

Cambodia, long an Asian mouse, may be ready to roar

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PHNOM PENH: Most Cambodians live with two realities: rain and rice. The country that three decades ago abolished money has today embarked on the very long process of adding two new words to the national vocabulary: stocks and bonds.

The Cambodian government recently got its first sovereign debt ratings from the global ratings agencies Standard & Poor's and Moody's, and plans are afoot to open domestic stock and bond exchanges in 2009.

Take a ride into the countryside, where the vast majority of Cambodians live and work in conditions more than one observer has described as more African than Asian, and the very notion of an incipient derivatives market seems absurd.

But in the past few years, investors - not just donors, who still prop up the economy of this tiny, impoverished nation - have started to give Cambodia a good, hard second look. That is no small accomplishment for a nation still recovering from the murderous reign of the Khmer Rouge, a radical communist group that not only abolished money during its 1975 to 1979 rule, but also oversaw the deaths of about two million people - roughly one-quarter of the population at the time. After the Khmer Rouge was ousted by the Vietnamese, Cambodia sank into two more decades of civil war.

These days, the notoriously weak judiciary, lack of openness, deep and pervasive corruption, rampant smuggling, mediocre infrastructure (the postal service is barely functional and electricity costs are exorbitant), and the lack of a well-trained work force make Cambodia what has been politely called a challenging business environment.

But not, apparently, too challenging. Foreign direct investment, led by South Korea and China, rose from \$121 million in 2004 to \$475 million in 2006, according to data from the National Bank of Cambodia and the International Monetary Fund. Historically high levels of liquidity in global markets, as well as a regional boom and a growing perception that, after 30 years of domestic strife, stability has finally taken root, have all helped draw investment.

In January, the country got its first investment bank, Tong Yang Investment, part of the Tong Yang Group of companies in South Korea. Tong Yang plans to start a real estate investment fund of about \$100 million focused on Cambodia and Vietnam and marketed to South Korean investors by the end of this year. Other private equity funds are apparently in the works.

Although Cambodia's meager population of 14 million people means that the country is a hard sell for big consumer companies, others have been drawn by the nation's soaring gross domestic product. In the past decade, GDP growth has ranged from a low of 5 percent in 1998, following the bloody factional fighting of 1997, to a high of 13.5 percent in 2005, according to the Finance Ministry.

Over the past three years, Cambodia has sustained average GDP growth of 11.4 percent a year, and the IMF predicts GDP growth will level off to around 9 percent for 2007. Inflation was at 4.7 percent in 2006, according to the ministry. The government has also been deepening its commercial law framework.

"You've got a story of macroeconomic stability," said John Nelmes, the IMF representative for Cambodia. "That's proving comfortable for businesses to invest."

The Australian mining giant BHP Billiton, and its partner, Mitsubishi, have begun a large bauxite exploration project in Cambodia, and Oxiana, the Australian company that runs the huge Sepon copper and gold mine in Laos, is digging for gold in the jungles of northeastern Cambodia.

The promise of oil off the coast of Cambodia has attracted a host of adventurous companies, including the U.S. oil giant Chevron and China's CNOOC and China Petrotech.

At the end of June, a delegation of French business leaders, including representatives of Total Exploration & Production, Société Générale, France Télécom, Lafarge Cement, and the hotel group Accor, came to Cambodia for a fact-finding tour. Japan sent a similar delegation this month, and Biwako Bio-Laboratory has said that it plans to invest up to \$800 million in Cambodia for biodiesel production. On Monday, General Electric opened a branch office in Phnom Penh.

Bretton Sciaroni, a lawyer who has practiced in Cambodia since 1993, cited another factor in the country's appeal: the pro-business stance of the government.

Sciaroni, who also serves as a legal adviser to the government, said that when a client, the U.S. packaging company Crown Holdings, wanted to open a factory in Phnom Penh, getting the government to lower its 7 percent tariff on raw aluminum imports was as simple as asking. "The minister of economy and finance, Keat Chhon, asked my client what they wanted it to be," Sciaroni recalled. "My client said zero percent. He said, fine, and zero percent it is."

"People at the highest levels of government understand the necessity of getting stuff done," he added.

Officials describe the turn to capital markets as part of the nation's natural economic evolution. Last month, donors, including China, pledged to deliver \$689 million in aid to Cambodia.

"We still need donor assistance," said Hang Chuon Naron, the secretary general of the Ministry of Economy and Finance. But he added that Cambodia would need more - and more kinds of - financing as its economy expands.

The nation's economic base is still quite narrow, dominated by tourism and the garment industry, which could suffer from Vietnam's recent accession to the World Trade Organization and the expiration of U.S. and European quotas on Chinese textiles, scheduled for the end of next year.

Cambodia also has a high level of public debt - most of it on favorable, concessional terms - and it does a poor job of collecting taxes.

On the upside, Cambodia's manufacturing base has been slowly broadening. Oil, natural gas and the mineral sector are promising, and real estate has been booming, some say too much.

Sciaroni said a number of his clients had been buying up property along Cambodia's southern beaches, hoping that the new airport in Sihanoukville would eventually draw tourists who intended to visit only the Angkor Wat temple, in the north, and then leave. "You don't see it yet, but in three to five years, you're going to see major development on the south coast of Cambodia," he said.

Look around Phnom Penh and the opportunities for growth are evident: no tall office buildings, no real golf course, few malls. But the question Han Kyung Tae, Tong Yang Investment's chief representative in Cambodia, has been asking himself lately is whether all the heady talk about surging investment and the rise of capital markets is premature.

"One day, I see the big potential," he said. "The next I'm skeptical."

Right now, Sciaroni said, few domestic companies outside the financial sector, where annual audits are required, would meet even minimal listing criteria. "Transparency doesn't exist for the majority of companies here today," he said.

That has not stopped the Korea Exchange, which operates the Korean Stock Exchange, from jumping in to help develop Cambodian securities markets.

Talk with Koreans of a certain age in Phnom Penh and they will tell you that Cambodia reminds them of their childhood home. The financial sector is no different: Fifty years ago, South Korea, like Cambodia today, depended heavily on foreign aid and was struggling to develop domestic sources of financing. Korea is now trying to share the miracle of its own growth, said Hong-Sik Choi, the executive director of Global Business Development at the Korea Exchange.

"Korea has experienced a miracle to transform itself from the poorest country to the 11th largest economy in the world during the last half century," he explained. "The securities market was at the center of Korea's economic growth."

Hang, the Finance Ministry official, knows that his country is not for the fainthearted. "Cambodia is high risk, but it's also high return," he said.

And while he concedes that Cambodia's road to economic maturity will be long, he maintains that the advent of publicly traded securities will demand new systems of accounting, openness and accountability, which could improve the quality of the business environment as a whole.

Jie Sun, the deputy director of the Research Center for International Finance at Beijing's Chinese Academy of Social Sciences, said that the major lesson - and perhaps the most instructive for Cambodia - that China learned in the 15 years since Deng Xiaoping opened the gates to Chinese-style capitalism, was that capital markets could help a country with the slow and challenging work of improving its business environment.

"The Chinese have realized that the main function of the stock market is to improve corporate governance," he said at a recent conference sponsored by the Economic Institute of Cambodia, an independent research institute and consultancy in Phnom Penh. "After 15 years, we have now come to the point."