INTERNATIONAL MONETARY FUND

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CAMBODIA

November 2016

2016 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR CAMBODIA

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2016 Article IV consultation with Cambodia, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its October 19, 2016 consideration of the staff report that concluded the Article IV consultation with Cambodia.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on October 19, 2016, following discussions that ended on July 20, 2016, 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 September 28, 2016.
- A **Debt Sustainability Analysis** prepared by the staffs of the IMF and the World Bank.
- An **Informational Annex** prepared by the IMF staff.
- A **Statement by the Executive Director** for Cambodia.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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FOR IMMEDIATE RELEASE
November 3, 2016

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

IMF Executive Board Concludes Article IV Consultation with Cambodia

On October 19, the Executive Board of the International Monetary Fund (IMF) concluded the 2016 Article IV consultation with Cambodia.[1]

Cambodia is a fast-growing, highly open economy, and attained lower-middle income status this year. The Cambodian economy grew at around 7 percent in 2015, supported by strong garments exports, real estate and construction activity as well as the reduction in oil prices. Inflation unexpectedly picked up at end-2015 to 2.8 percent due to higher food prices resulting from extreme weather, but it remains well contained. Private sector credit growth has averaged nearly 30 percent (year-on-year) over the past three years, doubling the credit-to-GDP ratio to 62 percent by end-2015, which exceeds the median emerging market level and is double the median low-income country level.

The current account deficit (CAD) narrowed to 10.6 percent of GDP in 2015, and is largely financed by FDI and official flows. Gross official reserves rose to US$ 5.3 billion at end-2015, more than 4 months of prospective imports. The fiscal deficit narrowed to 1.6 percent of GDP in 2015, below the budget target, as the result of stronger-than-expected revenue growth, owing to improved revenue administration.

The near-term outlook remains broadly favorable. Growth is projected to remain robust at around 7 percent for 2016–17, supported by strong garments exports, real estate and construction activity, notwithstanding weaker agricultural and tourism growth. Medium-term growth is projected to decline to around 6.3 percent by 2021, due to a moderation in the credit cycle and challenges in economic diversification. The current account deficit (CAD) is projected to narrow to 9.7 percent of GDP in 2016, due to reduced imports following the completion of major hydro projects, low commodity prices and growing remittances. Over the medium-term, the CAD is forecast to decline to around 8.5 percent of GDP.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

The outlook is subject to substantial downside risks. Rapid credit growth, along with growing concentration in real estate, poses heightened risks to financial and macroeconomic stability. External risks include a significant slowdown in China, U.S. dollar appreciation, structurally weaker growth in Europe coupled with increased uncertainty from the Brexit referendum result, and a sharper-than-anticipated tightening in global financial conditions.

Executive Board Assessment[2]

Directors welcomed Cambodia's robust economic growth over the last two decades, which has resulted in an impressive decline in poverty and the country's successful transition to a lower-middle income status. Directors noted that while the growth outlook remains strong, the economy faces downside risks stemming from rapid credit growth, fiscal pressures, and possible spillovers from an uncertain external environment. They recommended that policies ahead should focus on securing sustained growth and mitigating financial sector vulnerabilities, including by enhancing resilience and building buffers.

Directors considered the current fiscal stance to be appropriate and commended the improvements in tax administration, which helped increase revenue and accumulate government deposits in the banking system. To sustain these gains, they encouraged modernization of tax policy and further efforts to strengthen revenue administration. Directors also advised that future increases in public wages should be fiscally sustainable and accompanied by continued civil service reform. They recommended curtailing non-development current spending and saving excess revenues in the event of overperformance. In addition, Directors encouraged the authorities to develop a medium-term fiscal framework, improve expenditure allocation efficiency, as well as strengthen the monitoring of contingent liabilities, particularly from public-private partnerships.

Directors welcomed the steps being taken to bolster financial stability, noting the recent institution of the liquidity coverage ratio and minimum capital requirements. They highlighted that stronger efforts will be needed to achieve a soft landing of the credit cycle and safeguard macro-financial stability. Directors underscored that well-coordinated policy measures, including raising reserve requirements, putting in place macroprudential measures, and strengthening micro-prudential regulations will help moderate the pace of credit growth and bolster financial stability. In addition, they encouraged upgrading and tightening of prudential regulations on large deposit-taking micro-finance institutions to match those of banks. Developing a crisis management framework will also be important going forward.

[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

Directors welcomed the policies to promote financial market development, particularly improvements in the negotiable certificates of deposits market. They considered that further progress in developing an interbank market is important for laying the groundwork for market-based monetary policy operations. They also recommended policies to promote de-dollarization and accelerate broader financial market development.

Directors encouraged the authorities to step up their efforts to boost competitiveness and promote economic diversification. Reducing the cost of doing business will help enhance competitiveness and foster diversification and inclusiveness. Directors highlighted that lowering energy costs, upgrading infrastructure, addressing skills bottlenecks, as well as strengthening transparency will also contribute to fostering inclusive and sustained growth.

Cambodia: Selected Economic Indicators, 2011–17

	2011	2012	2013	2014	2015 Est.	2016 Proj.	2017 Proj.
Output and prices (annual percent change)							
GDP in constant prices	7.1	7.3	7.4	7.1	7.0	7.0	6.9
(Excluding agriculture)	8.6	8.4	9.4	9.2	9.0	8.7	8.4
Inflation (end-year)	4.9	2.5	4.7	1.0	2.8	3.2	2.9
(Annual average)	5.5	2.9	3.0	3.9	1.2	3.1	2.7
Saving and investment balance (in percent of GDP)							
Gross national saving	11.8	12.5	11.2	11.1	11.8	12.7	13.6
Government saving	0.8	1.9	2.2	3.4	4.0	3.4	2.5
Private saving	11.0	10.6	9.0	7.7	7.8	9.4	11.0
Gross fixed investment	22.0	23.5	23.5	23.2	22.4	22.9	23.0
Government investment	8.7	9.0	8.9	7.9	7.0	7.8	8.1
Private investment 1/	13.3	14.5	14.6	15.3	15.4	15.1	14.9
Money and credit (annual percent change, unless otherwise indicated)							
Broad money	21.4	20.9	14.6	29.9	14.7	19.9	10.2
Private sector credit	31.2	28.0	26.7	31.3	27.1	26.0	24.4
Velocity of money 2/	2.0	2.0	2.0	2.0	2.0	2.0	2.0
Public finance (in percent of GDP)							
Revenue	15.6	16.9	18.6	19.6	18.8	19.7	20.5
Domestic revenue	12.4	14.1	14.6	16.7	16.6	17.8	17.9
Of which: Tax revenue	10.2	11.3	11.8	13.7	14.6	14.9	15.0
Grants	3.2	2.8	3.9	2.9	2.3	1.9	2.6
Expenditure	19.7	20.7	20.7	20.9	20.4	22.3	23.4
Expense	11.3	12.0	12.0	13.0	13.2	14.5	15.4
Net acquisition of nonfinancial assets	8.4	8.7	8.7	7.9	7.2	7.8	8.0
Net lending (+)/borrowing (-)	-4.1	-3.8	-2.1	-1.3	-1.6	-2.6	-2.9
Net lending (+)/borrowing (-) excluding grants 3/	-7.5	-6.3	-6.4	-4.2	-2.9	-4.3	-5.5
Net acquisition of financial assets	0.0	0.6	0.5	2.3	2.8	1.1	1.0
Net incurrence of liabilities 4/	4.1	4.4	2.6	3.6	4.4	3.7	3.9
Of which: Domestic financing	1.4	0.7	-0.6	-1.4	-0.8	-1.1	-0.3
Government deposits	4.6	4.9	5.0	6.8	9.1	9.3	8.7
Balance of payments (in millions of dollars, unless otherwise indicated)							
Exports, f.o.b. 5/	5,035	5,633	6,530	7,408	8,461	9,363	10,337
(Annual percent change)	28.9	11.9	15.9	13.4	14.2	10.7	10.4
				-	-	-	-
Imports, f.o.b.	-7,730	-8,600	-9,744	10,997	12,145	13,147	14,515
(Annual percent change)	32.9	11.3	13.3	12.9	10.4	8.3	10.4
Current account (including official transfers)	-1,303	-1,547	-1,880	-2,032	-1,889	-1,969	-1,973
(In percent of GDP)	-10.2	-11.0	-12.3	-12.1	-10.6	-10.2	-9.4
Gross official reserves 6/	3,032	3,463	3,642	4,391	5,271	6,322	7,421
(In months of prospective imports)	3.6	3.6	3.4	3.7	4.1	4.5	4.8
External debt (in millions of dollars, unless otherwise indicated)							
Public external debt	3,833	4,474	4,852	5,291	5,645	6,138	6,726
(In percent of GDP)	29.7	31.5	31.6	31.8	32.1	32.1	32.3
Public debt service	77	85	112	143	172	189	249
(In percent of exports of goods and services)	1.0	1.0	1.1	1.3	1.4	1.4	1.7
Memorandum items:							
Nominal GDP (in billions of riels) 7/	52,069	56,682	61,390	67,740	73,423	81,978	90,318
(In millions of U.S. dollars)	12,818	14,057	15,244	16,778	17,789	19,368	20,937
Exchange rate (riels per dollar; period average)	4,062	4,032	4,027	4,038	4,127	...	...

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

1/ From 2011, includes FDI related to public-private power sector projects.
2/ Ratio of nominal GDP to the average stock of broad money.
3/ According to GFS 86 used by Cambodian authorities.
4/ Includes statistical discrepancy.
5/ Trade data has been revised backward to 2008.
6/ Excludes unrestricted foreign currency deposits held as reserves at the National Bank of Cambodia; starting in 2009, includes the new SDR allocations made by the IMF of SDR 68.4 million.
7/ GDP data have been revised backward to 2010.

INTERNATIONAL MONETARY FUND

CAMBODIA

STAFF REPORT FOR THE 2016 ARTICLE IV CONSULTATION

September 28, 2016

KEY ISSUES

Context. Growth remains strong supported by robust garments exports, real estate and construction activity. Inflation has increased slightly due to higher food prices. Rapid credit growth, along with growing concentration in real estate, poses heightened risks to financial and macroeconomic stability. External risks include a significant slowdown in China, U.S. dollar appreciation, structurally-weaker growth in Europe coupled with increased uncertainty from the Brexit referendum result, and a sharper-than-anticipated tightening in global financial conditions.

Main Policy Recommendations

Policies should focus on securing sustained growth and mitigating growing financial sector vulnerabilities, including by enhancing resilience and building buffers preemptively. Key elements of the policy strategy should include:

- Monetary and financial sector: Mitigating macro-financial risks by engineering a soft landing of the credit cycle and building capital and liquidity buffers using a well-sequenced set of micro- and macro-prudential policy tools, developing a crisis management framework, and continued upgrading of regulation and supervision.

- Fiscal policy: Maintaining fiscal sustainability and supporting development by further boosting revenues (by modernizing revenue administration and tax policy), while developing a medium-term fiscal framework to facilitate more strategic allocation of resources.

- Structural policy: Increasing competitiveness and encouraging diversification through lowering energy costs, improving human capital and infrastructure, and strengthening the rule of law and transparency to reduce business costs and uncertainty.

- Exchange rate policy and market development: Develop money and foreign exchange markets to promote de-dollarization and support implementation of an effective monetary framework. This would allow gradually increasing exchange rate flexibility, which would help respond to external shocks.

Approved By
Markus Rodlauer and Steve Barnett

Discussions took place during July 6–20, 2016. The staff team comprised S. Jain-Chandra (Head), M. Ghazanchyan, M. Ishiguro, T. Ikoma, S. Rafiq (all APD), J. Park (MCM), and Y. Zhou (Resident Representative). Mr. Rodlauer (APD) joined the second half of the mission. Mr. Omar and Mr. Chea (OED) participated in the concluding meetings. Ms. L. Zhuang and Ms. R. Sirihorachai assisted in this report's preparation.

CONTENTS

CONTEXT

1. Context. Cambodia is a fast-growing, highly open economy, and attained lower-middle income status this year. Over the last two decades, Cambodia grew rapidly (average real GDP growth of around 8 percent) and its integration with the global economy increased sharply, accompanied by an impressive decline in poverty. Going forward, Cambodia's strategic location, China's changing trade patterns, and ongoing regional integration provide further opportunities.[1] Important steps have been taken by the government that will help Cambodia capitalize on these opportunities, including energy-related investments to help reduce the cost of doing business and measures to facilitate trade, payments and business registration. Nonetheless, further measures are needed to support sustained growth, including reforms to improve the business climate and policies to mitigate rising financial sector vulnerabilities.

2. Past Fund advice. Policies have generally been in line with past Fund advice, but implementation should be accelerated in key areas. Consistent with past Fund recommendations, the authorities are implementing the Revenue Mobilization Strategy (RMS) and improving revenue administration, and strengthening public financial management. The National Bank of Cambodia (NBC) recently introduced the Liquidity Coverage Ratio (LCR) to improve liquidity regulation, and raised minimum capital requirements to build capital buffers. Going forward, the key policy focus should be to secure sustained growth and mitigate growing financial sector vulnerabilities, along with continuing efforts to meet the sustainable development goals and promote inclusion.

DEVELOPMENTS, OUTLOOK, AND RISKS

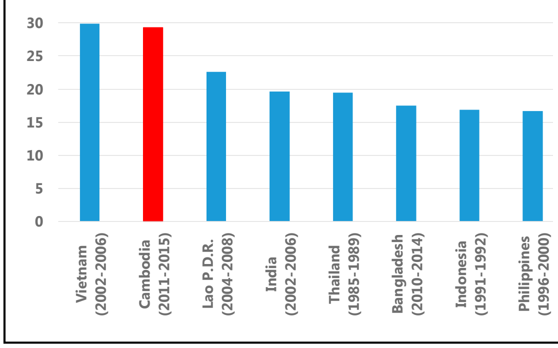
3. Growth and inflation. The economy grew at 7 percent in 2015, supported by strong garments exports, real estate and construction activity, as well as the reduction in oil prices, notwithstanding weaker agricultural and tourism growth.[2] Growth is projected to remain robust at 7 percent for 2016–17. Medium-term growth is projected to decline to around 6¼ percent by 2021, due to a moderation in the credit cycle and challenges in economic diversification. To sustain growth at around 7 percent and above (through 2021), expeditious implementation of business climate reforms coupled with targeted investments, particularly in agriculture and transportation infrastructure, as well as measures to protect financial stability are needed (Box 1). Inflation unexpectedly picked up at end-2015 to 2.8 percent due to higher food prices resulting from extreme weather, and is projected to rise modestly to 3.2 percent by end 2016.

[1] See "China and the CLMV: Integration, Evolution, and Implications" (IMF, 2016).

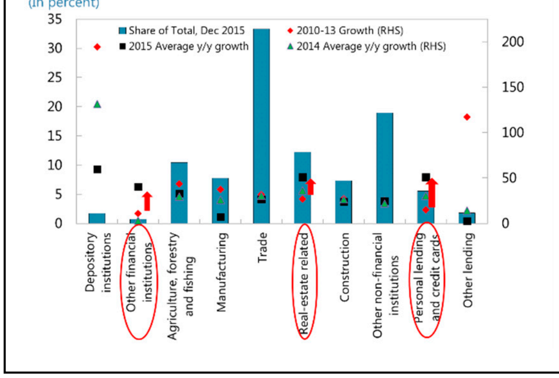
[2] Garment exports, accounting for 74 percent of exports, grew at around 15 percent (y/y) in 2015, which was above expectations, despite exchange rate appreciation and weak trading partner growth (particularly in the EU).

4. Credit cycle. Credit growth has been rapid, leading to one of the fastest financial deepening episodes by historical cross-country standards. Private sector credit growth has averaged nearly 30 percent (year-on-year) over the past three years, doubling the credit-to-GDP ratio to 62 percent by end-2015, which exceeds the median emerging market level and is double the median low-income country (LIC) level. While credit to the manufacturing and agricultural sectors slowed, real estate and mortgage lending continue to grow rapidly, averaging 50 percent in 2015 and H1 2016. Broad money growth slowed as deposit growth fell to 19 percent in the first half of 2016, from 25 percent in the first half of 2015. Banks are relying more on foreign borrowing to maintain credit growth, and the average loan-to-deposit (LTD) ratio reached 108.5 percent in June 2016, from 79 percent in 2010. The financial system remains highly dollarized, with foreign currency deposits constituting 95 percent of total deposits.

Credit Growth at Similar GDP Levels
(PPP per capita, Five-year average)



Credit growth by Economic Sector
(In percent)



5. External sector outlook. The current account deficit (CAD) is projected to narrow to 10.2 percent of GDP in 2016, from 10.6 percent in 2015, due to reduced imports following the completion of major hydro projects, low commodity prices and growing remittances. Over the medium-term, the CAD is forecast to decline to around 8½ percent of GDP, as major power projects are completed (and related imports decline), exports and tourism grow (aided by an expansion of US GSP access for specific travel-related items) with some product diversification amid ASEAN Economic Community integration. Indeed, recent FDI trends point to early signs of diversification into other manufacturing products as regional producers attempt to diversify their supply chains. FDI and official sector flows are expected to continue financing the CAD over the medium-term. Gross official reserves are projected to increase to US$6.3 billion as of end-2016 (around 4½ months of total imports) and to continue rising over the medium term.

6. External sector assessment and policies. Based on the IMF's External Balance Assessment-lite methodology, the external position is assessed to be moderately weaker than suggested by fundamentals and desirable policies (Box 2). The moderate overvaluation of the real effective exchange rate (REER), in the absence of an independent exchange rate regime, calls for policies to improve productivity and competitiveness.[3] Measured against traditional metrics, reserves appear to

[3] The de jure exchange rate arrangement is a managed float. The de facto exchange rate arrangement is a "other managed" arrangement.

be adequate; however, there are benefits to building reserves further given high dollarization and elevated financial vulnerabilities. The current exchange rate regime, based on keeping the riel broadly stable against the U.S. dollar, is appropriate given high dollarization and a concentration in U.S. dollar-invoiced exports (primarily garments). Over time, as dollarization declines, capacity improves, and the economy diversifies, gradually introducing greater exchange rate flexibility is recommended to better absorb external shocks and enable implementation of an independent monetary policy.

7. **Risks**. The outlook is subject to downside risks:

- **External risks:** A significant slowdown in China would spill over through the FDI, banking and tourism channels (Box 3). A surge in the US dollar and/or weaker growth in Europe could constrain garments exports, particularly amid stiff competition from other low-cost producers (see Appendix I, Risk Assessment Matrix). In the near term, the Brexit referendum result is not expected to have a large direct impact on Cambodian exports (despite Cambodia's trade export exposure to the UK being the highest in the ASEAN at close to 6 percent of GDP) due to UK-bound Cambodian exports being relatively income inelastic. A more important headwind for Cambodian exports could be the increasing redirection of new garment orders to Vietnam as a result of the TPP agreement, which would lead to declining FDI growth in the Cambodian garment sector. Also, sharper-than-anticipated tightening in global financial conditions could raise funding costs and heighten liquidity risks for Cambodian banks and MFIs, which have become increasingly reliant on foreign funding.

- **Macro-financial risks.** Rising financial sector vulnerabilities amid a credit boom pose significant risks to macro-financial stability.

    - Several macroeconomic shocks may adversely affect the financial system.

        - ❖ Macroeconomic shocks could potentially lead to a funding squeeze and result in a credit crunch. Possible shocks include a sharper-than-anticipated global liquidity tightening, and a significant slowdown in China.

        - ❖ A sharp slowdown in economic growth could lead to an increase in bad loans in specific sectors (e.g. slower-than-expected growth in the EU and China can affect garments exports and construction).

