strong growth.*
- *Substantial progress in structural reforms has been achieved and the authorities are committed to keep up the momentum despite significant capacity constraints and a still fragile but stable political situation. Greater attention would have to be focused on reforms of the legal and judiciary systems, forestry management and governance.*
- *Preparation of the full PRSP is progressing with completion scheduled for October 2002.*
- *Debt resolution is in progress. To sustain its ongoing efforts in poverty reduction, Cambodia needs to restructure its bilateral debts on highly concessional terms in view of its limited fiscal capacity.*

Introduction

On behalf of the Cambodian authorities, we would like to thank staff and Management for their advice and guidance as well as the Board for their continued support of the PRGF program. The authorities would also like to express their gratitude to their development partners for their broad support to strengthen Cambodia's efforts in reducing poverty and improving governance at the recent Consultative Group Meeting in Phnom Penh (June 19-21, 2002). The authorities are committed to strengthen their efforts to implement their reform program and particular attention will be paid to legal and judicial reforms, social sector spending, tax and customs administration, management of natural resources, and private sector development.

Reform measures for the fifth review under the PRGF program have been successfully implemented. With macroeconomic stability established and substantial progress made in structural reforms, economic growth continued while advances in poverty reduction and economic reconstruction were achieved. All quantitative and structural performance criteria for the fifth review were met, except the performance criterion for end-May 2002 relating to the completion of an unqualified audit of the 2001 accounts of the Foreign Trade Bank. Due to technical reasons, this was observed with a slight delay and the authorities are requesting a waiver for missing this performance criterion.

To comply with the policy on safeguarding the Fund's resources, an audit of the 2001 accounts of the National Bank of Cambodia (NBC) has been completed by an international audit firm, and the results of the audit along with the financial statements will be published.

Macroeconomic Developments

In 2001, real GDP growth reached 6.3 percent, higher than the program target, due to strong garment exports in the first half of the year and sustained growth in tourist arrivals. The Cambodian economy continues to perform well in the first half of 2002. Inflation remains subdued, the exchange rate was stable, and official reserves have been gradually built up, reaching US$623 million or 3½ months of imports as of July 12. The increased tourist receipts coupled with the expected gradual recovery in external demand for garments in the second half of 2002 and improved agricultural production will help sustain growth at 4.5 to 5.5 percent in 2002. The medium term economic growth prospect therefore looks favorable, although the sources of growth will need to be diversified beyond the garment and tourism sectors.

Fiscal Policy and Reforms

To support the pro-poor fiscal policy, the authorities plan to increase priority spending for the social sector to 3.7 percent of GDP in 2002 from 3.2 percent in 2001. In this respect, the revenue target for fiscal year 2002 has been set at 12.8 percent of GDP, about a percentage point higher than the 2001 revenue performance. The current budget surplus will be increased slightly to 1.3 percent of GDP and the fiscal deficit contained at less than 6 percent of GDP. To meet the revenue target, the government will vigorously implement the 2002 fiscal measures, focusing particularly on enhancing anti-smuggling efforts and collection of non-tax revenue from telecommunication and tourism services as well as from the lease of public assets. In the meantime, the expenditure process will be improved, including further strengthening cash management efforts. These efforts have produced encouraging results in the first four months of 2002, with revenue collection and the pace of expenditure spending showing signs of improvement. However, the authorities recognize that a more prudent monitoring process has to be put in place to ensure that the annual targets are achieved comfortably.

With TCAP technical assistance, reforms in the Tax as well as Customs and Excise Departments, with respect to both their administration and operations, will be further deepened as planned. A comprehensive reform strategy for public expenditure management covering expenditure control, cash management, treasury reforms, and standardization of accounting and fiscal reporting systems is being developed.

Financial Sector Reforms

After over two years of comprehensive review, the NBC has completed its bank re-licensing process. Of the 13 banks which operated under the Memoranda of Understanding (MOUs), only three banks failed to meet the licensing requirements and were closed, raising the total number of banks closed to 15. The remaining ten banks were issued new banking licenses, raising the total number of licensed banks to 14, but one of these banks recently downgraded its operations to a representative office while another will be voluntary liquidated. In addition, four banks were granted licenses to operate as specialized banks under the new NBC guidelines and regulations. The NBC is continuing to restructure the banking sector in accordance with the blueprint for financial sector development drawn up with the assistance of the Asian Development Bank. Under this blueprint, strengthening banking supervisory capacity is one of the key objectives and a new set of prudential regulations has since been adopted. Further improvements in surveillance and inspection procedures, risk assessments and prompt corrective action systems, prudential regulations on risk management and risk control as well as anti-money laundering regulations are expected to be completed by September 2002. A standardized accounting system for the banking sector, which will be in line with the International Accounting Standard, is expected to be implemented in January 2003. In addition, to establish a modern payment system in Cambodia, the draft law on negotiable instruments and payment transactions has been completed and submitted to the Council of Ministers in June 2002.

The restructuring of the Foreign Trade Bank (FTB) has been further advanced. The new reorganization plan established with the assistance of experts from Australia is being implemented. The Ministry of Economy and Finance (MEF) has already issued government bonds to replace the bridge financing provided by NBC in FTB's capital base. Accordingly, the MEF will soon appoint their representatives on FTB's Board of Directors to replace the members from NBC. The Board will speed up the restructuring process in order to upgrade the bank's management and prepare it for eventual privatization.

