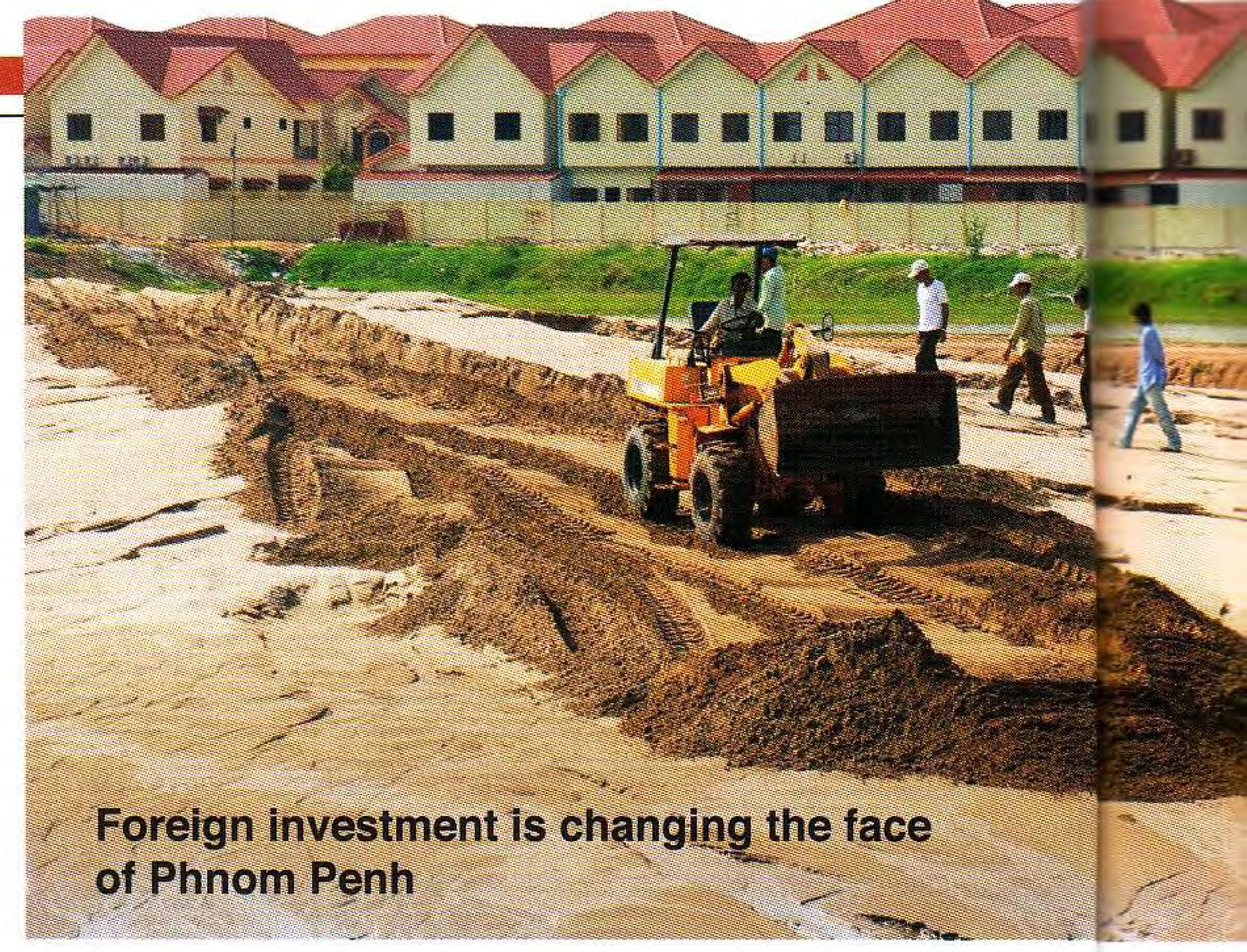


Foreign investment is changing the face of Phnom Penh

INVESTMENT

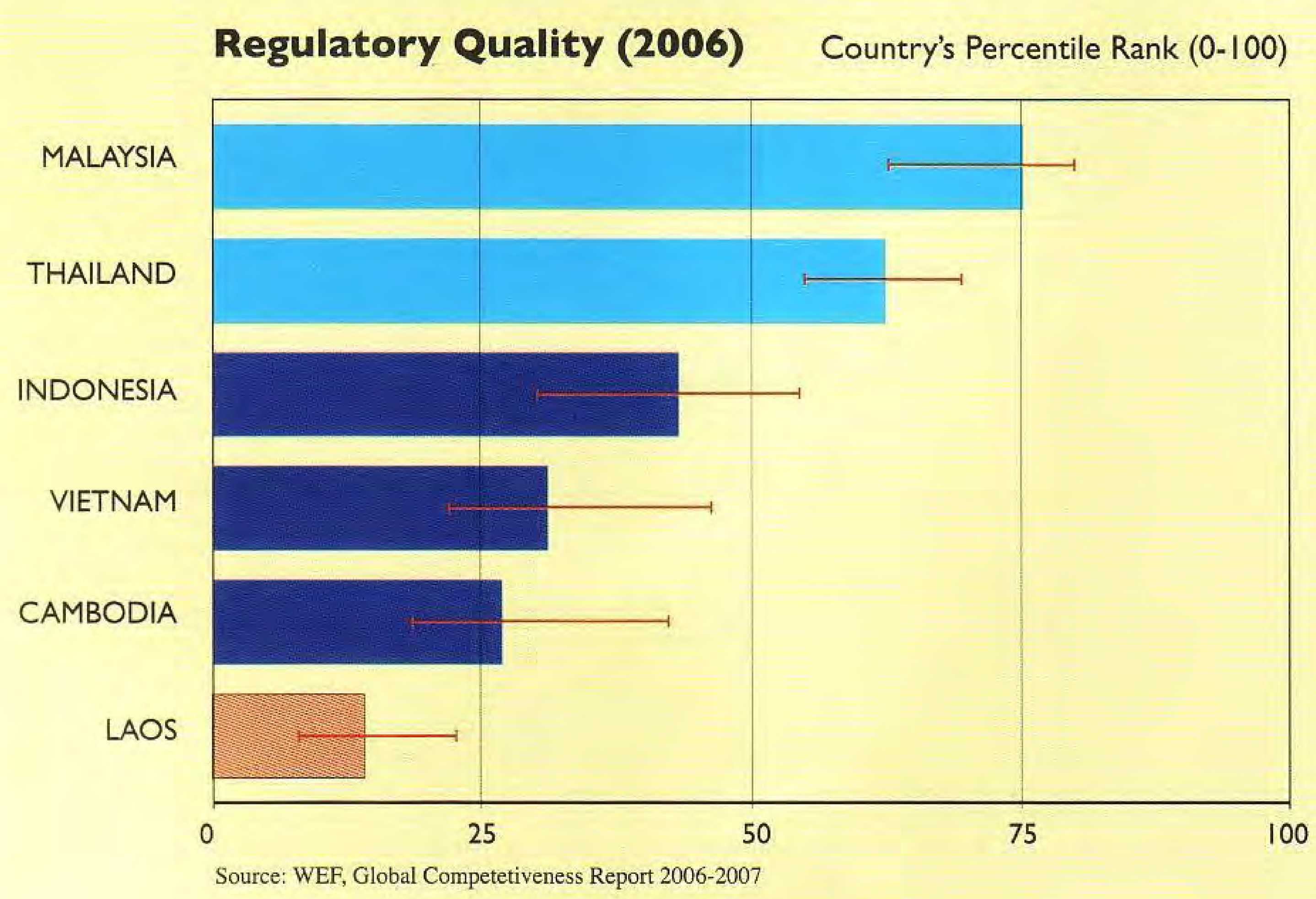
Climate changed

Cambodia is becoming an increasingly attractive alternative for foreign funds

Standing on the toes of neighbouring economic giants, Cambodia's nascent investment climate is attracting record levels of Foreign Direct Investment (FDI) thanks to its open business environment and newfound political stability, say the World Bank and local investment chiefs. The optimism comes despite a recent study by business intelligence group Stratfor suggesting corrupt judicial and regulatory systems will continue to prevent all but the most speculative international firms from injecting capital into the kingdom. "In Cambodia there are positives - government rhetoric is pro and not anti-foreign business, the country has abundant natural resources and foreign investors may well soon need additional sites apart from China, Vietnam or Thailand - Cambodia could their be third or fourth alternative," an author of Stratfor's 'Cambodia: Flaws in the Investment Picture' told **SE GLOBE**. But until critical legislation protecting profits, ownership and property rights are approved and implemented, firms will continue to turn to regional competitors, she added.