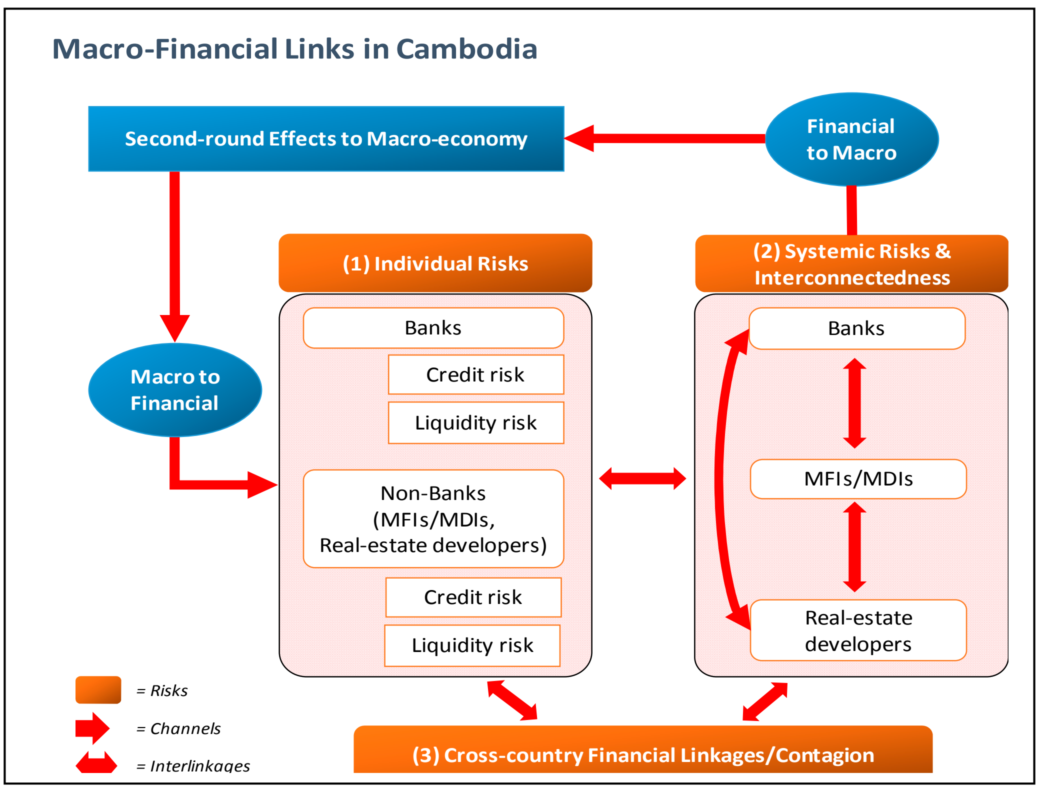
    - Vulnerabilities in certain banks or MFIs and in the real estate market may lead to a financial system-wide shock, which could spill over to the macro economy.

- Growing oversupply in the real-estate sector could trigger a disorderly price correction.[4] This in turn could lead to rising defaults (as collateral values fall) and a spike in NPLs, which would pose a drag on credit growth and economic activity.

- **Other domestic risks** include fiscal pressures and the erosion of competitiveness from wage hikes potentially outstripping productivity increases.

- **Upside risks**. Faster structural reforms and efforts to slow credit and channel it to more productive sectors will lead to faster and more durable growth over the medium term (Box 1).

- **Policy response**. Policy options in case financial sector risks materialize are limited in view of high dollarization and a lack of monetary instruments, as well as the projected lack of fiscal space over the medium term. There is a need to build up the crisis management framework by bolstering the financial safety net, including instituting deposit insurance, putting in place a robust bank resolution framework, and strengthening the lender of last resort function of the NBC.



[4] According to a report by the real estate company, Knight Frank, while the supply of retail and office space will approximately double by 2018, the supply of condominiums will increase more than six fold.

8. Authorities' views. The authorities broadly shared staff's assessment of the outlook and risks. Over the medium term, they also project growth to fall absent further diversification. They had a similar assessment of macro-financial risks and emphasized their plans to mitigate them, while closely monitoring the impact on growth. They expressed concerns regarding spillovers from EU growth on garment exports, while noting that Brexit and Vietnam's inclusion in the TPP agreement were unlikely to hurt exports (and FDI) significantly over the next few years, but could weigh on medium-term prospects. To support exports, a short-term priority for the government is to expand US GSP access to other garments. The authorities considered minimum wage negotiations, rather than further appreciation of the U.S. dollar, as the biggest near-term risk to competitiveness. Reserve accumulation in 2016 thus far has exceeded the authorities' expectations, and is projected to remain strong for the rest of the year.

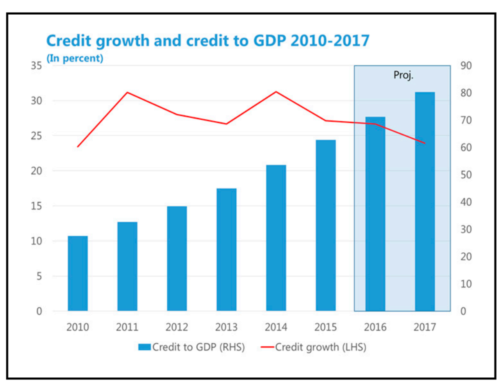
KEY POLICY ISSUES

9. The key policy challenges are to secure sustained growth and mitigate growing financial sector vulnerabilities. Along with building resilience, efforts are needed to meet the sustainable development goals and promote inclusion. Policy efforts should focus on: (i) containing growing macro-financial risks, (ii) maintaining fiscal sustainability, (iii) boosting competitiveness and diversification, and (iv) expediting financial market development.

10. Policy strategy. In view of rising financial sector vulnerabilities and elevated external risks, *macroeconomic policies* should be tightened to secure buffers, notwithstanding low debt levels. *Fiscal policy* should continue focusing on boosting revenues and rationalizing expenditure to maintain fiscal sustainability, amid rising wage pressures and needed capital and development spending, and to ensure sufficient fiscal buffers. *Financial sector policies* should focus on securing a soft landing of the credit cycle and building capital and liquidity buffers, using a well-coordinated and sequenced set of micro- and macroprudential policy tools, as well as upgrading regulation and supervision. Finally, *structural reforms* should be geared towards promoting diversification, enhancing competitiveness, and improving the business climate, to secure inclusive and sustained growth.

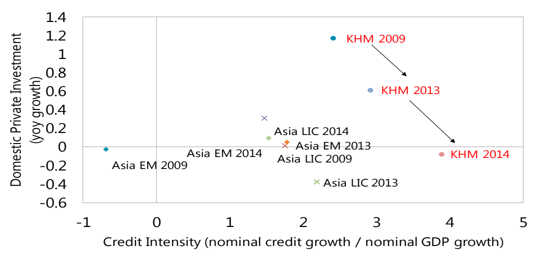
A. Containing Growing Macro-Financial Risks

11. Excessive credit growth. The duration of the current credit boom, which began at around end-2011, significantly exceeds the average length of past credit booms, leading to the buildup of financial stability risks. Credit growth is projected to remain high at around 25 percent over 2016–17, moderating only slightly due to tightening global financial conditions and the imposition of tighter liquidity regulations and higher capital requirements. This would result in an already-high credit/GDP ratio to continue rising sharply (to over 80 percent by 2017). The credit-to-GDP gap (a widely used



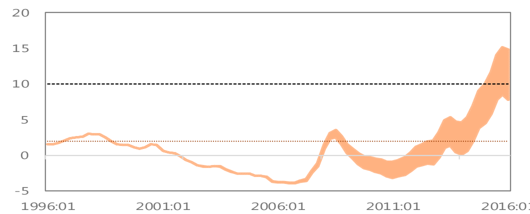
cross-country indicator of potential crises/banking stress), which by end 2015 had already exceeded the pre-crisis peak reached in 2008, is projected to breach the 10-percent threshold by end 2017.[5] Credit intensity of growth has trended up to 3.8 in 2015 from 3 in 2011–14 (average), implying that credit is becoming less efficient in generating growth and investment.[6] Over the medium term, sustaining high economic growth and avoiding financial instability will require decisively moderating the pace of credit growth.[7]

Credit Intensity and Domestic Private Investment Growth 1/



Sources: Data from Cambodian authorities; and IMF staff caluclation.
1/ Asia LIC include Bangladesh, Myanmar, Mongolia, Sri Lanka, and Vietnam. Asia EM include India, Indonesia, Malaysia, Philippines, and Thailand.

Credit Gap, 1996–2016[1]
(In percent of GDP)

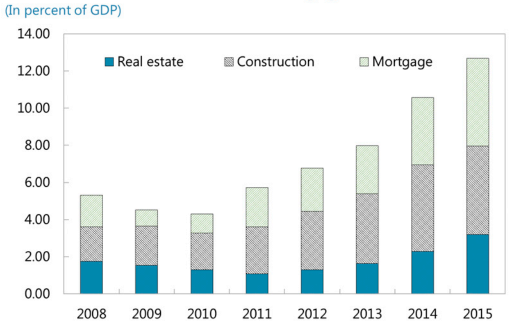


Source: IMF staff estimates.

[1] The credit-to-GDP gap fan chart is based on a one-sided HP filter estimated using a Kalman filter, with multiple smoothing parameters to account for uncertainty regarding the extent of financial deepening.

12. Intensifying credit risk in real estate. Real estate market expansion has continued unabated, with new construction permits continuing to rise. While credit growth has been broad-based, there is growing concentration in the real estate sector, leading to rising credit risk linked to asset prices. Rapid construction could eventually lead to an over-supply in the real estate market (especially for condominiums), which risks precipitating a large disorderly adjustment in real estate prices, adversely impacting the banking sector and economic activity.[8]

Real estate, Construction and Mortgage, 2008–15
(In percent of GDP)



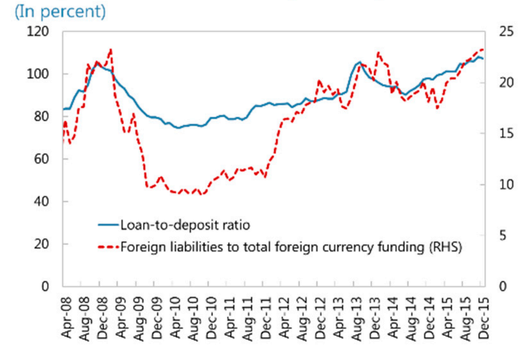
[5] Credit-to-GDP gap is considered a leading indicator for financial sector stress or crises or a sharp growth slowdown. Following the BIS methodology, a threshold of 10 percent is considered a strong signal of an impending crisis (Drehman and others, 2010). The credit gap discussed here is based on the HP filter, and is at the lower bound of the range of estimates.

[6] Credit intensity is defined as nominal credit growth divided by nominal GDP growth.

[7] Dell'Ariccia and others (2012) found that while it is difficult to tell "bad" from "good" credit booms, bad booms tend to be larger and last longer. Roughly half of the booms lasting longer than six years ended in a severe financial downturn.

[8] There is currently no official housing data, which poses serious challenges to analyzing the link between housing boom and credit boom. There is also limited data on household balance sheets and leverage. Data from a real estate agency suggests that Phnom Penh's land price for residential and office space increased 26 percent and 19 percent, respectively, year-on-year in 2015; the highest growth among Asian cities. Since 95 percent of loans in Cambodia are collateralized against land, a negative shock in the real estate sector could put more debtors in negative equity, which in turn could prompt rising defaults and fire sales.

13. Increasing reliance on foreign funding. The banking sector has increased its reliance on foreign borrowing, further raising structurally high liquidity risks. The average LTD ratio reached 108.5 percent in June 2016 (20 banks with LTD ratios over 100 percent, and 14 banks over 200 percent).



14. Rising risks from the nonbank sector. Microfinance institutions (MFIs) are now playing a systemic role, with credit stock and flows from MFIs at 20 and 25 percent, respectively, of those in the banking system. A number of MFIs are now larger than some mid-sized commercial banks and accept deposits, thereby competing for the same client base while being subject to looser regulations.[9] Moreover, large deposit-taking MFIs are heavily reliant on foreign funding, even more so than banks.

15. Financial Soundness Indicators. Financial soundness indicators (FSIs) appear healthy, suggesting adequate capitalization levels, low nonperforming loans (NPLs), and high profitability. However, healthy FSIs may mask the build-up of credit risk in individual banks given the lack of clarity in the classification of restructured loans. While the system NPL ratio is under 2 percent—suggesting robust asset quality— lack of detailed guidance on the treatment of restructured loans could possibly underestimate the NPL ratio and overstate capital adequacy. While the aggregate capital adequacy ratio is above 20 percent, the solvency ratio of many banks, including large ones, may be vulnerable to higher loan losses should defaults unexpectedly increase. Furthermore, liquid assets relative to total assets or short-term liabilities appear to be low, rendering many banks vulnerable to liquidity risks.

Selected Financial Soundness Indicators (FSIs), 2011–15
(In percent)

	2011	2012	2013	2014	2015
Capital Adequacy					
Regulatory capital to risk-weighted assets	26.23	25.00	24.23	20.41	21.04
Asset Quality					
Nonperforming loans to total gross loans	2.13	2.01	2.30	1.62	1.59
Earnings and Profitability					
Return on equity 1/	9.74	10.25	12.15	15.54	16.34
Return on assets 1/	1.76	1.72	2.40	2.87	3.98
Interest margin to gross income	64.27	66.65	68.60	72.94	63.07
Liquidity					
Liquid assets to total assets	16.16	15.37	17.93	16.21	16.61
Liquid assets to short-term liabilities	22.96	21.21	24.24	23.13	25.42

Source: National Bank of Cambodia.
1/ Annualized.

16. Containing growing financial risks. Cognizant of growing financial risks, the NBC has recently taken a number of pre-emptive steps to enhance the resilience of the financial system. Liquidity regulations have been strengthened by introducing a Basel-III compliant Liquidity Coverage Ratio (to be met by September 2016), and while it is too early to assess the impact, this regulation is expected to dent credit momentum and help build buffers against liquidity shocks. The

[9] MFIs are expanding loans at a faster pace to maintain growth targets and average loan size has risen sharply. Also, more than 20 percent of MFI customers have multiple loans, which is partly due to the highly-saturated MFI industry and the ensuing competition.

NBC has also raised minimum capital requirements in March 2016 (to be in full effect in two years).[10] The NBC's plans to impose bank-specific prudential measures on institutions deemed to be engaged in excessive risk-taking is welcome. While these efforts are to be commended, further measures are needed to ensure financial stability. Therefore, the NBC should follow through on their plans to adopt a liquidity risk management framework in 2016, improve regulations on asset classification and provisioning, and refine the solvency ratio during 2017. Also, while supervisory capacity has improved, further efforts are required to close gaps in financial supervision.[11] The government has recently tightened licensing and supervision on real estate developers, and improved the efficiency and expanded the coverage of stamp duty on real estate transactions. These measures are welcome and should be used more actively going forward as an additional counter-cyclical policy tool to help manage the real estate cycle.

17. Policy recommendations. The following policy measures are recommended to encourage financial institutions to build resilience and engineer a soft landing of the credit cycle. To this end, a range of tools should be implemented and coordinated among multiple government agencies in a well-designed and sequenced way. The recommended sequencing of specific measures is contained in the table on page 12.

- **Raise reserve requirements** (RR). RR should be raised, particularly on short-term foreign currency deposits and foreign borrowing. This would also increase the size of NBC's liquidity buffer that can be promptly released should liquidity conditions unexpectedly tighten.
- **Strengthen microprudential policies.** The NBC should revisit loan classification, align provisioning rules with international best practices, improve asset classification regulation, and ensure that rules are consistently enforced by banks, particularly focusing on sound underwriting standards and prudent valuations.[12] Capital adequacy regulations, which are based on Basel I, need to be upgraded to ensure financial institutions have adequate buffers commensurate with their risk profiles.
- **Put in place a comprehensive crisis management framework**. First, the NBC should strengthen the existing prompt corrective action framework to enable it to take early action.[13] Second, building on the memorandum of understanding (MOU) signed by the NBC, the Ministry of Economy and Finance (MEF), and the Securities and Exchange Commission of Cambodia (SECC) in 2014, the crisis

[10] Minimum capital requirements for commercial banks were raised from $37.5 million to $75 million, and for deposit-taking MFIs from $2.5 million to $30 million.

[11] The discrepancies are attributable to both the limited number and technical capabilities of supervisors. Capacity building efforts are thus crucial, and the NBC has requested IMF assistance in a number of areas.

[12] The regulations should provide more detailed guidance on the treatment of restructured loans. For instance, a bank should be required to limit the number of times an individual loan may be restructured, formally agree on new terms of agreement with borrowers, and have in place policies and procedures approved by the Board. Restructured loans should also attract a higher risk weight under the capital adequacy framework reflecting a higher probability of default. Many of these minimum standards did not appear to be in place or observed by the banks.

[13] As a first step, the NBC should consider introducing triggers for domestic systematically important banks with regard to asset quality and liquidity position, in addition to existing legal triggers on the regulatory minimum for solvency ratio, for prompt corrective action.

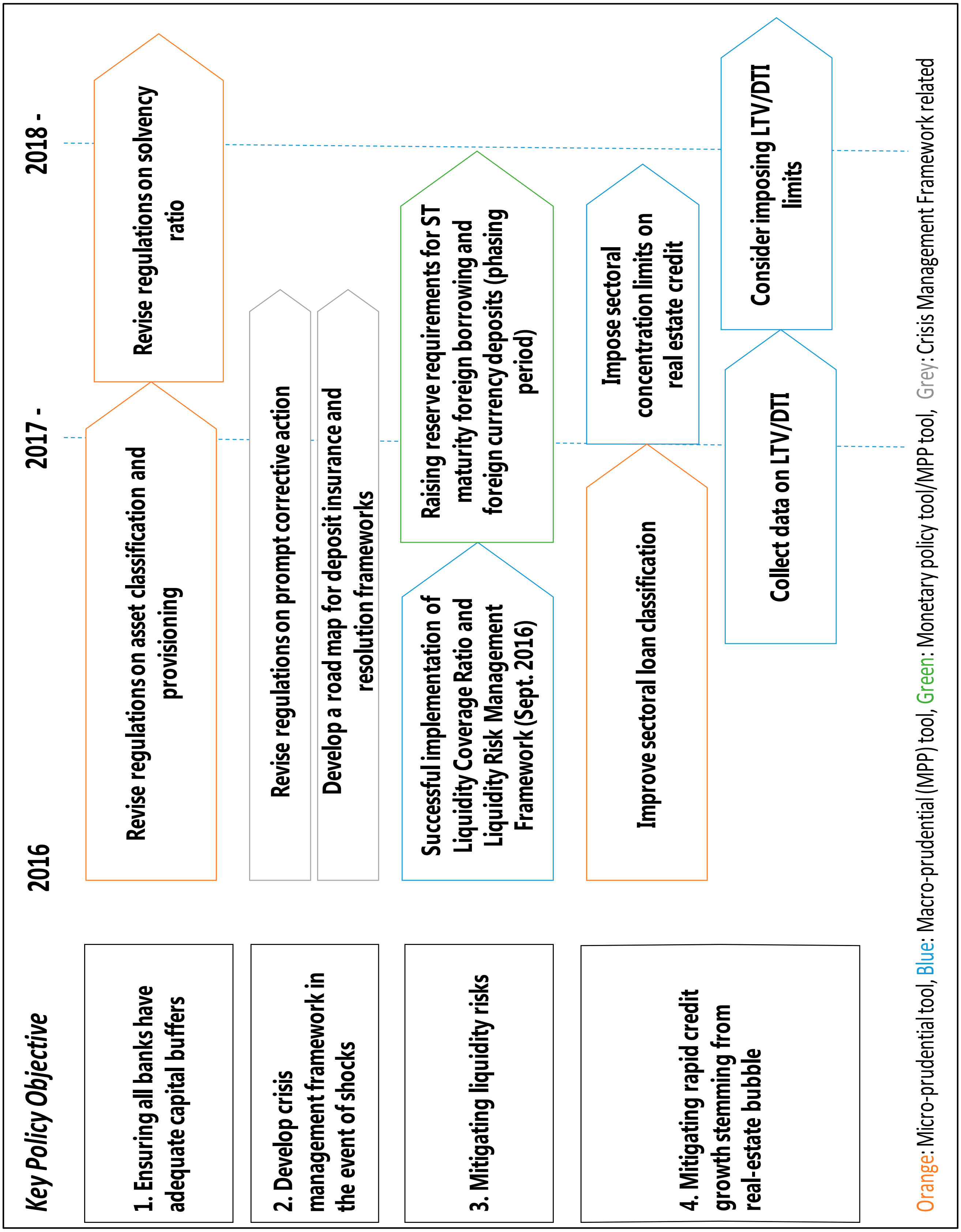
management framework should provide a sound institutional arrangement with more explicit inter-agency coordination mechanisms, including the exchange of information, contingency planning, and reforms to the legal framework in line with 2010 FSAP recommendations.

- **Introduce macroprudential policies.** (i) *Sectoral tools:* imposing sectoral concentration limits and/or higher risk weights for real-estate loans should be considered. Collection of real-estate data and household balance sheets should be expedited to enable the introduction of limits on debt-to-income ratio and loan-to-value ratios; (ii) *Liquidity tools*: funding requirements such as limits on LTD ratios would ensure that banks hold more internal and stable liabilities, and can also serve as an effective brake on excessive credit growth; (iii) *Capital tools*: counter cyclical capital requirements (tailored to Cambodia) could be implemented to build buffers in the financial system, which can be drawn upon in a downturn.

- **Strengthen non-bank regulation.** The growing systemic relevance of large MFIs calls for strengthening regulation to prevent regulatory arbitrage (Box 4). Specifically, (i) revising the capital adequacy regulations, (ii) standardizing asset classification in line with banks, (iii) raising RR, and (iv) better monitoring of systemic linkages between MFIs and banks.