Governance Action Plan

The recent Consultative Group Meeting in Phnom Penh has emphasized some key issues on governance for the greater interest of Cambodia. These issues coincide with the already established Governance Action Plan (GAP) that is meant to enhance good governance as a prerequisite for sustainable socio-economic development and social justice in Cambodia. While substantial satisfactory outcomes have already been achieved in many areas, greater vigilance will be needed in legal and judicial reforms, civil service and administration reforms, forestry reforms, and measures to combat corruption. As part of the GAP framework, the National Audit Authority (NAA) has been established and began operations in early 2002. The NAA will soon conclude its first audits of public revenues and expenditures at the MEF for fiscal year 2001 in order to improve transparency and accountability.

Forestry Policy

The authorities have taken decisive actions since the end of 2001 to strengthen forestry management. Further to the suspension of logging activities with effect from January 2002, the ban on log transportation was put into effect from May 23, and the license of a company, which violated the forestry regulations, was withdrawn in June 2002. Financial control of forestry revenues has also been strengthened, and legal action is being taken against a logging company for irregularities in their claims for refund of royalties from the government. The government remains committed to completing restructuring agreements or cancel further concessions of logging companies following the completion of the evaluation of their management plans and environmental impact assessments. In addition, to preserve the country's natural resources, the government has designated additional protected areas in different parts of the country. In June 2002, about 400,000 hectares of forest were withdrawn from concession companies and designated conservation areas for trees and wildlife.

Civil Service Reform and Military Demobilization

As part of the first phase of the civil service reform strategy, following the registration of all civil servants and the adoption of the nationwide computerized payroll system, the government moved to a new remuneration system that provided for an increase in the average salary by about 38 percent, in line with fiscal limits in the 2002 budget. A new job classification system was introduced and the selection of Priority Mission Groups and payment of incentives will be implemented in the second half of 2002. In the period ahead, the size of the civil service will be broadly maintained at the current level with normal attrition offsetting the recruitment of new teachers. The next phase of the reform strategy will be carried out after the national elections to be held in the second half of 2003. In this connection, assisted by the World Bank, the authorities will undertake studies on the labor market, the design of a social safety net, possible financing options and a functional analysis. With regard to military demobilization, the discharge of another 15,000 soldiers is expected to begin by end-2002, completing the process of discharging a total of 30,000 soldiers.

Poverty Reduction Strategy Papers

With improved coordination among all stakeholders, a national workshop was held in May 2002 with broad participation to discuss the draft of the PRSP outline and sectoral matrices prepared by line ministries. In the meantime, the design of poverty assessments and monitoring frameworks, medium-term policy actions and the linkages between trade policy and poverty reduction are in progress. All these efforts are in support of meeting the schedule to complete the full PRSP by October 2002.

Debt Resolution

The Cambodian authorities have continued their efforts to seek a resolution to its outstanding debts to bilateral creditors. A Cambodian delegation led by the Senior Minister, Minister of Economy and Finance visited Washington DC on February 19-20, 2002 and held discussions with the US Treasury and State Departments. A month later, a Cambodian technical team followed-up with a visit on March 19-20 to obtain the relevant documentation from the US Department of Agriculture. With the assistance of their US counterparts, the documents were delivered to Cambodia in April 2002. A preliminary finding by the authorities has been sent to the US authorities in early July 2002, and it is hoped that a team from the US could visit Phnom Penh in the near future to discuss the reconciliation of the outstanding debt, as a step towards negotiating a debt rescheduling.

With regard to the outstanding debt to Russia, as a follow-up to the earlier discussions, on February 21, 2002, a Cambodian technical team visited Moscow to discuss the remaining issues with their Russian counterparts. The Russian team followed up with a visit to Phnom Penh from 24 to 28 June 2002. Both parties have agreed to meet again in Moscow to find an appropriate resolution that would take account of Cambodia's limited fiscal position and allow Cambodia to continue to meet its other developing expenditure needs.

In order to sustain the momentum of its reform program to reduce poverty and overcome the setbacks from its past history, Cambodia has to overcome two main obstacles—human resource constraints and its high outstanding bilateral debt. The first obstacle is being resolved under the current TCAP-supported program. As for the second obstacle, the government of Cambodia has strong political will to find a satisfactory resolution to its financial obligations to all its creditors. It has concluded successive agreements with many creditors, and would like to conclude the negotiations with the United States and the Russian Federation, as soon as possible. However, Cambodia's fiscal position remains weak and it needs to dedicate substantial resources to the priority areas under the poverty reduction program in the years ahead. In this context, completing debt rescheduling agreements on highly concessional terms will facilitate meeting the twin objectives of poverty reduction and debt resolution as noted by Executive Directors during the last Board meeting on Cambodia in February.

Conclusion

Over the last three years of peace and political stability, Cambodia's performance in socio-economic development has been remarkable. The authorities have demonstrated a strong commitment to accelerate the speed of poverty reduction through advancing further the reform program despite its significant capacity constraints and the still fragile political situation. They are grateful for the technical and financial assistance they have received from various development partners and will devote these resources to the benefit of the country and its people.