Cambodia's strategic positioning between established regional powerhouse, Thailand, and flourishing Vietnam, lends it the perfect opportunity to serve as a bridge between the two. However, concerns about political freedoms and a host of environmental and human rights issues may keep western investors away for fear of a public image disaster, claim the authors of Stratfor's study. They go on to say that the FDI in Cambodia is limited to a narrow base of garments and tourism, and suffers from "lengthy, costly and unclear arbitration systems [which] plague business activities nationwide."

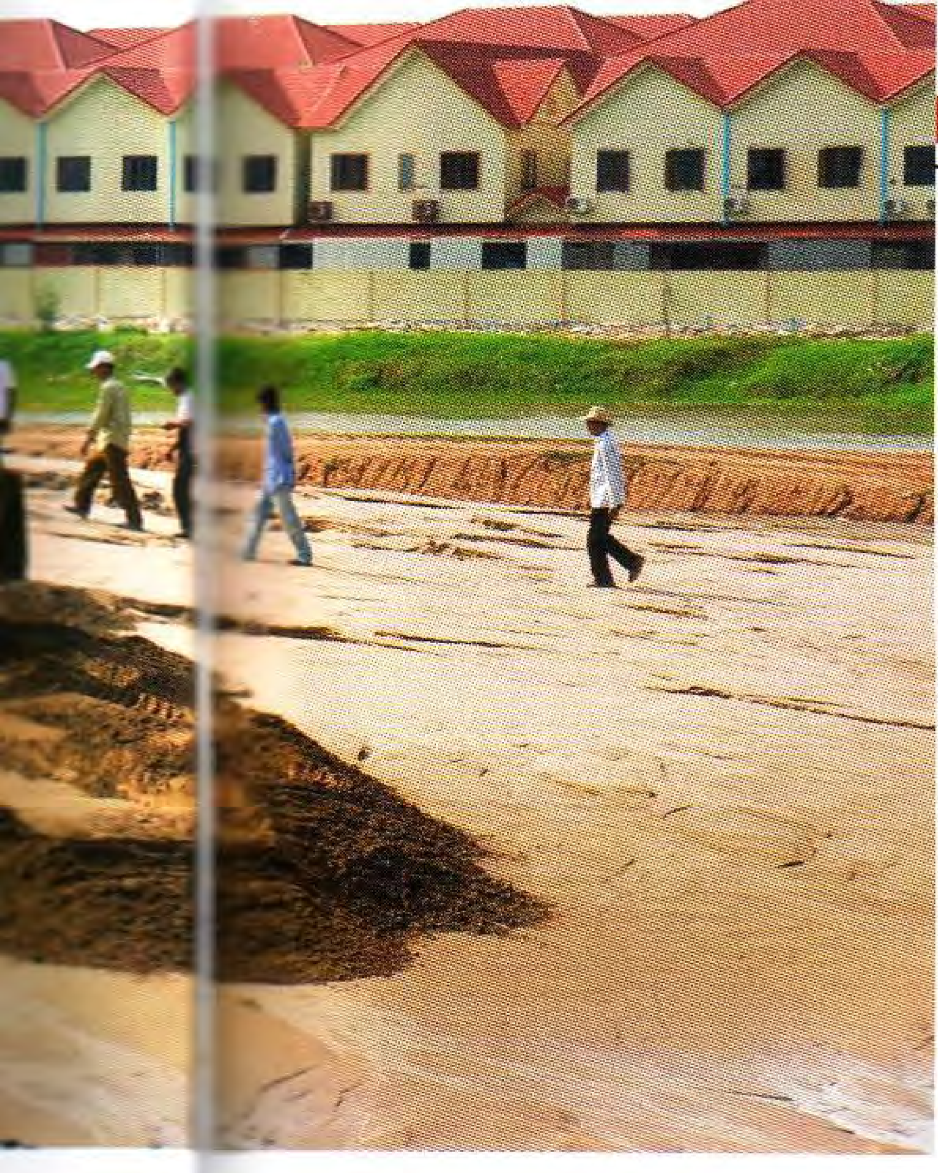
The first impressions may confuse some. A visit to the website of the Cambodian Investment Board - the Council for the



Source: WEF, Global Competetiveness Report 2006-2007

One aspect of Cambodian governance that is not on the upturn is the regulatory quality of government institutions. Not only does the country rank below most of its neighbours, but it has seen its percentile ranking in this area fall by almost half since surveys in 1998 and 2002. Given the somewhat subjective methods of judgement used by the World Economic Forum, the red line indicates possible margins of error.