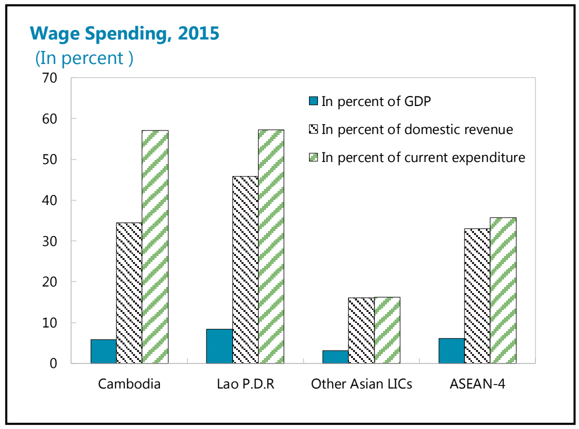
- **Implement complementary prudential measures**. A coordinated policy response across government agencies, complementing actions taken by the NBC, is recommended to moderate rapid credit growth and contain rising financial stability risks. Well-designed and targeted fiscal measures, such as stamp duties and a capital gains tax, to augment the monetary prudential measures taken by the NBC, could be deployed to more decisively dampen excessive real estate price inflation. Such measures are especially useful when the real estate cycle is being driven by capital inflows that bypass the domestic banking system.

18. Authorities' views. The authorities broadly agreed with staff's assessment and highlighted their efforts to incorporate staff's previous recommendations. They agreed that there is a need to engineer a soft landing of the credit cycle, including by focusing on strengthening regulation and improving institutional capacity. They noted that in addition to the speed of credit growth, they are closely monitoring the quality of credit and the sectoral allocation of credit with the objective of increasing credit to productive sectors. The authorities also broadly agreed with staff's proposed sequencing of financial sector policy recommendations, though they noted that the exact timing of additional measures would be contingent upon the assessment of past measures and the impact on credit growth and economic activity. The NBC has implemented microprudential and macroprudential measures such as reserve requirements on non-resident borrowings, liquidity coverage ratio and increase in minimum registered capital. The NBC has already started working on revising regulations on asset classification and provisioning, as well as on the prompt corrective action framework, and plans to upgrade solvency regulation. To curb credit, it is considering introducing targeted bank-by-bank level regulation. The NBC has launched a Financial Literacy Program to help support financial stability. Finally, the authorities highlighted progress in strengthening crisis preparedness, as the MEF and SECC have recently established financial stability working groups to improve information sharing, and have committed to set up, together with the NBC, a national financial stability committee that will establish a crisis management framework and strengthen financial stability oversight.


Key Policy Objective
2016
2017 -
2018 -
1. Ensuring all banks have adequate capital buffers
Revise regulations on asset classification and provisioning
Revise regulations on solvency ratio
2. Develop crisis management framework in the event of shocks
Revise regulations on prompt corrective action
Develop a road map for deposit insurance and resolution frameworks
3. Mitigating liquidity risks
Successful implementation of Liquidity Coverage Ratio and Liquidity Risk Management Framework (Sept. 2016)
Raising reserve requirements for ST maturity foreign borrowing and foreign currency deposits (phasing period)
4. Mitigating rapid credit growth stemming from real-estate bubble
Improve sectoral loan classification
Impose sectoral concentration limits on real estate credit
Collect data on LTV/DTI
Consider imposing LTV/DTI limits
Orange: Micro-prudential tool, Blue: Macro-prudential (MPP) tool, Green: Monetary policy tool/MPP tool, Grey: Crisis Management Framework related

B. Maintaining Fiscal Sustainability

19. Fiscal outlook in 2016. The fiscal deficit is projected to widen to 2.6 percent of GDP (but remain below the budget target) from 1.6 percent of GDP in 2015 as rising current expenditure is expected to more than offset revenue mobilization efforts.[14] Strong revenue performance, following the 2014 adoption of the government's RMS, is expected to continue as the result of improvements in tax administration, and is projected to raise tax revenues by 0.3 percent of GDP (following 0.9 percent of GDP increase in 2015).[15] However, wage pressures persist, and current expenditure is projected to rise by about 1.2 percent of GDP driven by an increase in the wage bill of about 0.2 percent of GDP and non-wage current expenditure by another 1 percent of GDP.[16] Government deposits are projected to be 9.3 percent of GDP, a level that is considered adequate. In view of impending spending pressures over the medium term, any revenue over-performance should be saved and non-development current expenditure curtailed, by continuing to enhance spending efficiency.



20. 2017 Preliminary budget. In the preliminary 2017 budget, the government plans to target a budget deficit of 2.6 percent of GDP. On the revenue side, the budget envisages a 0.5 percent of GDP increase in tax revenues owing to improvements in tax administration and compliance. On the spending side, the budget includes a 0.4 percent of GDP increase in the wage bill to 7.4 percent of GDP. Spending on social protection and pensions will also rise (by about 1 percent of GDP). Plans to increase social spending and growth-enhancing capital spending are welcome. However, revenue projections appear optimistic, and staff projects lower revenue growth and a higher fiscal deficit.

21. Medium-term fiscal pressures. Over the medium term, strong revenue administration efforts (based on RMS implementation) are expected to continue to boost revenues, but the pace of

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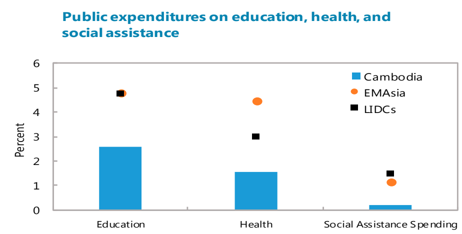
[14] The 2015 fiscal deficit (-1.6 percent of GDP) was much smaller than the budget target of -4.2 percent of GDP, due to robust revenue growth, following the implementation of the RMS.

[15] Initiated in late 2012, the RMS focuses on strengthening revenue administration, revenue policy and the institutional framework in order to continue raising domestic revenue by at least ½ percent of GDP annually over the medium term. Improved tax administration includes enhanced taxpayer registration, filing support, auditing, and arrears management. For customs, the focus is on strengthening clearance processes (customs declaration, risk management, and audit) and cross border control (smuggling, valuation). On revenue policy, the RMS focuses on excises, VAT, widening the tax base, rationalizing tax incentives and holidays, and imposing property taxes.

[16] In late 2014, the government pledged to raise the civil servants' minimum monthly wage to US$250 by 2018 from about US$100 in 2013/14, matching the opposition's campaign promise.

revenue gains is expected to moderate.[17] Recent revenue increases relied heavily on strengthened auditing, which while welcome, should be accompanied by institutional improvements to sustain revenue performance.[18] Furthermore, revenue performance could disappoint if there are delays in deeper and broader tax reforms, or if the economy weakens. At the same time, public wages are projected to continue rising, while the government is facing mounting social spending pressures (Cambodia's development spending remains lower than that of peers). Reflecting these trends, the fiscal deficit is projected to widen to around 3½-4 percent of GDP and government deposits are projected to fall to 3.7 percent of GDP by 2021, below comfortable levels.[19] In the absence of a government debt market, maintaining adequate government deposits (the main source of financing to conduct countercyclical fiscal policy) will be essential for maintaining macroeconomic stability as they act as a buffer in the event of shocks. Staff analysis suggests that a government deposit level of about 5.5 percent of GDP is adequate to withstand a major shock. This will necessitate consolidation over the medium term, even though the Debt Sustainability Analysis (DSA) indicates a low risk of debt distress (see DSA).[20]

Development Expenditures--Comparatives 1/
(In percent of GDP)



Sources: IMF staff estimates; World Bank.

1/ Dashline is the average of EMAsia

22. Policy Recommendations.

- **Continued revenue increases are needed in view of rising spending pressures and to maintain an adequate fiscal buffer**. The government's target of raising domestic revenues by about 0.5 percent of GDP annually is welcome.[21] However, achieving this goal will require continued improvements in revenue administration and a modernization of tax policy. To continue improving tax administration, the authorities should systematically implement the RMS and continue with the reforms to improve institutional capacity (Box 5). Tax policy reforms should initially focus on rationalizing tax

[17] Staff has estimated the revenue to GDP norm for Cambodia, and the results indicate that Cambodia has scope to increase revenues by about 2-2.5 percent of GDP. However, between 2013-2015, the revenue-to-GDP ratio increased by 2.8 pp of GDP. Given the higher base and the authorities' plans to focus only on strengthening revenue administration (in line with the RMS) without introducing any new taxes until 2018, the pace of revenue gains in the near term is likely to moderate.

[18] In particular, progress in other key areas of the RMS, such as return filing management, arrears collection, transparent and simplified tax accounting and performance monitoring, is needed.

[19] Relative to the last Article IV Consultation, medium-term projections assume higher concessional project loans which finance increased development (education) and capital expenditures. Project loans are below the line, and the commensurate increases in expenditures have widened the fiscal deficit modestly over the medium term.

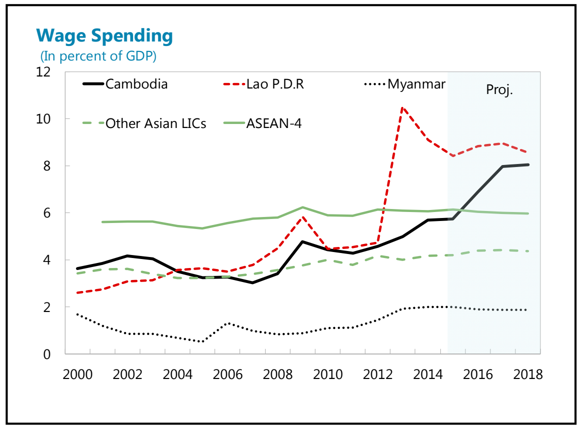
[20] Notwithstanding the low risk of debt distress, debt sustainability continues to be vulnerable to the materialization of contingent liabilities related to financial sector risks and PPPs.

[21] The average level of government deposits for 2000–15 was 4.6 percent of GDP. In the baseline (including gains from RMS reforms), their level is projected to decline below 4 percent of GDP by 2021. Furthermore, if the revenue-to-GDP ratio remains flat and concessional borrowing does not materialize, the fiscal deficit will widen while government deposits will be depleted. Thus, continued revenue efforts are needed to maintain adequate government deposits (estimated at about 5.5 percent of GDP).

incentives and excise taxes, and over the medium term aim at reforming VAT and personal income taxes, and increasing property taxes.

- **Development spending should be prioritized as revenue gains are secured.** Recent plans to boost social protection spending are welcome. However, public expenditure on education and health will still remain below low-income and emerging Asia country averages.

- **Wage increases should be fiscally sustainable and accompanied by continued efforts to accelerate civil service reforms.** Further wage increases should be contingent on meeting revenue targets and maintaining adequate fiscal buffers. The ongoing efforts to reform Cambodia's civil service sector, especially to strengthen the monitoring of work attendance and compensation systems through the adoption of IT systems, are welcome. Commendable efforts are also being made to strengthen human resource planning and recruitment across sectors. These efforts should continue, including to increase skills and efficiency of civil servants at all levels including management, and to enhance the transparency of public sector operations. In particular, balancing the goals of fiscal sustainability and competitive civil service salaries will require careful targeting of incentives and higher pay increases to priority functions and good performers.



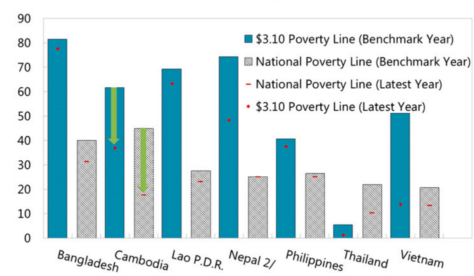
- **Domestically-financed public investment should be increased, while raising its efficiency and limiting contingent liabilities from Public Private Partnerships (PPPs).** Specific recommendations include: (i) increasing domestically-financed public investment to maintain public investment at about 8.5 percent of GDP financed by boosting revenues (to prepare for an eventual decline in external concessional financing as Cambodia's per capita income rises further); (ii) improving efficiency in all stages of the public investment process including planning, allocation and implementation, and (iii) developing an appropriately structured institutional framework for PPPs to reduce risks from contingent liabilities. In June 2016, the MEF adopted a policy on PPPs outlining legal, regulatory and institutional frameworks. In addition, a central PPP unit for risk management is being established in the MEF. Going forward, the preparation and selection of PPPs should be integrated with the overall investment strategy and the budget cycle, with clear procedures in place for budgeting, reporting, and accounting.

- **A Medium Term Fiscal Framework (MTFF) should be developed to systematically allocate expenditure and improve efficiency.** A MTFF will also integrate capital expenditure into the budgetary process, and allow for a better assessment of the trade-offs between various types of expenditures and their medium-term impact.

23. Authorities' views. The authorities broadly agreed with staff's assessment and key policy recommendations. On the revenue side, they agreed with the need to continue to boost revenues to maintain fiscal sustainability, but noted the need to strike a balance and meet other objectives such as promoting job creation and efficiency. They remained committed to continue implementing the RMS, along with improving the institutional framework for revenue administration. They plan to implement tax policy reforms over the medium term. On expenditures, they agreed on the importance of developing a MTFF to improve expenditure allocation efficiency and are currently reviewing the public expenditure framework. They are also planning to continue with civil service reforms to improve public services, but noted constraints to speedy implementation. They highlighted significant progress in increasing development spending, especially in health, primary education, and social assistance. They plan to use PPPs to enhance infrastructure and social spending, and acknowledged the need to develop a well-designed PPP framework.

C. Structural and Financial Sector Reforms to Enhance Sustainable and Inclusive Growth

Poverty Cross-Country Comparison 1/
(Poverty headcount ratio in percent of population)



Sources: World Development Indicators; and IMF staff estimates.
1/ Poverty headcount ratio at $3.10 a day is 2011 PPP adjusted.
2/ For Nepal, poverty headcount ratio at national poverty lines is only available in 2010.

24. Structural Constraints. Rapid growth over the past two decades has significantly reduced the poverty rate, which has fallen from 50 percent in 2005 to 18 percent in 2012, helping to reduce income inequality.[22] However, a large share of the population remains vulnerable at just above the poverty line. Also, despite rapid credit growth, financial access remains limited, which indicates that financial deepening has not been broad based.[23] Cambodia also faces structural constraints and vulnerabilities, including a narrow economic base, weak business climate, and high dollarization coupled with underdeveloped financial markets. These structural features constrain growth potential and render the economy and financial system vulnerable to shocks, while limiting the scope for responding to such shocks.

- **Narrow Economic Base**. Despite some early signs of diversification, Cambodia's export base remains narrow and reliant on low value-added garments. Garments production is highly substitutable between countries, and can migrate quickly to those with better price competitiveness. The government launched the Industrial Development Policy (IDP) in 2015 to attract FDI into non-garments labor-intensive manufacturing, and while recent FDI trends point to early signs of diversification, progress has been slow.

[22] Recent rapid growth has been associated with a reduction of inequality in Cambodia, with Gini coefficient falling from 0.41 in 2007 to 0.31 in 2012 (World Bank's World Development Indicators).

[23] According to the World Bank's Global Findex, the percentage of population having accounts increased (from 3.7 percent in 2011 to 22.2 percent in 2014), but remains low.

- **Weak Business Climate and Eroding Competitiveness**. Rising minimum wages and stalled productivity improvements, along with heightened uncertainty from labor disputes, have been eroding competitiveness. The cost of doing business remains high due to inadequate transportation links, elevated energy costs, nontransparent and onerous government procedures.

- **Dollarization**. High dollarization increases banks' vulnerability to solvency and liquidity risks, and limits the scope for exchange rate and monetary policies.

- **Underdeveloped Financial Markets**. There is no government bond market despite the need to channel domestic savings to finance growth-enhancing expenditure. The foreign exchange market remains thin and transactions center on small retail money changers. Limited financial markets impede the efficient allocation of resources and risk sharing, and constrain monetary policy implementation and the efficacy of fiscal policy, given the absence of financing instruments.

25. Business Climate Reforms. Efforts should focus on lowering the costs of doing business to boost competitiveness and create more employment opportunities in higher value-added industries. Priorities would include reducing energy costs, improving its reliability, enhancing transportation links, and addressing skills gaps via improving the quality of education and promoting technical and vocational training. Efforts should be made to accelerate the implementation of the IDP, which was formulated to improve the business climate. Additionally, strengthening the rule of law, and increasing the transparency of business regulation and tax compliance requirements will help create a more conducive business environment and encourage long-term investment.

26. Financial Market Development. Reforms should be geared towards increasing usage of the local currency and accelerating financial market development. While success in de-dollarization will be gradual, the development of interbank, government bond, and foreign exchange markets is needed to promote de-dollarization and allow for the eventual implementation of an effective monetary policy framework. Specifically, (i) expedite issuing shorter-term Negotiable Certificates of Deposits (NCD) to make the interbank market more liquid and move towards auction pricing, (ii) restructure the FX market and encourage banks (instead of money changers) to play a greater role, (iii) develop government bond markets in line with the authorities' Financial Sector Development Strategy (2011–2020), (iv) ensure proper supervision and regulation, (vi) adopt measures to encourage de-dollarization, potentially based on the draft national strategy to promote increased usage of local currency (see below).[24]

27. Authorities' views. The authorities remain committed to implementing the IDP and agreed with staff on the need to accelerate implementation. Both the Law on Investment and the Law on Special Economic Zones are under revision and aim to improve the business environment and support diversification, in line with IDP. The government has implemented various measures to

[24] Specific measures to encourage de dollarization, as noted in past Article IV staff reports, include imposing higher reserve requirements on foreign currencies liabilities relative to riel liabilities.

promote securities market development, and has also prepared rules and regulations for a government bond market (to be finalized by 2018). The NBC highlighted their efforts to develop the interbank market by supporting greater usage of NCDs. In line with government policy, the NBC remains committed to promoting the usage of local currency and has recently launched a new electronic payments and FAST system (Fast and Secure Transfer) system to better facilitate riel transactions. The national strategy to increase local currency usage, drafted by the NBC, is currently at the Economic and Financial Policy Committee for consideration.

STAFF APPRAISAL

28. Economic setting. Growth is projected to remain strong, driven by strong garments exports, real estate and construction activity as well as the reduction in oil prices, and notwithstanding weaker contributions from agriculture and tourism sectors. Inflation has increased slightly but is expected to remain well contained. Private sector credit growth has been and is projected to remain high, and is increasingly concentrated in the real estate and construction sectors. Medium-term growth is projected to moderate somewhat due to a gradual reduction in FDI, challenges in diversification, and a moderation in the credit cycle. The external position is assessed to be moderately weaker than suggested by fundamentals and desirable policies.

29. Risks. The outlook is subject to downside risks. On the external side, a significant slowdown in China would spill over through the FDI, banking and tourism channels. A surge in the US dollar and/or weaker growth in Europe could weigh on garments exports. Also, a sharper-than-anticipated tightening in global financial conditions could raise funding costs and heighten liquidity risks in the financial system. On the domestic side, the ongoing credit boom poses significant risks to macro-financial stability and growth. Other domestic risks include fiscal pressures and erosion of competitiveness from wage hikes potentially outstripping productivity gains.

30. Financial sector policies. Securing a soft landing of the credit cycle and continuing to build capital and liquidity buffers through well-coordinated and sequenced prudential policy tools will be key to containing rising macro-financial risks. On the micro-prudential side, regulations on asset classification, provisioning, and sectoral loan classification need to be strengthened. Well-designed macro-prudential tools should be gradually introduced, including implementing countercyclical capital buffers and provisions, imposing concentration limits and higher risk weights for real-estate loans, and instituting limits on LTD ratios. The prompt corrective action framework should be strengthened and a crisis management framework should be put in place with more explicit inter-agency coordination mechanisms.

31. Monetary policy and other prudential tools need to be used to further contain rapid credit growth. Reserve requirements should be raised, particularly on short-term foreign currency deposits and foreign borrowing. Well-designed and targeted fiscal measures, such as stamp duties, a capital gains tax, and tightening the issuance of new construction permits should be used to manage the real estate cycle.

32. **Supervision and financial market development.** Strong supervision is essential to ensure proper risk identification and enforce micro and macro prudential policies. In this respect, the implementation of FSAP recommendations should be expedited including continued supervisory capacity building. With the growing systemic relevance of large MFIs, strengthening regulation to prevent regulatory arbitrage is warranted. Reforms to reduce dollarization and to develop the interbank, government bond, and foreign exchange markets are needed to build an effective monetary policy framework.

33. **Fiscal Policy.** To ensure that the recent revenue gains are sustained over the medium-term, reforms should focus on modernizing tax policy and further improving revenue administration. Tax policy reforms should center on improving the productivity, efficiency and transparency of most taxes, and rationalize tax incentives, improve business taxation, and reform excise and property taxes. Tax administration reforms should focus on building a strong institutional framework to entrench recent administrative improvements and implement future reforms. On the expenditure side, developing a medium-term budget framework to systematically allocate expenditures and improve spending efficiency would be key going forward. An appropriately structured institutional framework for PPPs is also needed to limit contingent liabilities. Wage increases should be fiscally sustainable and be accompanied by continued efforts to enhance civil service reforms.

34. **Structural reforms** are needed to secure inclusive and sustained growth. These should include promoting diversification, enhancing competitiveness, and improving the business climate and inclusiveness. A focus should be on accelerating the implementation of the Industrial Development Policy to boost investor confidence, implementing key infrastructure projects (in energy and transportation), strengthening the rule of law and transparency/predictability of business regulation, and further investing in education and skills building.

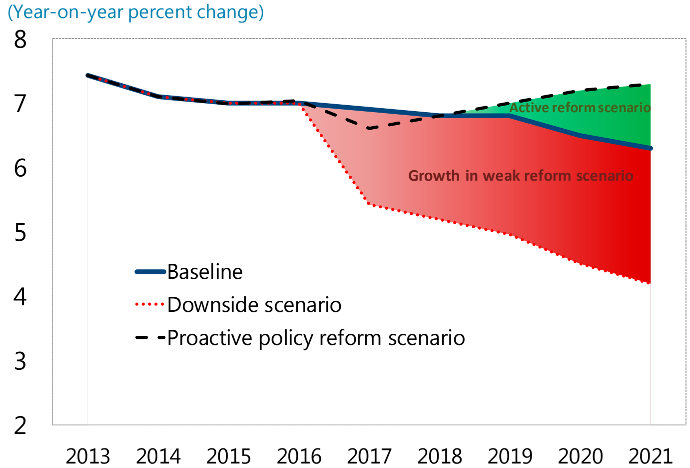
35. It is recommended that the next Article IV consultation takes place on the standard 12-month cycle.

Box 1. Cambodia: Proactive Policy Reform and Weak Reform Scenarios[1]

This box illustrates projections of medium-term GDP growth in a proactive policy reform scenario, compared with a weak-reform scenario. The scenarios suggest that (1) decisively moderating the pace of credit growth and boosting potential growth through supply-side reforms will yield substantial benefits, after an initial adjustment period, in terms of higher and safer growth. Conversely (2) in the weak-reform scenario, growth may initially be somewhat higher but at the cost of significantly weaker growth down the road and, most importantly, and increasing risk of a 'hard landing" (sharply reduced growth and/or financial crisis).

- **Proactive policy reform scenario.** This assumes implementation of key structural reforms, including the investment law, which would boost investor confidence, timely management of planned infrastructure projects, and investments in education and skills building. These policies are projected to boost the country's growth potential. At the same time, policies that mitigate rising financial sector vulnerabilities and engineer a soft landing of the real estate and credit cycle will reduce risk of a 'hard landing' and boost confidence in the government's policy framework. These measures together are predicted to generate economic growth that averages 7 percent or above. Thus, by 2021, GDP would be about 8 percent higher than in the weak reform scenario, and—most importantly—the risk of a hard landing/financial crisis would be much reduced.
- **Weak reform scenario.**[2] This scenario assumes no significant supply-side reforms and continuing rapid credit growth. In particular, the 'credit-to-GDP ratio' would continue to grow over the medium term, to around 125 percent by 2021. As a result, the risk of a sharp slowdown of growth or a financial crisis—which is already non-trivial given the duration of the credit boom since 2011—would continue to grow (quantified based on the BIS framework for crisis probability in a credit boom). The resulting risk-adjusted growth outlook in the weak-reform scenario is shown as a 'fan chart' below the projected non-crisis path of GDP in the baseline.

Figure 1. Real GDP Growth
(Year-on-year percent change)



[1] Prepared by Mari Ishiguro and Sohrab Rafiq.

[2] The upper bound (blue line) in weak reform scenario refers to a scenario absent of proactive reforms and crisis and is equivalent to the baseline scenario in the macroframework, while the lower bound refers to growth in a 'hard-landing' scenario adjusted by the probability of such a scenario.

Box 2. Cambodia: External Sector Assessment[1]

The external position is assessed to be moderately weaker than implied by fundamentals and desirable policy settings. The real effective exchange rate is assessed to be moderately overvalued by around 5–10 percent. There is room to build reserves given high dollarization and elevated financial vulnerabilities.

BoP Developments. Cambodia's external position in 2015 (CA balance of -10.6 percent of GDP) is assessed to be moderately weaker than suggested by fundamentals and desirable policy settings. The estimated cyclically-adjusted current account deficit is slightly larger than the norm determined by fundamentals and desirable policies (2.6 percentage points of GDP weaker than the norm using the macro balance approach of the Fund's EBA-lite exercise, which translates into a REER overvaluation of around 5.7 percent). Much of the misalignment in the external sector can be explained by the current calibration of credit and monetary (and to a lesser extent fiscal) policies away from the most desirable policy settings, which are looser than would be optimal given the economic cycle.

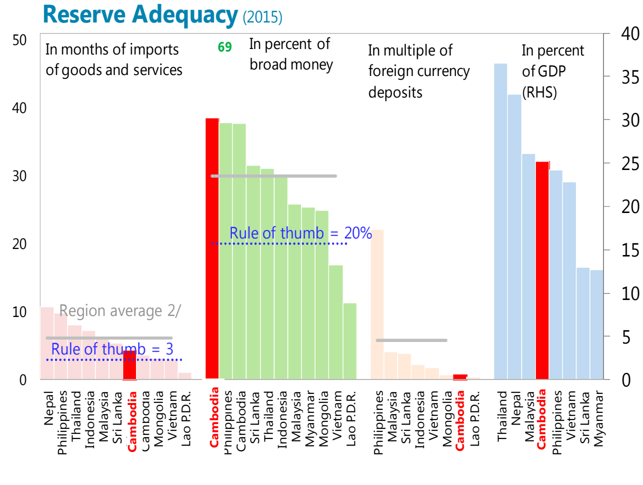
External Balance Assessment Results

Current account gap (percent of GDP)	2.6
Implied over(+)/under(-) valuation from CA	5.7
REER gap, level regression (percent)	10.1

Source: IMF Staff estimates

Exchange Rate Assessment. Since end-2015, the REER has appreciated by around 8 percent (year-on-year). The appreciation reflects the nominal rise in the US dollar against major trading partner countries (EU and China), buoyant economic growth, and inflows of foreign banking flows. The REER is assessed to be overvalued by around 5–10 percent, which implies that a 5–10 percent real effective depreciation would be necessary to close the gap between the underlying current account and the level that can be explained by fundamentals and desirable policies. The overvaluation, in the absence of an independent exchange rate regime, calls for policies to slow credit growth in the near term, and consolidate the fiscal position and improve productivity and competitiveness over the medium term.

Reserve Adequacy (2015)



Sources: IMF staff calculations.

Reserve Adequacy. Reserve coverage, in terms of FX deposits, has been declining. In December 2015, reserves were equivalent to about 4 months of prospective imports of goods and services. Measured against several traditional metrics, Cambodia's gross international reserves appear to be adequate, also considering the long-term nature of most of Cambodia's external debt. Reserve adequacy metrics for LICs suggests the optimal level of reserves in an open economy with a managed exchange rate like Cambodia to be around 4 months of imports.[2] However, foreign currency deposits are still more than two times gross official reserves, which severely limits the central bank's lender of last resort capacity, and is lower than regional comparators. Customizing the Jeanne and Ranciere (2006) model, which incorporates high dollarization and financial fragilities when assessing reserve adequacy, suggests that the optimal level of reserves ranges from 28 to 30 percent of GDP, which is equivalent to additional reserves of US$250 to US$480 million. The authorities should continue to accumulate reserves beyond the level suggested by traditional reserve adequacy metrics to enhance resilience against financial sector vulnerabilities and rapid capital flow reversals.

[1] Prepared by Sohrab Rafiq.

[2] See External Balance Assessment method in the 2015 External Sector Report. Also see Board paper "Assessing Reserve Adequacy—Specific Proposals" (2015).

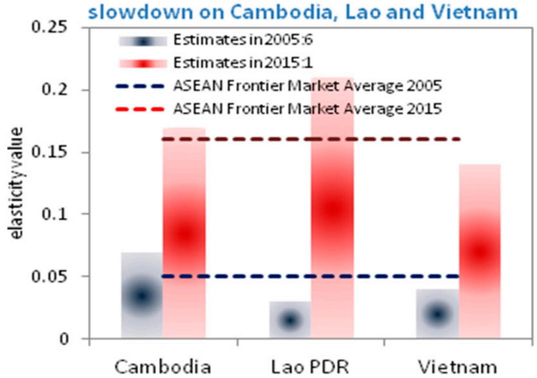
Box 3. Cambodia: Real and Financial Spillovers from China to Cambodia[1]

Increased economic integration over the last 15 years has resulted in larger real and financial spillovers from China to Cambodia. To preserve macro stability in the face of rising vulnerability to regional shocks, policy frameworks, including moving towards greater monetary flexibility, need to be strengthened.

A high degree of openness suggests that Cambodia is vulnerable to spillover effects from China via a number of potential transmission channels:

- FDI and official flows: Chinese companies invest in the garment sector to take advantage of Cambodia's preferential tariffs with the EU. China is the largest provider of official flows to Cambodia.
- Banking sector flows: Chinese banks, reliant on wholesale funding, have sizeable market share in Cambodia.
- Tourism: Chinese citizens have contributed most to Cambodia tourism growth in recent years.

Growth elasticity of a China growth slowdown on Cambodia, Lao and Vietnam

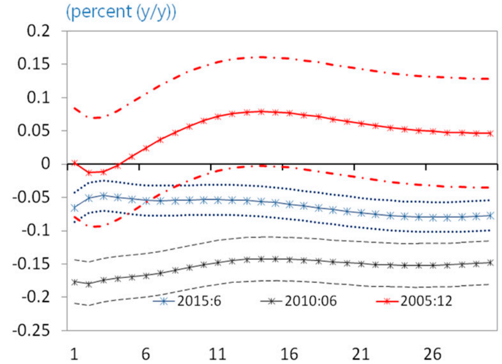


Source: IMF staff calculations

Trade and financial linkages between Cambodia and China have grown. To assess the spillovers from Chinese economic shocks to Cambodia (real and financial effects), a time-varying structural dynamic factor model is estimated.[2] The main results are:

- **Cambodia's growth elasticity to China's growth is around 0.2 percent.** This is double the magnitude compared to 10 years ago, which is consistent with Cambodia's strengthening regional trade and financial integration.
- **A slowdown in Chinese growth tightens credit conditions in Cambodia and leads to declining credit growth**. This effect has strengthened since the global financial crisis. The findings imply that stronger growth in China, through a compression in risk premia, could contribute to the pro-cyclicality of credit flows into Cambodia.

Response of Cambodia Credit Growth to a One Percent China Slowdown
(percent (y/y))



As trade and financial linkages grow, Cambodia is increasingly likely to be buffeted by external shocks, including from China. To preserve financial stability, policy frameworks need to be strengthened, including reforms to allow for greater monetary flexibility to cope with regional shocks, and financial safety nets need to be widened and deepened to build resilience. The findings also call for enhancing surveillance of cross-border financial flows to derive a more comprehensive picture of the deeper network of interconnections and spillovers to Cambodia, as well as identification of associated data gaps and working toward their closure.

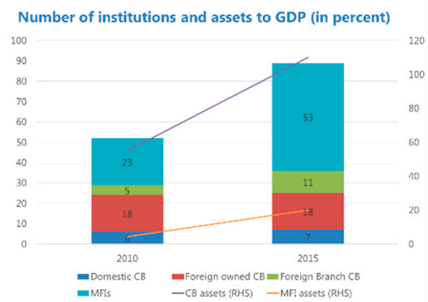
[1] Prepared by Sohrab Rafiq.

[2] Rafiq, S. (2016), "When China Sneezes, Does ASEAN Catch a Cold?," IMF Working Paper (forthcoming).

Box 4. Cambodia: Upgrading Nonbank Regulations[1]

Rapid growth of deposit-taking micro-finance institutions (MFIs) have rendered them systemically important. Regulations need to be tightened and be brought in line with banks to adequately contain potential risks and prevent regulatory arbitrage.

Regulators face the twin challenges of closing regulation gaps between banks and MFIs and mitigating stability risks from rapidly growing MFI lending. The bank assets-to-GDP ratio has grown from 55 percent in 2010 to 110 percent as of 2015, while MFI assets-to-GDP ratio has grown rapidly from 4 percent to 20 percent. The largest deposit-taking MFI (MDI) is equivalent in terms of total assets to the 7th largest bank. MDIs are competing with banks for the same funding base while being subject to different regulations, creating room for regulatory arbitrage. There are four possible financial stability risks that could result: (1) credit risk (risk of highly-indebted households rolling over debt), (2) liquidity risk (sudden withdrawals of deposits and/or squeeze in foreign borrowing), (3) FX risk (currency mismatch between deposits in U.S. dollars and lending in local currency), and (4) systemic risks due to increased interconnectedness between MFIs and banks.



In general, regulations on deposit-taking MFIs should be broadly in line with those of commercial banks though some principles require tailoring. As with other forms of financial regulation, the primary aim is to ensure the stability of the financial system and to protect depositors without imposing undue compliance burdens or stifling lending. MFIs pose an additional layer of complexity in that the industry's need for flexibility to innovate and grow must be balanced with rules and restrictions to protect low-income and vulnerable clients (CGAP, 2012). Thus, regulations should aim to (i) reduce risk of regulatory arbitrage and (ii) minimize costs created by additional regulation for MFIs. Supervision should be proportionate to the risks involved, while keeping in mind stretched supervisory capacity.

Recommendations.

(1) The CAR should be aligned with Basel II and III principles. While current regulations apply equally to MDIs and banks, actual CARs are, on average, lower than that of banks. If MDIs' ability to raise additional capital is limited compared to banks, or they exhibit a more pronounced risk profile, the minimum CAR should be set higher than that for banks.

(2) Asset classification should be standardized for all banks and MFIs.

(3) Reserve requirements (RR), including on foreign currency deposits, for MDIs should be adjusted to be in line with banks. Since MFIs are more reliant on foreign financing, RR on foreign borrowings should be instituted to all MFIs and applied based on the maturity profile of borrowings (short term borrowings). To limit the impact on the financial system and financial inclusion, implementation should be gradual.

(4) The NBC must constantly evaluate how effectively MFIs are managing potential currency mismatches, including cross-border financing arrangements with international lenders, and consider further restricting MDI's net open position should risks abruptly rise.

(5) Clear identification of systemically important MDIs is needed and routine monitoring of interbank, inter-MFIs, inter-financial institutions linkages should be strengthened.

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[1] Prepared by Mari Ishiguro.

Box 5. Cambodia: Domestic Resource Mobilization[1]

An ambitious set of tax reforms are needed to provide adequate resources to meet Cambodia's development and infrastructure needs. The strategy should be two-pronged via strengthening tax policy and continuing improvements in revenue administration.

Tax Policy. There is room for improvement in productivity, efficiency and transparency. Significant reforms are needed across all tax categories with immediate emphasis on improving the productivity of business profits taxes. A priority is to eliminate the "tax notches" between small and medium enterprises by applying a flat tax rate structure to profits.

- **Tax incentives.** The framework needs to be rationalized and streamlined, including for withholding taxes on interest, dividends and other payments to foreign investors.
- **Property taxes** should be raised gradually.
- **Patent and business tax** The patent tax should be eliminated, and the current system of minimum turnover tax should be replaced with a modern advanced payment system.
- **Excise taxes** should be rationalized and all ad valorem rates should be replaced with specific rates.
- **VAT exemptions** on utility sales (electricity and water) should eliminated.
- **Personal income tax**. A comprehensive PIT scheme including on pensions and capital income should be developed, once a well-designed administrative framework is in place.

Tax Administration. Reforms on tax policy should move alongside the development of a strong institutional framework for revenue administration. The General Department of Taxation (GDT) needs to be strengthened to be able to implement the major tax policy reforms while increasing taxpayer compliance levels in an ever-more sophisticated economic environment. Thus, the GDT needs to establish an effective tax headquarters with the capacity to drive the ongoing reforms under the RMS and implement any proposed policy changes. This will involve:

- Improving core functional areas such as taxpayer education to increase awareness of tax compliance laws, and return filing management and tax arrears collection that ensure equitable tax enforcement across businesses and sectors;
- Implementing the simplified accounting format to replace the estimated regime and enhancing large and medium taxpayer compliance.
- Strengthening performance monitoring including on RMS progress would require developing a set of broader performance indicators for the GDT that would also enhance transparency.

On the customs, the emphasis should be on effective implementation of the strategic plan adopted by General Department of Customs and Excise (GDCE) and program development capacities in customs valuation and post-clearance audit. GDCE's customs enforcement and compliance strategy should also include an anti-smuggling policy and action plan. Opportunities also exist for increased cooperation and sharing of information between GDCE and GDT.

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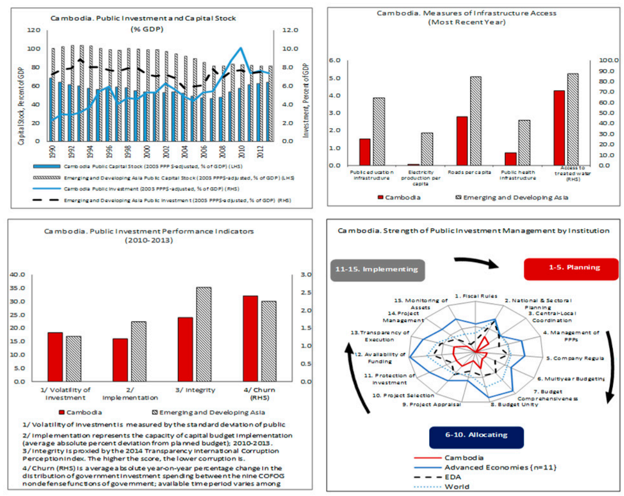
[1] Prepared by Manuk Ghazanchyan, Debra Adams, David Wentworth, Hebous Shafik, and Janos Nagy.

Box 6. Cambodia: Public Investment, Efficiency, and Growth[1, 2]

Infrastructure gaps are large and the public investment management process is inefficient. Continuing to mobilize revenues and channeling them to public investment, while improving its efficiency, will boost growth.

Large infrastructure gaps exist in Cambodia, despite increasing public investment. Cambodia compares unfavorably on infrastructure outcomes relative to Emerging and Developing Asia (EDA). Lagging areas include electricity, public education, and public health outcomes. The last two decades have seen public investment (as percent of GDP) increase and converge to the EDA average. However, Cambodia's public capital stock and private investment still lag the EDA average.

Test Figure 1. Cambodia: Public Capital and Infrastructure Indicators



Source: FAD; Staff assessments.

Low public investment efficiency has hampered public capital accumulation. Improvement is needed across all areas of the Public Investment Management Assessment (PIMA) framework including: (i) moving to multi-year budgeting, (ii) protection of investment and monitoring of assets, (iii) budget comprehensiveness and fiscal rules and (vi) the management of PPPs. Strengthening the PPP framework requires better managing and monitoring fiscal risks related to PPPs, while fully integrating PPPs into the government's overall investment strategy, medium-term fiscal framework, and budget cycle.

Limited domestic financing sources constrains any attempt to boost public capital spending. A projected decline in donor support with the attainment of LMIC status and limited progress in developing local debt markets, means options for increasing public investment going forward is tied to success in boosting revenues, and implementing well-structured PPPs.

Public investment is estimated to have a strong positive effect on growth in Cambodia. A gradual scaling up of public investment by around 2 p.p. of GDP over 8 years, in which investment is financed by improved revenue collection and learning-by-doing productivity improvements, would increase Cambodia's real GDP growth by around 2 percentage points with little risk to long-term public debt sustainability.[3]

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[1] Prepared by Manuk Ghazanchyan.

[2] This box is based on the forthcoming IMF Working Paper, "Public Investment and Growth: Experience of Selected Asian Frontier Markets" by Manuk Ghazanchyan, Ricardo Marto, Jiri Jonas and Kaitlin Douglass. Cambodia is a pilot case in the on-going initiative on the Fund's new focus on infrastructure investment, in the context of the "Infrastructure Policy Support Initiative.

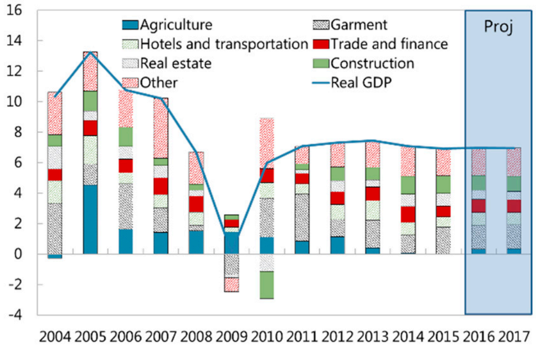
[3] We adopted the DIG model for Cambodia from Buffie, Edward F., and others, 2012, "Public Investment, Growth, and Debt Sustainability: Putting Together the Pieces," IMF Working Paper 12/144 (Washington: International Monetary Fund).