Though arguments persist as to whether WTO membership is to be thanked for recent FDI climbs, it cannot be denied things are getting better. From 2000 to 2004, FDI languished in the doldrums with a mere $61 million in 2003. 2006 saw real FDI reach nearly $500 million.



Vietnam is providing serious competition to Cambodia's textile and shoe industries

Development of Cambodia's (CDC) 'one-stop shop' for private sector development - lists dead links, phone lines that ring-off and email addresses that bounce. To be fair, an economy that suffered the rigours of the Khmer Rouge needs time to redevelop, but for how long is the country's business environment expected to remain under construction?

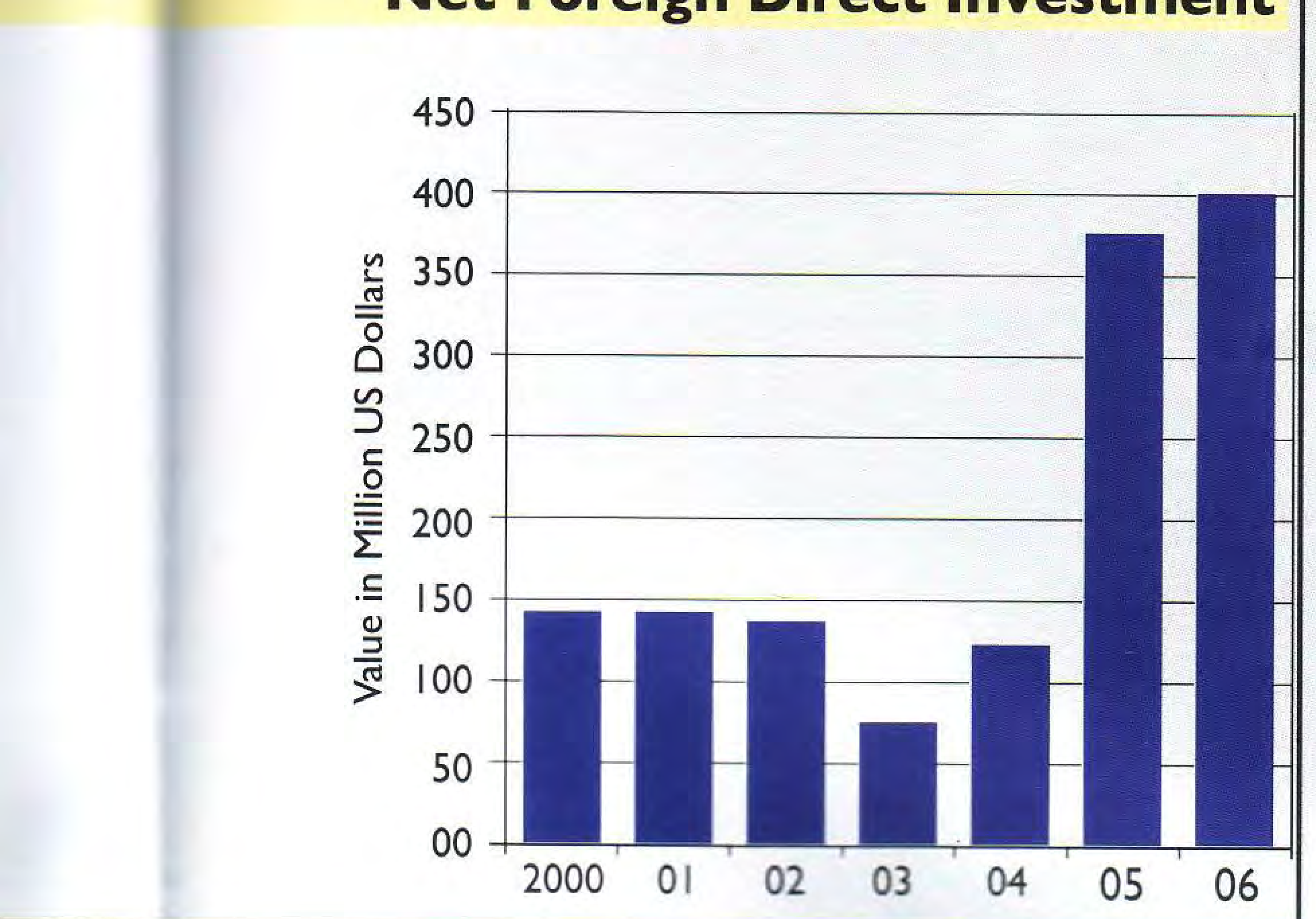
So, what other factors limit the appeal of a nation forced to rebuild its economy from year zero? FDI had fluctuated at low levels since the regional economic crisis and internal strife of 1997, falling to $61 million in 2003 from $129 million in 2002. In an effort to catch up, Cambodia joined the World Trade Organization (WTO) in 2004 as a least-developed country - granting it some economic and international legitimacy. But while corruption, political instability and a turbulent history are still often cited as deterrents, far less emotive issues such as expensive utilities, a lack of a developed infrastructure, a highly restrictive labour market, and costly start-up procedures are more practical limitations.