Figure 1. Cambodia: Robust Growth Amid Elevated Risks

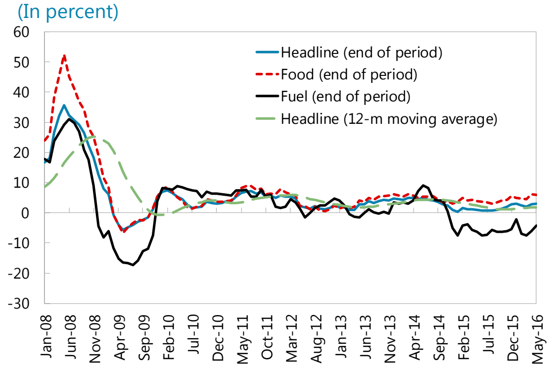
Economic growth remains strong supported by garment exports, tourism, and real-estate.

Inflation remains contained due to low commodity prices.

Contribution to Growth
(In percent)



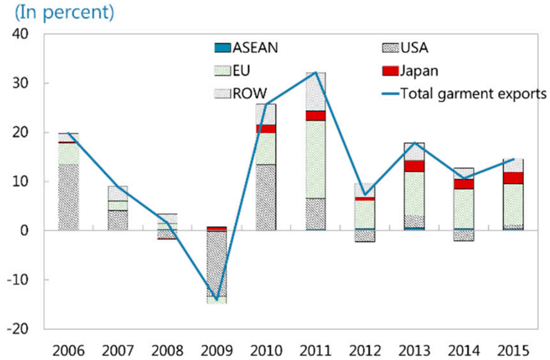
Inflation
(In percent)



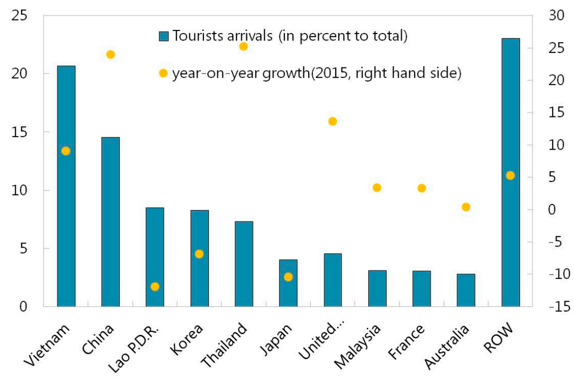
Garment exports grew strongly despite exchange rate appreciation…

…while tourist arrivals have been strong, particularly from China.

Garment Export Growth (contribution by destination)
(In percent)



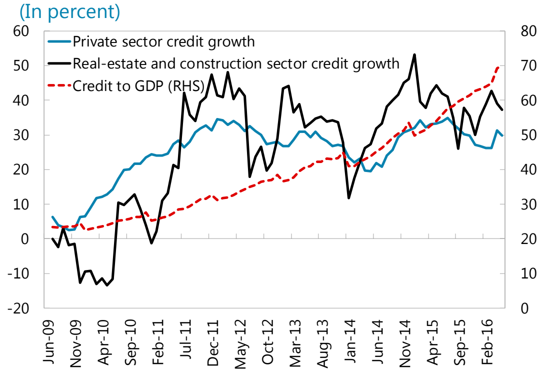
Tourists arrivals (top ten markets)



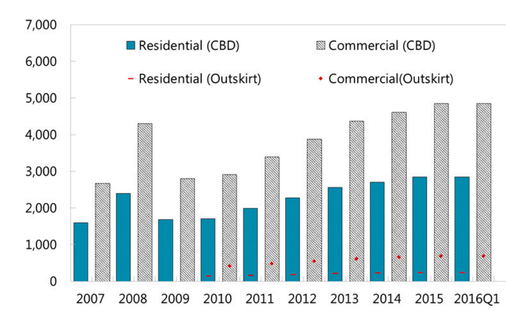
Rapid credit growth particularly in construction and real estate sectors…

…as well as and rising real estate prices are increasing macro-financial risks.

Private credit growth
(In percent)



Average Land Market Price, 2007–16
($/sqm)



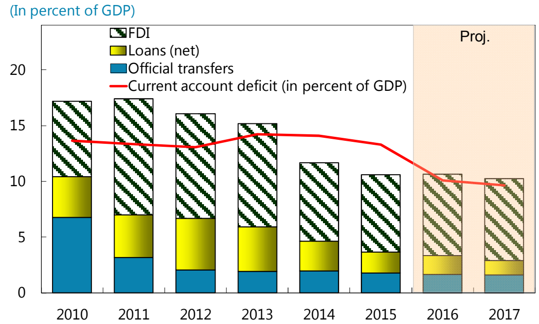
Sources: Bonna Realty Group; and IMF staff calculations.

Sources: Cambodian authorities; IMF's World Economic Outlook; and IMF staff estimates.

Figure 2. Cambodia: External Position Stable

The current account deficit has been narrowing owing to lower commodity prices and strong garment export growth…

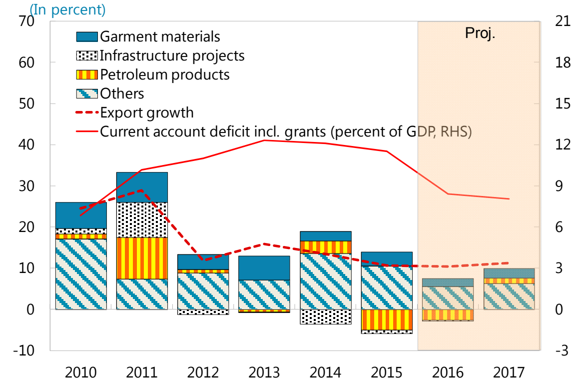
Current Account Deficit and Financing Flows
(In percent of GDP)



1/ Current account balance excluding official transfers.

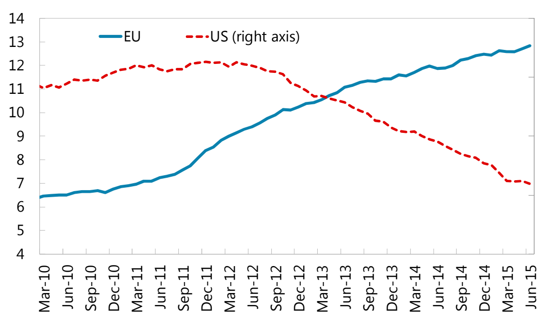
…while import growth is projected to slow due to lower oil prices and the completion of key hydro power projects.

Contribution to Import Growth
(In percent)



Cambodia's share in the EU garment market continues to rise, and while TPP may accelerate the fall in share of the US market.

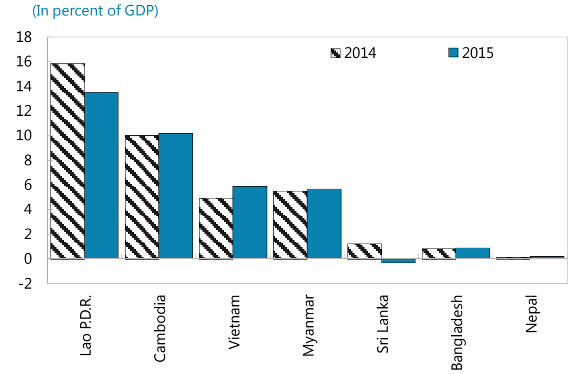
Garment Export Market Share 1/
(In percent, 12mma)



1/ Share of Cambodia in Asian LICs' (Bangladesh, Cambodia, Sri Lanka, and Vietnam) garment exports.

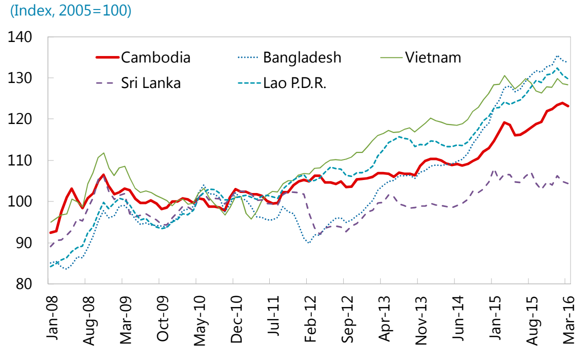
FDI continued to grow strongly in 2015 due to more garment factory investment

Foreign Direct Investment
(In percent of GDP)



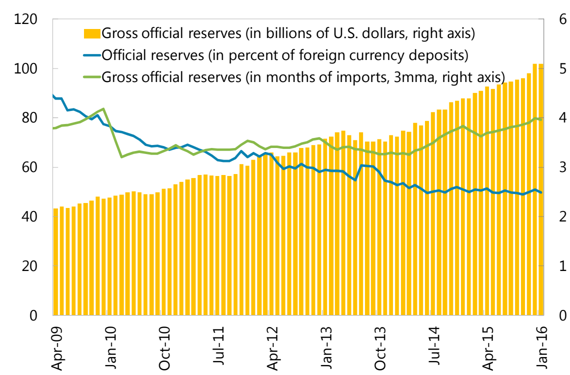
The real effective exchange rate has appreciated since 2015 due to a stronger U.S. dollar…

Real Effective Exchange Rate
(Index, 2005=100)



…resulting in further reserve accumulation, though reserve coverage in terms of FX deposits has declined.

Official Reserves

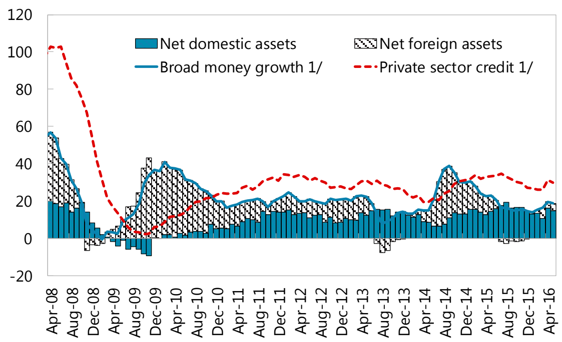


Sources: Cambodian authorities; and IMF staff estimates.

Figure 3. Cambodia: Rising Risks from Rapid Credit Growth

Broad money growth has been slowing down with net foreign assets turning negative…

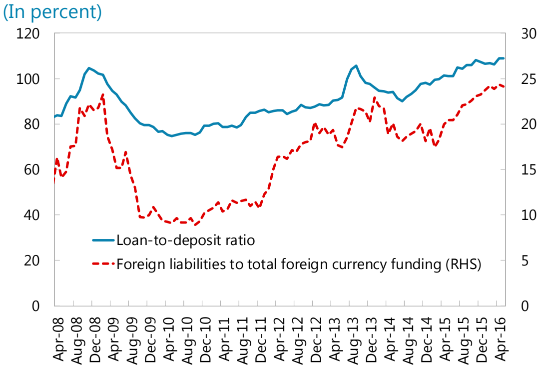
Monetary Development, 2008–16
(In percent)



1/ Year-on-year percent change.

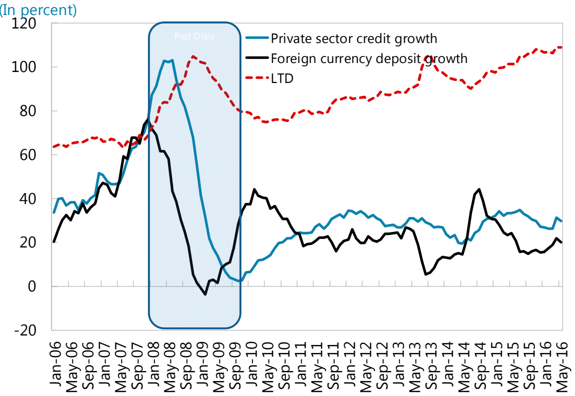
… due to increase in foreign funding , resulting in the average loan-to-deposit ratio breaching 100 percent.

Foreign Liabilities to Total Foreign Funding
(In percent)



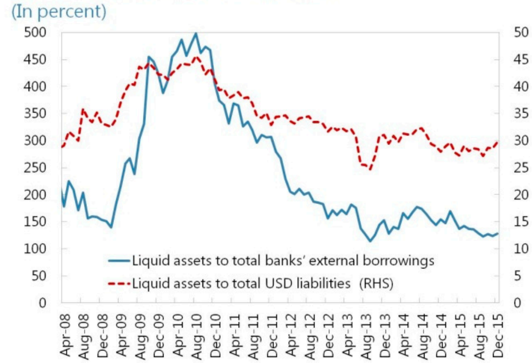
LTD is rising due to gap between still high credit growth and decreasing foreign currency deposit growth.

Credit Growth, Foreign Currency Deposit Growth and LTD
(In percent)



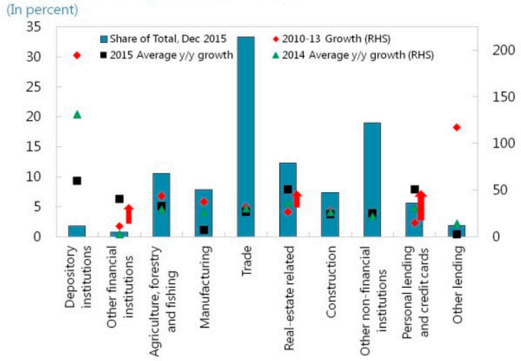
Liquid assets are falling in terms of foreign flows and need to be rebuilt.

Liquid assets to banks' USD liabilities
(In percent)



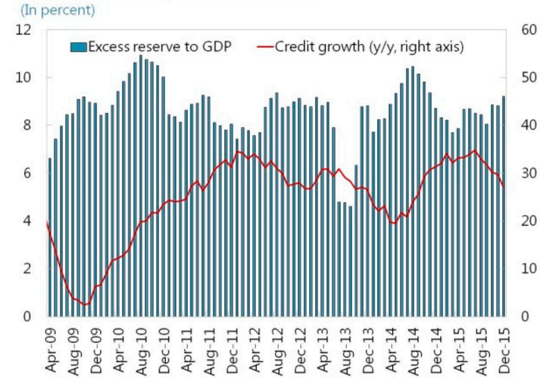
Credit growth has been increasingly channeled into real-estate, other financial institutions, and personal lending sectors.

Credit growth by Economic Sector
(In percent)



Meanwhile, the excess reserves to GDP remains high under the absence of interbank market.

Credit to the Economy and Excess Reserves
(In percent)

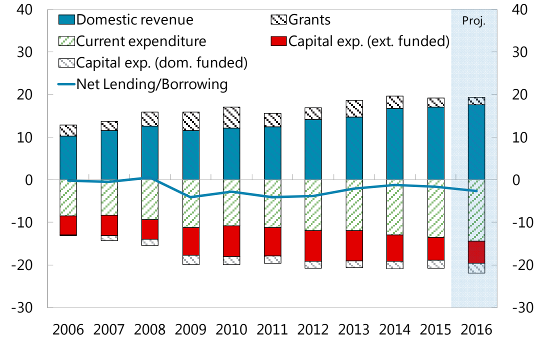


Sources: Cambodian authorities; and IMF staff estimates.

Figure 4. Cambodia: Robust Revenues Performance Amid Spending Pressures

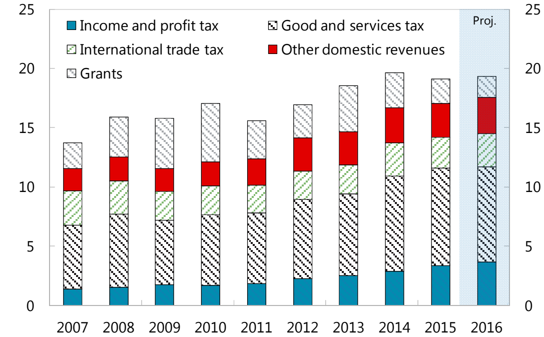
Fiscal performance is still strong owing to robust revenue performance but the spending mix is deteriorating.

Fiscal Balance
(In percent of GDP)



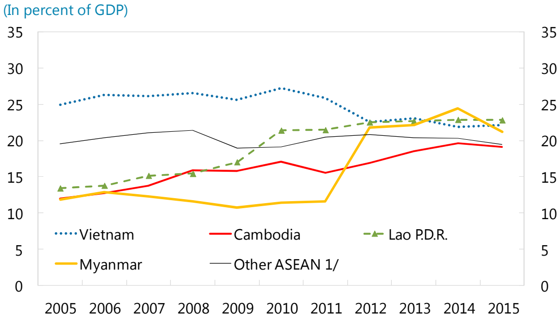
Revenue performance continues to be enhanced by strong collection efforts.

Fiscal Revenues
(In percent of GDP)



However, Cambodia's fiscal revenues are still below those of many LICs.

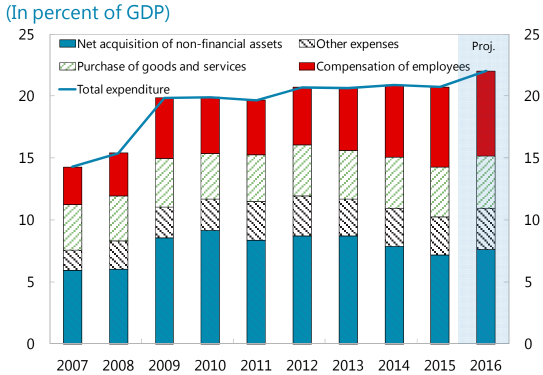
Total Revenue and Grants in Asian LICs
(In percent of GDP)



Sources: Cambodian authorities; and IMF staff estimates.
1/ Average of Indonesia, Malaysia, Singapore, Philippines, and Thailand.

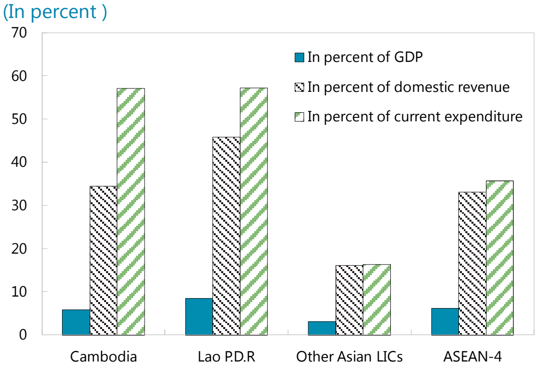
Public wages have been rising, squeezing other expenditures...

Goverment Spending
(In percent of GDP)



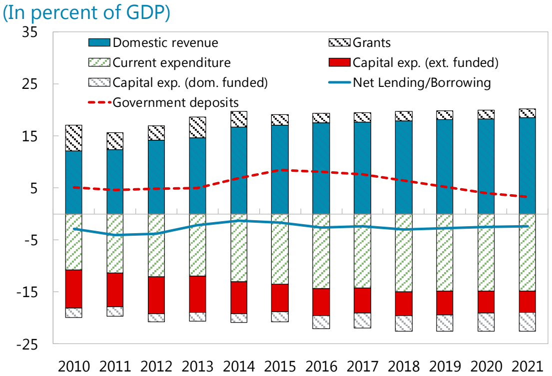
...resulting in public wages that are higher than that of most other Asian LICs.

Wage Spending, 2015
(In percent)



Efforts are needed to maintain fiscal sustainability while making space for development and capital spending.

Medium-term Fiscal Outlook
(In percent of GDP)

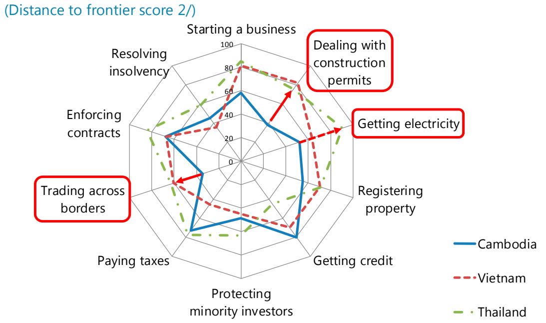


Sources: Cambodian authorities, IMF staff estimates.

Figure 5. Cambodia: Considerable Structural Challenges to Growth and Resilience

Cambodia's doing business indicators lags its peers on some dimensions.

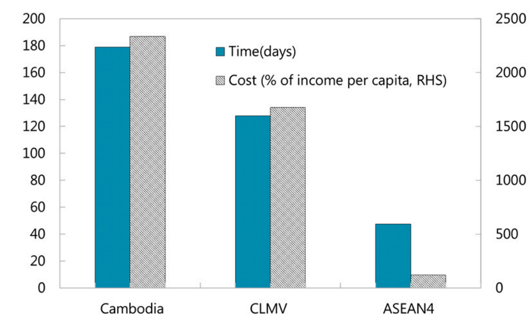
Doing Business Indicators Cross Country Comparison 1/
(Distance to frontier score 2/)



1/ These indicators should be interpreted with caution due to a limited number of respondents, a limited geographical coverage, and standardized assumptions on business constraints and information availability.
2/ On a scale of 0 to 100; 100 is the frontier and 0 is the furthest from the frontier.

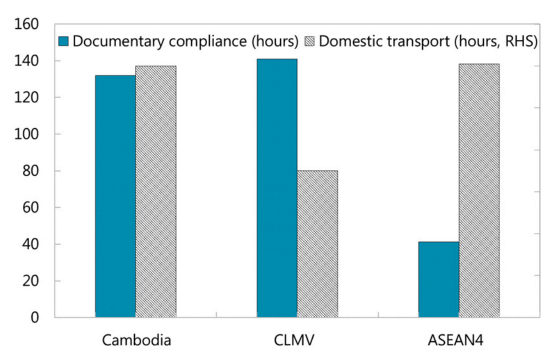
Electricity costs are higher and access less efficient than peers.

Getting electricity



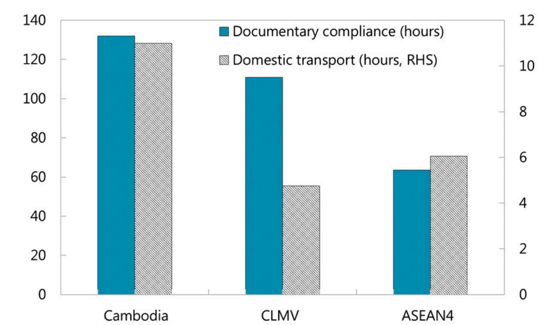
Processing time has also been higher compared to peers both for exports…

Trading across borders — export



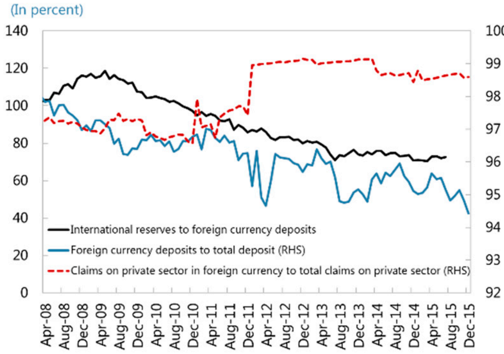
… and imports.

Trading across borders — import



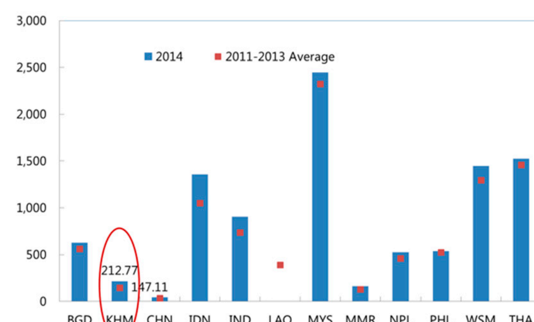
Cambodia's dollarization level remains high, while reserve cover of FX deposits has been falling.

Dollarization
(In percent)



Financial access is lower than peers, notwithstanding rapid credit growth.

Deposit account with commercial banks per 1,000 adults



Sources: Cambodian authorities; IMF's World Economic Outlook; and IMF staff estimates.

Table 1. Cambodia: Selected Economic Indicators, 2011–17

	2011	2012	2013	2014	2015	2016	2017
					Est.	Proj.	
Output and prices (annual percent change)							
GDP in constant prices	7.1	7.3	7.4	7.1	7.0	7.0	6.9
(Excluding agriculture)	8.6	8.4	9.4	9.2	9.0	8.7	8.4
Inflation (end-year)	4.9	2.5	4.7	1.0	2.8	3.2	2.9
(Annual average)	5.5	2.9	3.0	3.9	1.2	3.1	2.7
Saving and investment balance (in percent of GDP)							
Gross national saving	11.8	12.5	11.2	11.1	11.8	12.7	13.6
Government saving	0.8	1.9	2.2	3.4	4.0	3.4	2.5
Private saving	11.0	10.6	9.0	7.7	7.8	9.4	11.0
Gross fixed investment	22.0	23.5	23.5	23.2	22.4	22.9	23.0
Government investment	8.7	9.0	8.9	7.9	7.0	7.8	8.1
Private investment 1/	13.3	14.5	14.6	15.3	15.4	15.1	14.9
Money and credit (annual percent change, unless otherwise indicated)							
Broad money	21.4	20.9	14.6	29.9	14.7	19.9	10.2
Private sector credit	31.2	28.0	26.7	31.3	27.1	26.0	24.4
Velocity of money 2/	2.0	2.0	2.0	2.0	2.0	2.0	2.0
Public finance (in percent of GDP)							
Revenue	15.6	16.9	18.6	19.6	18.8	19.7	20.5
Domestic revenue	12.4	14.1	14.6	16.7	16.6	17.8	17.9
Of which : Tax revenue	10.2	11.3	11.8	13.7	14.6	14.9	15.0
Grants	3.2	2.8	3.9	2.9	2.3	1.9	2.6
Expenditure	19.7	20.7	20.7	20.9	20.4	22.3	23.4
Expense	11.3	12.0	12.0	13.0	13.2	14.5	15.4
Net acquisition of nonfinancial assets	8.4	8.7	8.7	7.9	7.2	7.8	8.0
Net lending (+)/borrowing(-)	-4.1	-3.8	-2.1	-1.3	-1.6	-2.6	-2.9
Net lending (+)/borrowing(-) excluding grants 3/	-7.5	-6.3	-6.4	-4.2	-2.9	-4.3	-5.5
Net acquisition of financial assets	0.0	0.6	0.5	2.3	2.8	1.1	1.0
Net incurrence of liabilities 4/	4.1	4.4	2.6	3.6	4.4	3.7	3.9
Of which: Domestic financing	1.4	0.7	-0.6	-1.4	-0.8	-1.1	-0.3
Government deposits	4.6	4.9	5.0	6.8	9.1	9.3	8.7
Balance of payments (in millions of dollars, unless otherwise indicated)							
Exports, f.o.b. 5/	5,035	5,633	6,530	7,408	8,461	9,363	10,337
(Annual percent change)	28.9	11.9	15.9	13.4	14.2	10.7	10.4
Imports, f.o.b.	-7,730	-8,600	-9,744	-10,997	-12,145	-13,147	-14,515
(Annual percent change)	32.9	11.3	13.3	12.9	10.4	8.3	10.4
Current account (including official transfers)	-1,303	-1,547	-1,880	-2,032	-1,889	-1,969	-1,973
(In percent of GDP)	-10.2	-11.0	-12.3	-12.1	-10.6	-10.2	-9.4
Gross official reserves 6/	3,032	3,463	3,642	4,391	5,271	6,322	7,421
(In months of prospective imports)	3.6	3.6	3.4	3.7	4.1	4.5	4.8
External debt (in millions of dollars, unless otherwise indicated)							
Public external debt	3,833	4,474	4,852	5,291	5,645	6,238	6,926
(In percent of GDP)	29.7	31.5	31.6	31.8	32.1	32.6	33.3
Public debt service	77	85	112	143	172	189	249
(In percent of exports of goods and services)	1.0	1.0	1.1	1.3	1.4	1.4	1.7
Memorandum items:							
Nominal GDP (in billions of riels) 7/	52,069	56,682	61,390	67,740	73,423	81,978	90,318
(In millions of U.S. dollars)	12,818	14,057	15,244	16,778	17,789	19,368	20,937
Exchange rate (riels per dollar; period average)	4,062	4,032	4,027	4,038	4,127	…	…

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

1/ From 2011, includes FDI related to public-private power sector projects.
2/ Ratio of nominal GDP to the average stock of broad money.
3/ According to GFS 86 used by Cambodian authorities.
4/ Includes statistical discrepancy.
5/ Trade data has been revised backward to 2008.
6/ Excludes unrestricted foreign currency deposits held as reserves at the National Bank of Cambodia; starting in 2009, includes the new SDR allocations made by the IMF of SDR 68.4 million.
7/ GDP data have been revised backward to 2010.

Table 2. Cambodia: Medium-Term Macroeconomic Framework, 2011–21

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
					Est.			Proj.			
Output and prices (percent change)											
GDP at constant prices	7.1	7.3	7.4	7.1	7.0	7.0	6.9	6.8	6.8	6.5	6.3
GDP deflator	3.4	1.4	0.8	3.1	1.3	4.4	3.1	3.0	3.1	3.1	3.1
Consumer prices (end-year)	4.9	2.5	4.7	1.0	2.8	3.2	2.9	3.0	3.0	3.0	3.0
Saving and investment balance (in percent of GDP)											
Gross national saving	11.8	12.5	11.2	11.1	11.8	12.7	13.6	14.1	14.6	14.6	14.6
Government saving	0.8	1.9	2.2	3.4	4.0	3.4	2.5	1.4	0.9	0.9	0.9
Private saving	11.0	10.6	9.0	7.7	7.8	9.4	11.0	12.6	13.7	13.7	13.7
Gross fixed investment	22.0	23.5	23.5	23.2	22.4	22.9	23.0	23.0	23.0	23.0	23.0
Government investment	8.7	9.0	8.9	7.9	7.0	7.8	8.1	8.0	8.1	8.2	8.3
Private investment 1/	13.3	14.5	14.6	15.3	15.4	15.1	14.9	15.0	14.9	14.8	14.7
Private credit growth (percent change)	31.2	28.0	26.7	31.3	27.1	26.7	23.9	22.0	22.0	22.0	22.0
Public finance (in percent of GDP)											
Revenue	15.6	16.9	18.6	19.6	18.8	19.7	20.5	21.3	22.0	21.3	21.5
Domestic revenue	12.4	14.1	14.6	16.7	16.6	17.8	17.9	18.1	18.1	18.2	18.2
Of which: Tax revenue	10.2	11.3	11.8	13.7	14.6	14.9	15.0	15.2	15.2	15.2	15.3
Grants	3.2	2.8	3.9	2.9	2.3	1.9	2.6	3.3	3.8	3.1	3.3
Total expenditure	19.7	20.7	20.7	20.9	20.4	22.3	23.4	24.6	25.3	25.4	25.6
Expense	11.3	12.0	12.0	13.0	13.2	14.5	15.4	16.6	17.3	17.3	17.3
Net acquisition of nonfinancial assets	8.4	8.7	8.7	7.9	7.2	7.8	8.0	8.0	8.1	8.1	8.3
Of which: Domestically-financed	1.8	1.6	1.7	1.7	2.3	1.8	1.6	0.5	0.1	0.8	1.4
Net lending (+)/borrowing(-)	-4.1	-3.8	-2.1	-1.3	-1.6	-2.6	-2.9	-3.3	-3.4	-4.1	-4.1
Net lending (+)/borrowing(-) excluding grants	-7.5	-6.3	-6.4	-4.2	-2.9	-4.3	-5.5	-6.6	-7.2	-7.3	-7.4
Net acquisition of financial assets	0.0	0.6	0.5	2.3	2.8	1.1	1.0	0.3	0.2	-0.1	-0.9
Net incurrence of liabilities	4.1	4.4	2.6	3.6	4.4	3.7	3.9	3.6	3.6	4.0	3.2
Domestic financing, net	1.4	0.7	-0.6	-1.4	-0.8	-1.1	-0.3	-0.2	0.1	1.0	1.7
Government deposits	4.6	4.9	5.0	6.8	9.1	9.3	8.7	8.2	7.4	5.7	3.7
Balance of payments (in percent of GDP, unless otherwise indicated)											
Exports (percent change) 2/	28.9	11.9	15.9	13.4	14.2	10.7	10.4	10.6	10.1	11.0	10.9
Imports (percent change) 3/	32.9	11.3	13.3	12.9	10.4	-8.3	-10.5	-10.9	-10.6	-9.8	-9.3
Current account balance (including transfers)	-10.2	-11.0	-12.3	-12.1	-10.6	-10.2	-9.4	-8.9	-8.4	-8.4	-8.4
(Excluding transfers)	-13.3	-13.1	-14.2	-13.9	-12.3	-11.9	-12.0	-12.1	-11.9	-11.6	-11.2
Foreign direct investment 4/	11.6	12.1	12.0	10.0	9.2	9.1	9.1	9.1	8.9	8.9	8.9
Other flows 5/	2.0	1.9	1.5	6.5	6.2	6.4	5.5	5.3	5.0	4.7	4.0
Overall balance	3.4	3.0	1.1	4.3	4.9	5.4	5.2	5.4	5.5	5.1	4.4
Gross official reserves (in millions of U.S. dollars) 6/	3,032	3,463	3,642	4,391	5,271	6,322	7,421	8,669	10,051	11,430	12,734
(In months of next year's imports)	3.6	3.6	3.4	3.7	4.1	4.5	4.8	5.1	5.3	5.6	5.7
Public external debt (in millions of U.S. dollars)	3,337	3,833	4,474	5,037	5,645	6,238	6,926	7,697	8,505	9,351	10,108
(In percent of GDP)	29.7	31.5	31.6	31.8	32.1	32.6	33.3	34.0	34.6	35.1	35.0
Public external debt service (in millions of U.S. dollars)	77	85	112	143	172	189	249	306	355	448	506
(In percent of exports of goods and services)	1.0	1.0	1.1	1.3	1.4	1.4	1.7	1.9	2.0	2.3	2.4

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

1/ Includes nonbudgetary, grant-financed investment, and, from 2011, public-private partnerships in the power sector projects.

2/ Excludes re-exported goods.

3/ Excludes imported goods for re-export; from 2011, includes imports related to public-private power sector projects.

4/ From 2011, includes FDI related to public-private power sector projects.

5/ Net official disbursements, exceptional financing, and official transfers.

6/ Excludes unrestricted foreign currency deposits held as reserves at the National Bank of Cambodia; starting in 2009, includes the new SDR allocations made by the IMF.

Table 3. Cambodia: Balance of Payments, 2011–21 (BPM5)

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
				Est.			Proj.				
Current account (including official transfers)	-1,303	-1,547	-1,880	-2,032	-1,889	-1,969	-1,973	-2,025	-2,076	-2,267	-2,435
(Excluding official transfers)	-1,711	-1,835	-2,171	-2,328	-2,193	-2,308	-2,508	-2,755	-3,001	-3,094	-3,177
Trade balance	-2,695	-2,967	-3,214	-3,590	-3,683	-3,784	-4,178	-4,650	-5,185	-5,530	-5,811
Exports, f.o.b.	5,035	5,633	6,530	7,408	8,461	9,363	10,337	11,431	12,589	13,974	15,492
Of which: Garments	3,937	4,245	4,911	5,334	6,246	6,848	7,449	8,095	8,809	9,601	10,478
Imports, f.o.b. 1/	-7,730	-8,600	-9,744	-10,997	-12,145	-13,147	-14,515	-16,081	-17,775	-19,504	-21,304
Of which: Garments-related	-1,752	-2,012	-2,483	-2,694	-3,216	-3,493	-3,799	-4,128	-4,405	-4,608	-4,610
Petroleum	-1,118	-1,179	-1,123	-1,397	-1,106	-1,012	-1,297	-1,503	-1,716	-1,940	-2,173
Services and income (net)	812	1,008	954	965	946	934	1,083	1,236	1,442	1,604	1,719
Services (net)	1,410	1,658	1,735	1,815	1,945	2,038	2,147	2,283	2,433	2,609	2,779
Of which: Tourism (credit)	2,084	2,463	2,660	2,947	3,063	3,233	3,444	3,680	3,930	4,208	4,465
Income (net)	-598	-649	-781	-850	-999	-1,105	-1,064	-1,047	-991	-1,006	-1,061
Private transfers (net)	172	124	89	297	544	542	586	660	742	832	915
Official transfers (net)	408	288	291	296	304	339	535	730	925	827	743
Capital and financial account	1,741	1,969	2,047	2,483	2,585	2,849	3,060	3,261	3,446	3,633	3,725
Medium- and long-term loans (net)	490	649	613	473	390	522	588	634	662	679	584
Disbursements	532	695	676	555	498	648	754	835	899	975	914
Amortization	-41	-47	-63	-83	-108	-126	-165	-201	-237	-296	-331
Foreign direct investment 2/	1,484	1,698	1,826	1,677	1,645	1,771	1,911	2,061	2,211	2,377	2,575
Net foreign assets of deposit money banks 3/	40	-330	180	-209	550	556	561	567	572	577	566
Unrestricted foreign currency deposit at NBC	127	-256	-59	-95	150	152	153	155	156	156	156
Commercial banks	-87	-73	240	-114	400	404	408	412	416	420	410
Other short-term flows and errors and omissions	-273	-48	-571	542	0	0	0	0	0	0	0
Overall balance	438	423	168	729	867	1,040	1,087	1,236	1,369	1,366	1,290
Financing	-438	-423	-168	-729	-867	-1,040	-1,087	-1,236	-1,369	-1,366	-1,290
Change in gross official reserves 4/	-454	-438	-184	-745	-879	-1,052	-1,099	-1,248	-1,382	-1,379	-1,304
Use of IMF credit	0	0	0	0	0	0	0	0	0	0	0
Debt restructuring	0	0	0	0	0	0	0	0	0	0	0
Accumulation of arrears	16	15	16	16	12	12	12	12	13	13	14
Memorandum items:											
Current account balance (in percent of GDP)											
Excluding official transfers	-13.3	-13.1	-14.2	-13.9	-12.3	-11.9	-12.0	-12.1	-12.1	-11.5	-10.9
Including official transfers	-10.2	-11.0	-12.3	-12.1	-10.6	-10.2	-9.4	-8.9	-8.4	-8.4	-8.4
Trade balance (in percent of GDP)	-21.0	-21.1	-21.1	-21.4	-20.7	-19.5	-20.0	-20.4	-21.0	-20.6	-20.0
Gross official reserves 5/	3,032	3,463	3,642	4,391	5,271	6,322	7,421	8,669	10,051	11,430	12,734
(In months of next year's imports)	3.6	3.6	3.4	3.7	4.1	4.5	4.8	5.1	5.3	5.6	5.7

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

1/ From 2011, includes imports related to public-private power sector projects.
2/ From 2011, includes FDI related to public-private power sector projects.
3/ Includes unrestricted foreign currency deposits (FCDs) held as reserves at the National Bank of Cambodia (NBC).
4/ Excludes changes in unrestricted FCDs held as reserves at the NBC, and changes in gold holdings and valuation.
5/ Excludes unrestricted FCDs held at the NBC; starting in 2009, includes the new SDR allocations made by the IMF of SDR 68.4 million.