Cambodian infrastructure continues to suffer from the ravages of its three-decade long civil war. In the 2006 World Economic Forum (WEF) Business Competitiveness Survey, 68% of interviewees considered high operating costs presented by the nation's debilitated rail network, postal system and telecoms sector as severely limiting factors. Only 12% of the population have access to public electricity. Those that do have access, use one of the costliest networks in the world, with tariffs in Phnom Penh and the provinces sometimes reaching 30 to 90 cents/kWh - over 65% more expensive than electricity provided to Vietnam.

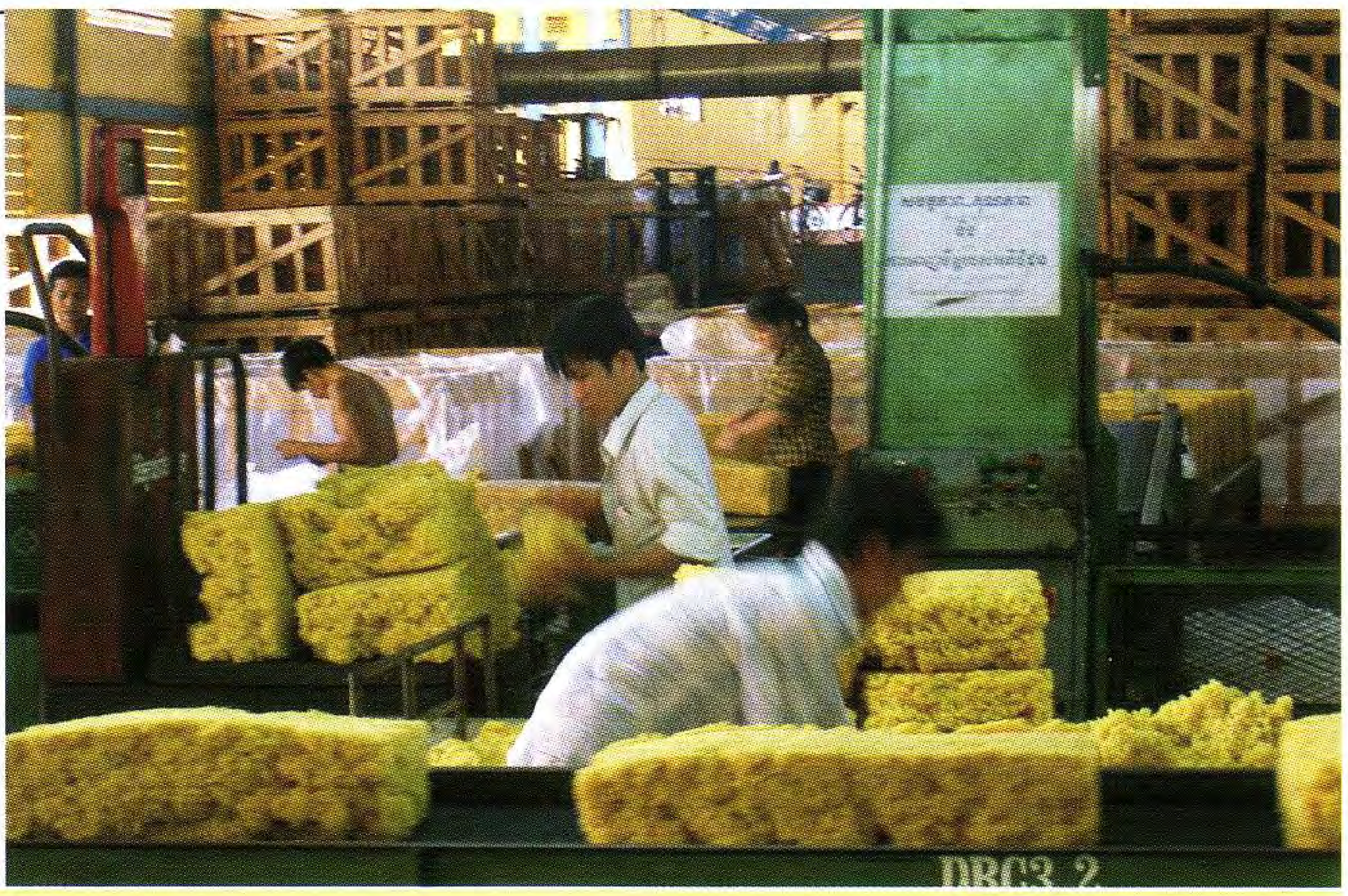
In the International Finance Corporation (IFC) report "Doing Business in 2007 – how to reform" Cambodia dropped a place from the previous year, ranking 143 out of 175 countries in terms of the ease of doing business. Though ranking well in terms of taxation, cumbersome start-up measures remained the greatest obstacle. To start a business here there are 10 procedures to go through, and a required waiting period of 86 days. This compares to 8 procedures and only 33 working days in Thailand, 11 procedures and 50 days in Vietnam, and 9 procedures and a mere 30 days in Malaysia. World Bank lead economist for Cambodia, Dr Kazi Matin, says, "This shows that the formal private sector in Cambodia faces myriad transaction costs and barriers to establishment and operation."

Southeast Asia is awash with flagrant breaches of Intellectual Property Rights (IPR), and Cambodia is no exception. From Ferrero Rocher to pharmaceuticals almost nothing is sacred. During a recent visit, Peter N. Fowler, the Senior Counsel of the US Patent and Trademark Office warned the Cambodian government that without strong IPR laws and their proper enforcement, large US firms will continue to ignore Cambodia. At the same time, he pointed out how Vietnam has successfully enforced its own anti-corruption laws,

Net Foreign Direct Investment



Construction and the property market are growing faster than the rest of the economy



Major targets for investment have been the textile industry (above) and rubber production (right)

punishing several leading officials for illicit activities. The general message was that Cambodia would do well to follow the Vietnamese role model. Vietnam now expects FDI to breach $20 billion in 2007, according to figures announced by the Vietnamese Foreign Investment Agency in late June. In the first six months of this year alone, $5.2 billion in FDI has been plugged into the country through 575 foreign-invested projects - an increase of nearly 70% in volume and 6.4% in value from 2006.

Other Southeast Asian nations are also no slouches in the search for foreign funds. Despite a lower ranking in the WEF index, Malaysia outstripped Thailand in FDI last year, luring nearly $60 billion to Thailand's $32 billion, according to the Malaysian International Trade and Industry parliamentary secretary Tan Yee Kew.

But there are positives for the country. FDI inflow to Cambodia continued its upward trend in 2006, according to a recent World Bank report, reaching a record high of $475 million in 2006, a 21% increase over the previous year's figures. The nation's current account deficit declined by over 7%, and Gross International Reserves expanded by 20% to $1.1 billion. "Increasing FDI is expected to be sustained and the discovery of offshore oil and gas reserves will likely bring about even higher growth," said the World Bank.

The CDC approved 74 investment projects in Cambodia in the first 9 months of 2006, representing about $1 billion worth of fixed assets. Larger projects include the Green Sea Agriculture project worth $141 million, the Cambodia Cement Chakrey Ting Factory project with $132 million of fixed assets, and the Sinohydro Kamchay Hydroelectric project with $170 million. The figure does not include the $2 billion Camko City development now under construction, nor the $2 billion concessionary agreement that the Cambodian government entered into with Australian mining group BHP Billiton in October 2006.