Table 4. Cambodia: General Government Operations, 2010–21 (GFSM 2001)

	2011	2012	2013	2014	2015		2016		2017	2018	2019	2020	2021
	Actual	Actual	Actual	Actual	Budget	Est.	Budget	Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
						(In billions of riels)							
Revenue	8,114	9,590	11,392	13,304	12,152	13,837	14,288	16,159	18,528	21,196	23,993	25,569	28,200
Of which: Nongrant	6,436	8,017	8,991	11,307	11,525	12,168	14,038	14,611	16,150	17,939	19,836	21,792	23,863
Tax	5,289	6,424	7,265	9,297	9,424	10,719	11,453	12,222	13,536	15,054	16,604	18,242	20,104
Income, profits, and capital gains	960	1,276	1,561	1,964	2,069	2,472	2,472	3,009	3,447	3,792	4,172	4,717	5,323
Good and services	3,123	3,815	4,210	5,450	5,395	6,238	6,462	6,902	7,561	8,487	9,446	10,315	11,301
International trade and transactions	1,206	1,333	1,493	1,883	1,961	2,009	2,519	2,311	2,528	2,775	2,986	3,210	3,481
Grants	1,678	1,572	2,401	1,997	627	1,669	250	1,548	2,379	3,257	4,157	3,776	4,337
Other revenues 1/	1,147	1,593	1,726	2,010	2,101	1,449	2,585	2,389	2,614	2,884	3,232	3,550	3,759
Total expenditure	10,236	11,741	12,686	14,160	15,231	14,977	18,163	18,277	21,127	24,472	27,699	30,529	33,620
Expense	5,888	6,818	7,351	8,838	9,939	9,717	11,885	11,859	13,867	16,502	18,896	20,765	22,716
Compensation of employees	2,290	2,660	3,119	3,952	4,768	4,941	5,636	5,636	6,697	8,000	8,847	9,712	10,640
Purchase of goods and services	1,962	2,310	2,400	2,798	2,941	2,941	3,474	3,430	4,136	4,777	5,713	6,271	6,871
Interest	160	305	439	232	276	223	335	337	324	328	268	295	309
Expense not elsewhere classified	1,476	1,543	1,393	1,856	1,954	1,612	2,440	2,456	2,710	3,398	4,069	4,487	4,896
Net acquisition of nonfinancial assets	4,348	4,922	5,335	5,322	5,291	5,260	6,279	6,418	7,260	7,970	8,802	9,764	10,904
Of which: Externally financed	3,403	4,023	4,306	4,147	3,687	3,594	4,228	4,982	5,807	7,502	8,713	8,750	9,001
Net lending (+)/borrowing(-)	-2,123	-2,151	-1,294	-856	-3,078	-1,139	-3,875	-2,118	-2,598	-3,276	-3,706	-4,960	-5,420
Net acquisition of financial assets	-3	363	308	1,564	-156	2,070	0	919	919	284	250	-102	-1,214
Net incurrence of liabilities 2/	2,119	2,514	1,603	2,420	2,923	3,209	3,875	3,037	3,518	3,560	3,956	4,857	4,206
Of which: External	1,779	2,350	1,943	2,115	2,923	1,835	3,875	3,168	2,973	3,631	3,779	3,935	3,458
						(In percent of GDP)							
Revenue	15.6	16.9	18.6	19.6	16.6	18.8	17.4	19.7	20.5	21.3	22.0	21.3	21.5
Nongrant	12.4	14.1	14.6	16.7	15.7	16.6	17.1	17.8	17.9	18.1	18.1	18.2	18.2
Tax	10.2	11.3	11.8	13.7	12.8	14.6	14.0	14.9	15.0	15.2	15.2	15.2	15.3
Income, profits, and capital gains tax	1.8	2.3	2.5	2.9	2.8	3.4	3.0	3.7	3.8	3.8	3.8	3.9	4.0
Good and services tax	6.0	6.7	6.9	8.0	7.3	8.5	7.9	8.4	8.4	8.5	8.6	8.6	8.6
International trade and transactions tax	2.3	2.4	2.4	2.8	2.7	2.7	3.1	2.8	2.8	2.8	2.7	2.7	2.6
Grants	3.2	2.8	3.9	2.9	0.9	2.3	0.3	1.9	2.6	3.3	3.8	3.1	3.3
Other revenues	2.2	2.8	2.8	3.0	2.9	2.0	3.2	2.9	2.9	2.9	3.0	3.0	2.9
Total expenditure	19.7	20.7	20.7	20.9	20.7	20.4	22.2	22.3	23.4	24.6	25.3	25.4	25.6
Expense	11.3	12.0	12.0	13.0	13.5	13.2	14.5	14.5	15.4	16.6	17.3	17.3	17.3
Compensation of employees	4.4	4.7	5.1	5.8	6.5	6.7	6.9	6.9	7.4	8.1	8.1	8.1	8.1
Purchase of goods and services	3.8	4.1	3.9	4.1	4.0	4.0	4.2	4.2	4.6	4.8	5.2	5.2	5.2
Interest	0.3	0.5	0.7	0.3	0.4	0.3	0.4	0.4	0.4	0.3	0.2	0.2	0.2
Expense not elsewhere classified	2.8	2.7	2.3	2.7	2.7	2.2	3.0	3.0	3.0	3.4	3.7	3.7	3.7
Net acquisition of nonfinancial assets	8.4	8.7	8.7	7.9	7.2	7.2	7.7	7.8	8.0	8.0	8.1	8.1	8.3
Of which: Externally-financed	6.5	7.1	7.0	6.1	5.0	4.9	5.2	6.1	6.4	7.6	8.0	7.3	6.8
Net lending (+)/borrowing(-)	-4.1	-3.8	-2.1	-1.3	-4.2	-1.6	-4.7	-2.6	-2.9	-3.3	-3.4	-4.1	-4.1
Net acquisition of financial assets	0.0	0.6	0.5	2.3	-0.2	2.8	0.0	1.1	1.0	0.3	0.2	-0.1	-0.9
Net incurrence of liabilities	4.1	4.4	2.6	3.6	4.0	4.4	4.7	3.7	3.9	3.6	3.6	4.0	3.2
Of which: External	3.4	4.1	3.2	3.1	4.0	2.5	4.7	3.9	3.3	3.7	3.5	3.3	2.6
Memorandum items:													
Net lending (+)/borrowing(-) excluding grant 3/	-7.5	-6.3	-6.4	-4.2	-4.9	-2.9	-4.8	-4.3	-5.5	-6.6	-7.2	-7.3	-7.4
Domestic financing	1.4	0.7	-0.6	-1.4	0.2	-0.8	0.0	-1.1	-0.3	-0.2	0.1	1.0	1.7
Government deposits	4.6	4.9	5.0	6.8	...	9.1	...	9.3	8.7	8.2	7.4	5.7	3.7
GDP (in billions of riels)	52,069	56,682	61,390	67,740	73,423	73,423	81,978	81,978	90,318	99,337	109,297	119,979	131,442

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

1/ Includes provincial tax and nontax revenue.

2/ Includes statistical discrepancy.

3/ The figure can be different from the domestic financing figure in Table 5 (GFSM 1986) because of differences in classification, in particular for capital revenue.

Table 5. Cambodia: General Government Operations, 2011–16 (GFSM 1986)

	2011 1/	2012	2013	2014	2015		2016	
	Actual	Actual	Actual	Actual	Budget	Est.	Budget	Proj.
				(In billions of riels)				
Total revenue	6,822	8,596	9,264	11,584	11,659	12,538	14,359	14,742
Of which: Central government	6,417	8,104	8,738	10,960	10,994	11,202	13,538	13,921
Tax revenue	5,092	6,208	7,035	9,092	9,801	12,176	12,333	13,617
Direct taxes	960	1,276	1,561	1,964	2,069	2,472	2,647	3,009
Indirect taxes	4,132	4,932	5,474	7,127	7,100	8,368	8,908	9,077
Of which: Trade taxes	1,093	1,218	1,366	1,760	1,831	2,009	2,146	2,300
Provincial taxes	385	465	501	591	632	1,336	778	821
Nontax revenue	959	1,344	1,435	1,580	1,724	1,577	1,896	1,704
Capital revenue 2/	386	579	293	321	134	121	131	131
Total expenditure	10,744	12,176	13,213	14,416	15,230	14,644	18,284	18,291
Current expenditure	5,997	6,946	7,647	8,959	9,939	9,507	11,825	11,859
Wages	2,233	2,598	3,057	3,862	4,566	4,517	5,636	5,636
Nonwage	3,521	4,348	4,591	5,097	4,709	4,550	5,521	5,521
Provincial expenditure	243	308	401	532	664	440	668	668
Capital expenditure	4,548	5,122	5,475	5,384	5,291	5,137	6,458	6,432
Locally financed	1,145	1,100	1,169	1,237	1,604	1,543	2,231	1,450
Externally financed	3,403	4,023	4,306	4,147	3,687	3,594	4,228	4,982
Net lending	198	107	91	73	0	0	0	0
Overall balance	-3,922	-3,579	-3,949	-2,832	-3,571	-2,106	-3,924	-3,550
Financing	3,922	3,579	3,949	2,832	3,571	2,106	3,924	3,550
Foreign (net)	3,457	3,923	4,344	4,112	3,550	3,504	3,612	4,716
Grants	1,678	1,572	2,421	2,042	627	1,421	250	1,548
Loans	1,943	2,541	2,165	2,382	3,360	2,414	3,871	3,681
Amortization	-164	-190	-242	-312	-437	-330	-509	-513
Domestic (net) 3/	465	-344	-395	-1,280	21	-1,398	312	-1,167
Total revenue	13.1	15.2	15.1	17.1	16.0	17.1	17.5	18.0
Of which: Central government	12.3	14.3	14.2	16.2	15.1	15.3	16.5	17.0
Tax revenue	9.8	11.0	11.5	13.4	13.5	16.6	15.0	16.6
Direct taxes	1.8	2.3	2.5	2.9	2.8	3.4	3.2	3.7
Indirect taxes	7.9	8.7	8.9	10.5	9.8	11.4	10.9	11.1
Of which: Trade taxes	2.1	2.1	2.2	2.6	2.5	2.7	2.6	2.8
Provincial taxes	0.7	0.8	0.8	0.9	0.9	1.8	0.9	1.0
Nontax revenue	1.8	2.4	2.3	2.3	2.4	2.1	2.3	2.1
Capital revenue 2/	0.7	1.0	0.5	0.5	0.2	0.2	0.2	0.2
Total expenditure and net lending	20.6	21.5	21.5	21.3	20.9	19.9	22.3	22.3
Current expenditure	11.5	12.3	12.5	13.2	13.7	12.9	14.4	14.5
Wages	4.3	4.6	5.0	5.7	6.3	6.2	6.9	6.9
Nonwage	6.8	7.7	7.5	7.5	6.5	6.2	6.7	6.7
Provincial expenditure	0.5	0.5	0.7	0.8	0.9	0.6	0.8	0.8
Capital expenditure	2.2	9.0	8.9	7.9	7.3	7.0	7.9	7.8
Locally financed	2.2	1.9	1.9	1.8	2.2	2.1	2.7	1.8
Externally financed	6.5	7.1	7.0	6.1	5.1	4.9	5.2	6.1
Net lending	0.4	0.2	0.1	0.1	0.0	0.0	0.0	0.0
Overall balance	-7.5	-6.3	-6.4	-4.2	-4.9	-2.9	-4.8	-4.3
Financing	7.5	6.3	6.4	4.2	4.9	2.9	4.8	4.3
Foreign (net)	6.6	6.9	7.1	6.1	4.9	4.8	4.4	5.8
Grants	3.2	2.8	3.9	3.0	0.9	1.9	0.3	1.9
Loans	3.7	4.5	3.5	3.5	4.6	3.3	4.7	4.5
Amortization	-0.3	-0.3	-0.4	-0.5	-0.6	-0.4	-0.6	-0.6
Domestic (net) 3/	0.9	-0.6	-0.6	-1.9	0.0	-1.9	0.4	-1.4
Memorandum item:								
GDP (in billions of riels)	52,069	56,682	61,390	67,740	72,767	73,423	81,978	81,978
Government deposits (percent of GDP)	4.6	4.9	5.0	6.8	...	9.1	...	9.3

1/ Includes supplementary budget.
2/ Includes privatization proceeds.
3/ Includes statistical discrepancy. The figure is different from the domestic financing figure in Table 4 (GFSM 2001) because of differences in classification, in particular for capital revenue.

Table 6. Cambodia: Monetary Survey, 2011–17

	2011	2012	2013	2014	2015				2016	2017
				Dec	Mar	Jun	Sep	Dec	Dec Proj.	Dec Proj.
	(In billions of riels)									
Net foreign assets	18,426	21,265	21,260	26,700	26,823	27,975	26,359	26,666	33,127	39,717
National Bank of Cambodia	16,010	18,583	19,535	24,476	24,904	27,443	27,485	29,490	36,539	42,846
Foreign assets	16,435	19,003	19,957	24,880	25,284	27,837	27,876	29,875	36,968	43,275
Foreign liabilities	425	421	421	404	380	394	391	385	428	428
Deposit money banks	2,416	2,682	1,725	2,224	1,919	533	-1,126	-2,824	-3,412	-3,129
Foreign assets	4,714	8,721	8,564	10,005	9,981	10,452	10,067	9,439	10,487	11,264
Foreign liabilities	2,298	6,038	6,839	7,782	8,062	9,920	11,192	12,263	13,899	14,393
Net domestic assets	5,215	7,327	11,508	15,860	16,863	18,178	20,601	22,158	25,409	24,769
Domestic credit	14,898	19,312	24,827	31,885	32,695	35,329	37,874	39,642	51,606	65,787
Government (net)	-2,123	-2,486	-2,795	-4,359	-5,064	-5,666	-5,933	-6,429	-6,436	-6,426
Private sector	17,021	21,793	27,609	36,245	37,759	40,995	43,807	46,071	58,042	72,214
Other items (net)	-9,684	-11,985	-13,318	-16,026	-15,832	-17,151	-17,273	-17,485	-26,197	-41,018
Broad money	23,640	28,592	32,768	42,560	43,686	46,154	46,960	48,823	58,536	64,486
Narrow money	3,956	4,046	4,878	6,308	6,628	6,293	6,288	6,741	8,066	8,881
Currency in circulation	3,772	3,756	4,454	5,593	5,884	5,633	5,653	5,897	7,072	7,792
Demand deposits	185	290	424	715	744	660	635	845	993	1,090
Quasi-money	19,684	24,546	27,890	36,251	37,058	39,861	40,673	42,082	50,470	55,605
Time deposits	557	780	945	1,090	1,065	1,159	1,448	1,550	1,859	2,048
Foreign currency deposits	19,127	23,766	26,945	35,161	35,993	38,701	39,224	40,532	48,612	53,557
	(12-month percentage change)									
Net foreign assets	8.0	15.4	0.0	25.6	14.9	6.6	-1.7	-0.1	24.2	19.9
Private sector credit	31.2	28.0	26.7	31.3	32.1	33.9	31.8	27.1	26.0	24.4
Broad money	21.4	20.9	14.6	29.9	24.2	20.6	15.2	14.7	19.9	10.2
Of which: Currency in circulation	21.7	-0.4	18.6	25.6	21.6	18.7	10.1	5.4	19.9	10.2
Foreign currency deposits	20.7	24.3	13.4	30.5	24.3	20.7	14.7	15.3	19.9	10.2
	(Contribution to year-on-year growth of broad money, in percentage points)									
Net foreign assets	7.0	12.0	0.0	16.6	0.4	3.3	-0.8	-0.1	13.2	11.3
Net domestic assets	14.3	8.9	14.6	13.3	2.9	6.1	11.6	14.8	6.7	-1.1
Domestic credit 1/	20.8	18.7	19.3	21.5	2.3	9.0	14.7	18.2	24.5	24.2
Government (net)	0.0	-1.5	-1.1	-4.8	-2.0	-3.4	-3.9	-4.9	0.0	0.0
Private sector	20.8	20.2	20.3	26.4	4.3	12.4	18.6	23.1	24.5	24.2
Other items (net)	-6.4	-9.7	-4.7	-8.3	0.6	-2.9	-3.1	-3.4	-17.8	-25.3
Memorandum items:										
Foreign currency deposits (in millions of U.S. dollars)	4,736	5,949	6,745	8,628	8,976	9,444	9,623	9,697	11,344	12,334
(In percent of broad money)	80.9	83.1	82.2	82.6	82.4	83.9	83.5	83.0	83.0	83.1
Riel component of broad money	4,513	4,826	5,823	7,399	7,693	7,452	7,736	8,291	9,925	10,929
(In percent of broad money)	19.1	16.9	17.8	17.4	17.6	16.1	16.5	17.0	17.0	16.9
Credit to the private sector (in millions of U.S. dollars)	4,214	5,455	6,911	8,894	9,416	10,004	10,748	11,022	13,544	16,630
(In percent of GDP)	32.7	38.4	45.0	53.5	51.4	55.8	59.7	62.7	70.8	80.0
Foreign Currency Loans	16,583	21,609	27,368	35,677	37,200	40,421	43,233	45,424	57,227	71,199
Loan-to-deposit ratio (in percent) 2/	86.7	90.9	101.6	101.5	103.4	104.4	110.2	112.1	117.7	132.9
Velocity 3/	2.0	2.0	2.0	2.0	1.7	1.7	1.6	2.0	2.0	2.0
Money multiplier (broad money/reserve money)	2.1	2.2	2.2	2.3	2.3	2.3	2.3	2.2	2.1	2.1
Reserve money (12-month percent change)	7.7	19.0	13.0	24.6	20.6	19.0	10.9	21.7	21.3	10.2

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

1/ Revisions of monetary survey to exclude banks' credits to nonresident.

2/ Foreign currency loans and deposits only.

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

Table 7. Cambodia: Core Financial Soundness Indicators (FSIs), 2013–15

(In percent)

	2013				2014				2015			
	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.
Capital-based FSIs												
Regulatory capital to risk-weighted assets	24.9	25.0	25.2	24.2	23.9	22.6	21.3	20.4	22.0	21.6	20.9	21.0
Nonperforming loans net of provisions to capital	3.4	3.7	4.1	3.9	3.3	3.7	4.0	3.3	4.1	4.6	4.4	3.3
Return on equity 1/	14.3	13.0	13.2	12.1	15.3	15.7	15.8	15.5	17.4	17.5	17.2	16.3
Net open position in foreign exchange to capital	1.5	1.3	0.9	1.2	1.1	1.4	1.4	1.3	1.2	1.2	1.1	1.1
Asset-based FSIs												
Nonperforming loans to total gross loans	2.1	2.3	2.3	2.3	1.9	1.9	2.0	1.6	1.9	2.0	1.9	1.6
Return on assets 1/	2.7	2.5	2.6	2.4	3.0	3.0	3.0	2.9	5.1	4.8	5.0	4.0
Liquid assets to total assets	16.2	16.0	16.8	17.9	15.2	17.8	17.6	16.2	16.6	16.3	15.5	16.6
Liquid assets to short-term liabilities	21.5	21.4	23.2	24.2	21.5	25.1	24.6	23.1	23.9	23.8	23.3	25.4
Sectoral distribution of loans to total gross loans												
Residents	93.3	93.1	92.6	92.8	90.8	93.3	93.6	94.6	94.9	95.2	95.0	96.0
Deposit-takers	0.5	0.5	0.6	1.1	0.9	0.5	1.1	1.4	1.4	1.5	1.5	1.8
Central bank	-	-	-	-	-	-	-	-	-	-	-	-
Other financial corporations	-	-	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
General government	-	-	-	-	-	-	-	-	-	0.0	0.0	0.0
Nonfinancial corporations	75.4	74.4	73.3	71.9	72.5	74.7	74.3	74.8	74.9	74.8	72.3	72.1
Other domestic sectors	17.4	18.3	18.7	19.6	17.3	17.9	18.1	18.3	18.4	18.8	21.2	22.0
Nonresidents	6.7	6.9	7.4	7.2	9.2	6.7	6.4	5.4	5.1	4.8	5.0	4.0
Income- and expense-based FSIs												
Interest margin to gross income	69.7	67.9	69.3	68.6	71.6	72.9	72.5	72.9	50.5	57.3	60.2	63.1
Noninterest expenses to gross income	49.5	51.3	51.0	52.4	56.6	55.3	55.2	55.1	67.4	63.5	61.5	60.6

Source: National Bank of Cambodia.
1/ Annualized.

Table 8. Cambodia: Key FSAP Recommendations of High Priority

Recommendation	Timeframe 1/	Status
General Stability		
I. Improve the quality of data to enable an appropriate assessment of risks, and to enhance the reliability of stress tests, including through strengthening supervision; and collecting additional credit-related information.	Short-term	In process
II. Ensure that banks retain an appropriate level of liquid assets to be able to meet short-term obligations by enforcing existing regulations.	Short-term	In process
III. Upgrade law to formalize delineation of responsibilities among supervisors, and establish procedures, through MOUs, for practical information exchange, coordination and accountability among domestic supervisors (NBC, MEF, SECC), and with foreign supervisors.	Short-term	In process
IV. Upgrade both the number and capacity of staff in the areas of banking, insurance, securities and payment system supervision; develop training programs for financial institutions on accounting, corporate governance, risk management, and for the external audit profession.	Medium-term	In process
V. Develop and implement a strategic plan to address the conflicts and overlaps in the financial sector legal and regulatory framework.	Medium-term	In process
Supervision and Regulation		
Banking		
VI. Develop supervisory strategy to deal with banks that cannot meet the new capital. requirement.	Short-term	Done
VII. Conduct comprehensive upgrades to the legal framework.	Short-term	In process
VIII. Reprioritize the work performed by the staff to facilitate forward-looking, risk-based supervision.	Short-term	In process
IX. Impose a moratorium on the issuance of new bank licenses as long as supervisory capacity and resources remain inadequate.	Short-term	Under NBC review
Non-Bank Financial Sector		
X. Revise capital regulations in concert with liability, investment and accounting rules to better reflect the risks in a growing insurance market.	Short-term	Done
XI. Enhance powers for intervention, corrective measures, and enforcement.	Short-term	In process
XII. Conduct a readiness study prior to the launch of the stock exchange.	Short-term	Done
Access to Finance		
XIII. Enhance supervisory practices to keep pace with the development of microfinance deposit-taking institutions, and impose a moratorium as long as supervisory capacity and resources remain inadequate.	Medium-term	In process
Crisis Management Framework		
XIV. Revise PCA framework by developing additional triggers for asset quality, liquidity, and earlier intervention based on the solvency ratio.	Medium-term	In process
XV. Introduce regulation allowing banks to use their fixed deposits at the NBC and any issue of government (including government bodies) or government-guaranteed securities as eligible collateral for interbank and NBC repos.	Short term	Done
XVI. Develop a crisis management framework.	Medium-term	In preparation
Transparency of Monetary and Financial Policies		
XVII. Introduce due process for the dismissal of NBC Board members and the Governor by specifying the legal grounds for doing so, and defining an appeal process.	Medium-term	In preparation
XVIII. Amend the law to reduce the government's representation on the Board of the NBC; and to reflect the practice of appointing two Deputy Governors.	Short-term	In preparation
Corporate governance of banks		
XIX. Draft and/or implement banking regulations on internal audit and controls, risk management, and compliance functions at banks.	Short-term	Done
AML/CFT 2/		
XX. Introduce new rules measures for conducting overall AML/CFT risk assessments and risk profiling of financial institutions.	Short-term	In process

Source: IMF staff.
1/ Short term: up to one year; medium term: one to three years.
2/ Since the 2010 FSAP, Cambodia has made progress in addressing deficiencies in its legal and regulatory framework. In July 2014 Cambodia exited the APG's (Asia/Pacific Group on Money Laundering) enhanced follow-up process and was placed on regular follow-up (also removed from the FATF's On-Going Global AML/CFT Compliance Process in February 2015). The authorities are encouraged to continue to address the full range of issues identified in its mutual evaluation report and to effectively implement the AML/CFT framework.