Projects on the cards this year include JSM Indochina's $35 million investment in shopping malls and apartment complexes in Phnom Penh. American International Data Group (IDG), a leading technology, media and research company, plans to invest about $100 million into burgeoning IT companies, to give this sector some much-needed impetus. In addition, CVI Resorts of Malaysia plans to input another $100 million in a five-star hotel, golf course and entertainment complex on 130 hectares of land in Svay Rieng province alongside the Cambodian-Vietnamese border. Malaysian companies consider the flexibility of doing business in Cambodia and the pro-business attitude of the Cambodian government towards investors as great positives, according to Teh Sing, the president of the Malaysian Business Council of Cambodia (MBCC), who adds, "a young and cheap labour force is another factor. As for the negative feelings, these are mainly towards the evolving laws of the country."

"Booming", in a word, is how Brett Scianori, president of the Cambodian-American Business Council describes the investment environment in Cambodia. Speaking to **SE GLOBE**, Scianori said that as Cambodia's secure microfinance numbers and its GDP have been hovering around double digits for the last few years - second only to China in Southeast Asia - the nation is finally able to broaden its investment base. "Cement in Kampot, minerals and mining resources throughout the provinces, and the continued interest in telecoms, banking and bio-diesel are remarkable prospects to have in the pocket of nation in only its third electoral mandate," said Scianori.

The recent plan by Philadelphia-based Crown Cork, the US's second-largest can manufacturer to build a sizeable factory in the country, may also signify

Countries' Ranks of the Nine Pillars in the Global Competitiveness Index 2006-2007

	Cambodia	China	Indonesia	Thailand	Vietnam
GCI 2006	103	54	50	35	77
Basic Requirements	100	44	68	38	71
1-Institutions	95	80	52	40	74
2-Infrastructure	97	60	89	38	83
3-Macroeconomy	101	6	57	28	53
4-Health & Primary Education	98	55	72	84	56
Efficiency Enhancers	110	71	50	43	83
5-Higher education & training	110	77	55	42	90
6-Market efficiency	99	56	27	31	73
7-Technological readiness	105	75	72	48	85
Innovation Factors	102	57	41	36	81
8-Business sophistication	100	69	42	40	86
9-Innovation	98	46	37	33	75

Source: WEF, Global Competitiveness Report 2006-2007

Cambodia ranks far behind its Southeast Asian neighbours and China in terms of overall competitiveness, and on the face of it is an unlikely choice for foreign investment. The positives are the progress made from starting the economy from all but zero, and the present government's open-minded business environment. Training and the development of technology are areas requiring special attention.

Photos: N. Dickinson for SE GLOBE; E. Bara

INFRASTRUCTURE

With the recent regeneration of cross-border road networks and national communications, and the planned Trans-Asian Railway, Cambodia's transport infrastructure is finally on the right track to improvement. The phone communications system will receive a welcome boost from US group IDG in 2007.

ENERGY

Prices of electricity in Cambodia are expected to tumble when new hydro-power dams and power lines importing power from Vietnam and Thailand come online. In the last six months alone the Asian Development Bank and the World Bank have poured nearly $50 million into new electricity networks.

INTELLECTUAL PROPERTY

Though awash with copied CDs, DVDs and clothing, some Intellectual Property Rights breaches in Cambodia are a little more sinister. The sale of copycat medicines is still endemic outside the capital. An April 2007 study by health NGO 'truthout' found fake malaria tablets containing chalk and maize flour.

a checking of the imbalance of Asian to US investors here, he adds. "There is lots of equity looking for a place to park, and Cambodia now has something of a proven track record with a stable government, the passing of WTO laws, and the strengthening of the legal and regulatory bodies, firms are more ready than ever to consider Cambodia. The world is shrinking – and Cambodia has at last arrived as an investment destination."

According to Scianori, it is precisely the fact that Cambodia is a less obvious destination than its neighbours that makes it appealing. In more established markets firms face greater competition. High utility costs here are offset by relatively low labour and land prices. The possibility of 100% foreign ownership and zero restrictions on money transfers are also favourable elements. Moreover, investors have returned from visits saying the excellent inter-personal relationships they have developed with Cambodian business people are a great attraction, especially if compared to other countries who seem jaded from foreign investment. Easing the regulatory burden on business, improving governance and strengthening infrastructure will clearly be critical to improving Cambodia's investment climate says Kazi Matin, adding, "The perception of corruption worries potential investors. Poor infrastructure also raises costs."

Craig Guthrie