Table 9. Cambodia: Millennium Development Goals (MDG) Indicators, 1990–2015

	1990	1995	2000	2005	2009	2010	2011	2012	2013	2014	2015 MDG Target
Goal 1: Eradicate extreme poverty and hunger											
Percentage share of income or consumption held by poorest 20 percent	…	8.5	…	…	8	…	…	…	…	…	11
Population below minimum level of dietary energy consumption (percent)	…	…	…	33	…	…	…	…			21
Poverty headcount ratio at $1.25 per day (PPP, percent of population)	…	49	…	40	13	11	10	…	…	…	20
Poverty headcount ratio at national poverty line (percent of population)	…	…	…	50	24	22	21	18	…	…	
Prevalence of underweight in children (under five years of age)	…	43	40	28	…	29	…	…	…	…	26
Goal 2: Achieve universal primary education											
Net primary enrollment (percent of relevant age group)	67	…	87	90	…	98	98	98	…	…	100
Primary completion rate, total (percent of relevant age group)	…	42	47	85	88	91	93	98	…	…	100
Proportion of pupils starting grade 1 who reach grade 5	…	…	63	55	…	85	66	…	…	…	100
Youth literacy rate (percent of ages 15–24)	73	76	79	83	87	…	…	…	…	…	100
Goal 3: Promote gender equality and empower women											
Proportion of seats held by women in national parliament (percent)	…	…	8	10	21	21	20	20	20	20	30
Ratio of girls to boys in primary and secondary education (percent)	73	..	82	..	…	…	…	…	…	…	100
Ratio of young literate females to males (percent ages 15–24)	81	84	89	90	97	…	…	…	…	…	100
Share of women employed in the nonagricultural sector (percent)	..	..	41	..	…	…	…	…	…	…	…
Goal 4: Reduce child mortality											
Immunization, measles (percent of children ages 12–23 months)	34	62	65	79	92	93	93	93	90	…	90
Infant mortality rate (per 1,000 live births)	87	87	80	73	39	37	36	34	33	…	50
Under five mortality rate (per 1,000)	119	119	107	96	46	44	42	40	38	…	38
Goal 5: Improve maternal health											
Births attended by skilled health staff (percent of total)	..	..	32	44	…	71	…	74	…	…	80
Maternal mortality ratio (modeled estimate, per 100,000 live births)	…	…	450	540	…	206	…	…	170	…	250
Goal 6: Combat HIV/AIDS, malaria, and other diseases											
Incidence of tuberculosis (per 100,000 people)	585	557	530	505	451	437	424	411	400	…	…
Prevalence of HIV, total (percent of population 15–49)	…	…	…	2	1	1	1	1	1	…	..
Goal 7: Ensure environmental sustainability											
Access to an improved water source (percent of population)	0	19	38	…	64	66	69	71	…	…	…
Access to improved sanitation (percent of population)	0	8	16	…	32	33	35	37	…	…	…
Nationally protected areas (percent of total land area)	…	…	…	24	26	26	…	26	…	…	…
Goal 8: Develop a global partnership for development											
Aid per capita (current U.S. dollars)	4	50	31	39	51	51	54	54	…	…	…
Fixed line and mobile phone subscribers (per 100 people)	0	0	1	8	45	59	98	132	137	…	…
Internet users (per 1,000 people)	0	…	0	3	1	1	3	5	6	…	…
Personal computers (per 1,000 people)	…	0	1	3	…	…	…	…	…	…	…
Total debt service (percent of exports of goods and services)	..	1	1	1	1	1	1	1	2	…	…
Goal 9: De-mining, UXO and assistance											
Annual numbers of civilian casualties recorded	…	1,691	…	797	244	286	240	240	…	…	0
Percentage of suspected contaminated areas cleared	…	10	…	50	53	59	56	56	…	…	100
Other											
Fertility rate, total (births per woman)	6	5	4	3	3	3	3	3	…	…	…
GNI per capita, Atlas method (current U.S. dollars)	..	280	280	450	690	740	810	880	950	…	…
GNI, Atlas method (current, in billions of U.S. dollars)	…	3.2	3.6	6.2	10	11	12	13	14	…	…
Gross capital formation (percent of GDP)	8	15	18	18	21	17	17	…	19	…	…
Life expectancy at birth, total (years)	50	…	…	58	70	71	71	71	…	…	…
Literacy rate, adult total (percent of people ages 15 and above)	62	64	68	…	74	…	…	…	…	…	…
Population, total (millions)	10	11	13	14	14	14	15	15	15	…	…
Trade (percent of GDP)	19	78	112	137	105	114	114	…	140	…	…

Sources: World Bank database, *World Development Indicators,* and *Poverty Assessment* (2009); UN Human Development Indicators Report (2003); Cambodia MDG 2011 update; UN MDG Indicators 2011 (http://mdgs.un.org); and IMF staff estimates.

Appendix I. Cambodia—Risk Assessment Matrix

	Event	Risk Horizon	Up/Down -side	Prob.	Impact	Transmission	Policy Recommendations
Domestic Risks	Revenue shortfall	Medium-term	↓	**High**	**Medium**	Fiscal position deteriorates - fiscal deficits widen and government deposits deplete sharply.	Steadfast implementation of RMS, while rationalizing non-developmental current expenditure.
	A large correction in real estate prices.	Short-term	↓	**Medium**	**High**	Turning of the credit cycle and fallout from excess household and corporate leverage (incl. in FX) as investors withdraw FX deposits, generating disorderly deleveraging	Increase reserve requirements to slow down credit growth, implement macro prudential measures, strengthen micro-prudential regulation and supervision, ensure adequate emergency liquidity, strengthen supervision and regulation for MFIs. Preemptively strengthen the crisis management framework.
	Recurrent political uncertainty and/or labor market disruptions	Short-term	↓	**Medium**	**High**	Large deposit withdrawal, drag in FDI and export growth and weaker investor confidence.	Ensure continued macroeconomic stability to support confidence in the economy
	Extreme weather	Short-term	↓	**Medium**	**Medium**	Weaker agricultural production and exports, weaker tourism, and wider income inequality.	Expedite structural reforms to accelerate diversification, improve infrastructure, and increase transfers to the rural poor after creating fiscal space.
External Risks	Structurally weak growth in Euro area	Short-term	↓	**High/Medium**	**High**	Weaker garment export growth	Expedite structural reforms to accelerate diversification, by expanding the narrow range of export products, while finding new export markets for existing products.
	Significant China slowdown	Short-term	↓	**Low/Medium**	**Medium/ High**	Lower exports coupled with weaker FDI and banking sector flows.	Expedite structural reforms to accelerate diversification. Ensure adequate emergency liquidity.
	Sharp asset price decline and decompression of global credit spreads	Short-term	↓	**Medium**	**High**	FX deposit outflows, foreign reserves fall.	Build up foreign reserve buffers against external shocks; where appropriate release limited short-term liquidity to troubled banks; expedite work on a crisis management framework; increasing reserve requirements on foreign deposits substantially during episodes of capital inflows would create a buffer that could be liberated when foreign deposits flow out in response to external shocks.
	Surge in the U.S. dollar	Short-term	↓	**Medium**	**Medium**	Weaker exports, tourism receipts, FDI, and bank lending from other partner countries	Maintain macroeconomic stability and develop interbank and foreign exchange markets to enhance monetary policy effectiveness and to reduce dollarization. Expedite structural reforms to boost non-price competitiveness

The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. "Short term" and "medium term" are meant to indicate that the risk could materialize within 1 year and 3 years, respectively.

INTERNATIONAL MONETARY FUND

CAMBODIA

STAFF REPORT FOR THE 2016 ARTICLE IV CONSULTATION—DEBT SUSTAINABILITY ANALYSIS

September 28, 2016

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This Debt Sustainability Analysis (DSA) shows that Cambodia is at low risk of debt distress with all debt burden indicators projected to remain below the respective indicative thresholds. The results also indicate that debt sustainability continues to be vulnerable to growth, exports, and adverse revenue shocks, and the materialization of contingent liabilities. The findings reinforce the need for continued structural reforms to increase the economy's resilience to external shocks, and to mobilize fiscal revenues.

1. **This DSA continues to assess Cambodia at a low risk of debt distress.** The indicative debt distress thresholds remain unchanged from the 2015 Article IV DSA. Under the baseline scenario, the external and the public debt burden indicators never breach the policy-dependent indicative thresholds, and the PV of external debt follows a downward trend in the medium term. Downside risks to the baseline scenario include external arrears, and the materialization of contingent liabilities. The macroeconomic assumptions underlying the baseline scenario remain similar to the 2015 DSA. Cambodia's Country Policy and Institutional Assessment (CPIA) rating remained unchanged at "medium performer."

CAMBODIA'S PUBLIC DEBT

2. **Cambodia's stock of external public debt, including arrears, stood at around US$5.6 billion or 32 percent of GDP (22 percent of GDP in present value terms) as of end-2015.** The debt-to-GDP ratio has been steadily increasing since 2008, when it was 27 percent of GDP. The increase in external debt since then has been driven largely by disbursement of bilateral loans. The corresponding present value (PV) of the external debt was 22.1 percent of GDP at end 2015.

Cambodia: External Public Debt 2015

	U.S. Dollar (U.S. millions)	Share of Total External Debt	In Percent of GDP
Total	5,645	100	32.1
Multilateral	1,656	29.3	9.5
Bilateral	3,989	70.7	22.6

Sources: Cambodia authorities; and World Bank estimates.

3. **Bilateral debt has been increasing over time, and the share of multilateral debt has continued to decline.** China remains the largest bilateral creditor, contributing to around 80 percent of the total bilateral debt stock, including arrears. Cambodia remains in arrears to the Russian Federation and the United States (nearly 16 percent of total debt or 4 percent of GDP), and the status of negotiations of these arrears has remained unchanged since the last DSA. Cambodia is not servicing its debt with these two creditors. The Cambodian authorities have been in contact with the Russian and the U.S. authorities at least on an annual basis, but further efforts are needed to conclude agreements under the Paris Club framework. Since prospects for resolution remain unclear, this DSA continues to assume no debt restructuring, with arrears continuing to build up over the projection period.

4. **Public domestic debt remains negligible.** There is a small amount of bonds (US$3.2 million) issued in the early 2000s and some old claims on the government (the total equal to half percent of GDP, with no interest) that were carried over from the 1990s and remain to be recorded in the monetary survey.

5. The authorities have made considerable progress in monitoring contingent liabilities from PPPs through strengthening the institutional framework, but further efforts are needed to enhance fiscal transparency and capacity. In line with past Fund recommendations, reinforced by contingent liability management technical assistance provided by the Bank, the authorities adopted an annual ceiling on PPP guarantees at 4 percent of GDP. On the institutional side, in June 2016, the Ministry of Economy and Finance (MEF) has adopted a policy on PPPs outlining legal, regulatory and institutional frameworks. In addition, a central PPP unit for risk management is being established in the MEF. To enhance fiscal transparency, the authorities should also list all contingent liabilities in the annual budget law. Even with debt remaining sustainable with a low risk of distress, continued close monitoring and analysis of fiscal risks through further strengthening of capacity is needed to safeguard fiscal space.

MACROECONOMIC FRAMEWORK

6. The macroeconomic framework underlying the baseline scenario remains broadly in line with the previous DSA.

- **Growth and inflation:** Economic activity remains strong driven by robust exports, real estate, and construction. GDP growth is expected at 7.0 percent in 2016 and is projected to slow to around 6.3–7.0 percent until 2021, assuming some product diversification and supportive policies. Inflation (CPI average) remained low in 2015 at 1.2 percent due to low energy and commodity prices, and is expected to rise slightly to 3.2 percent at end-2016. In the medium-term, inflation is expected to average 3 percent.

- **External sector stability:** Higher-than-expected garment exports and tourism arrivals helped narrow the current account deficit, including official transfers, in 2015 to 10.6 percent of GDP. Continued strong export growth and low commodity prices are expected to narrow the non-interest current account deficit to around 10.2 percent of GDP in 2016. The completion of large power projects should help lower import growth, while improved competitiveness and diversification spurred by the participation in the ASEAN Economic Community (AEC) should help lower the current account deficit over the medium-term to around 8½ percent of GDP, which is expected to remain fully financed by FDI and official loans. Gross official reserves are projected to rise to around 5.7 months of prospective imports through to 2021. External bilateral debt disbursement is projected to average about US$700 million annually during 2015–21 (about 4 percent of GDP on average), resulting in a debt to GDP ratio of just over 35 percent by 2021, after which the debt ratio is projected to decline.

- **Fiscal sustainability:** Revenue performance, supported by the implementation of the Revenue Mobilization Strategy (RMS), saw tax revenues rise by 0.5 percent of GDP to 14.6 percent of GDP in 2015 from 13.7 in 2014. However, the expenditure mix worsened in 2015 as pressure to raise public wages led to a 0.9 percent of GDP increase in the wage bill, while capital spending was compressed by 0.7 percent of GDP. As a result, the 2015 fiscal deficit widened slightly from 1.3 percent of GDP in 2014 to 1.6 percent of GDP in 2015 (but remained well below the budget target). The level of government deposits (as a share of GDP) rose to 9.1 percent of GDP by end-2015. The fiscal deficit is projected to widen to 2.6 percent of GDP (but remain below the budget target) in 2016 as rising current expenditure (the wage bill by 0.2 percent of GDP and non-wage current expenditures by 1 percent of GDP) more than offsets gains from revenue mobilization. Government deposits are projected to stay at around 9.3 percent of GDP in 2016, which are assessed to be adequate. Over the medium-term, fiscal pressures are expected to emerge due to wage pressures even though strong revenue performance is projected to continue as the tax administration measures contained in the RMS generate revenue gains. Medium-term fiscal policy should be anchored to safeguarding government deposits and long-term fiscal debt sustainability, while striking a balance between providing resources for Cambodia's vast development needs and rising wage and social spending pressures.

- **Domestic debt:** As Cambodia's financial sector continues to develop, it is expected that the government will start issuing domestic government bonds to provide additional fiscal financing. By issuing debt starting from ¼ ppt of GDP annually in 2021 and gradually increasing to about ½ ppt of GDP in 2035, the total stock of domestic debt would reach about 3.7 percent of GDP by 2035. This remains low compared to the average domestic debt in low-income countries (LICs) of about 15 percent of GDP. However, this conservative estimate is in line with the authorities' intention of not issuing domestic debt over the medium term and to focus more on mobilizing domestic revenue and raising government deposits (i.e., saving, not borrowing).

EXTERNAL AND PUBLIC DEBT SUSTAINABILITY

7. Under the baseline scenario, the external DSA shows that Cambodia's risk of debt distress is low (Figure 1, Tables 1a and 1b). The PV of debt-to-GDP, debt-to-exports, and debt-to-revenue ratios never breach their respective policy-dependent indicative thresholds and are projected to decline over the projection period. Moreover, the debt service-to-exports and debt service-to-revenue ratios remain well below the thresholds throughout the projection period, partly due to the concessional nature of the debt.

8. Standard stress tests do not indicate any major vulnerability, but highlight that large exchange rate or export shocks could potentially have a major impact on external debt dynamics. A decline in export growth remains an important risk to debt sustainability. As shown in Figure 1, this shock would bring the PV of debt-to-GDP to 39 percent in 2018 (just below the indicative threshold of 40 percent), declining to 18 percent in the long-term. Similarly, a large one-off depreciation would bring the PV of debt-to-GDP to about 35 percent in 2018, and subsequently declining to 21 percent in the long-term. While this highlights the importance of continuous monitoring of debt dynamics, the PV of external debt declines over the projection period and does not currently indicate any major vulnerability.

9. **Public debt is vulnerable to a large exchange rate depreciation shock and to weak revenue growth.** Under a one-off real depreciation shock, the PV of public debt-to-GDP would reach 33 percent in 2018, and then decline over time. If the primary balance remains unchanged at the 2015 level, the PV of public debt-to-GDP would increase to about 27 percent by 2020, with debt projected to continue modestly rising over the long-term. This implies that efforts to mobilize revenues to guarantee long-term debt sustainability should continue. Public debt is projected to decline over the medium-term in the baseline and extreme shock scenario, and do not present any major vulnerability at present.

10. **Public debt sustainability is at risk from a rise in contingent liabilities related to PPPs and potential financial stress.**[1] PPP investments in power generation and distribution projects are large, and in case of adverse scenarios, associated fiscal risks could arise and potentially add substantial liabilities to the debt stock. Other potential contingent liabilities include the fiscal costs to support the financial sector during a banking crisis.

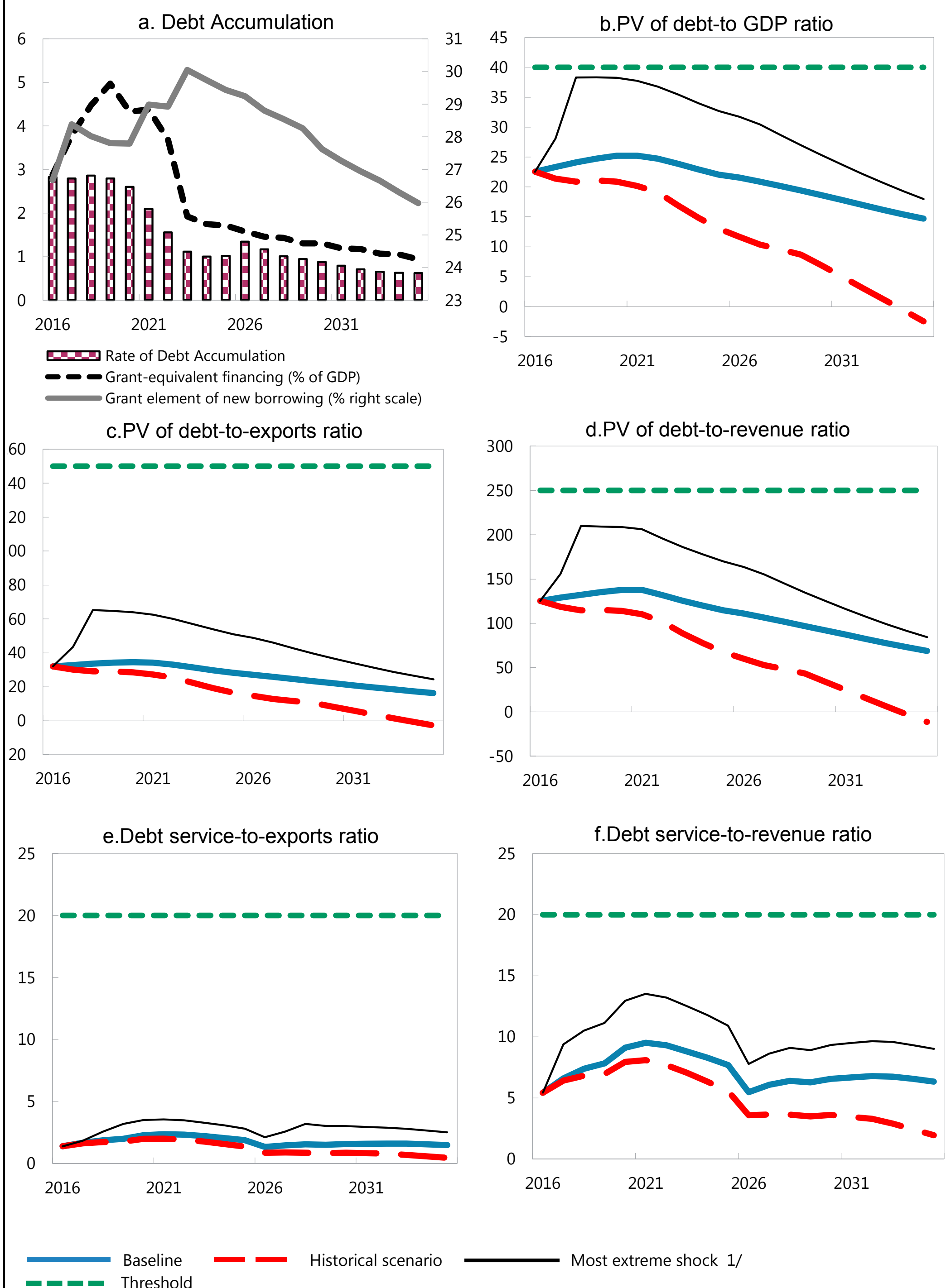
11. **The authorities broadly agree with the findings from the DSA exercise.** The debt management unit at the Ministry of Economy and Finance (MEF) conducts its own internal DSA analysis, and has reached the same conclusion of low risk of debt distress. They use the results of these analyses to propose annual ceilings of new net debt disbursements. The authorities assume a similar loan disbursement profile and current account deficits, but are slightly more optimistic than staff on the medium-term real GDP growth assumption. The MEF expressed concern about the accumulation of contingent liabilities from PPPs and have imposed annual ceilings on PPP guarantees.

CONCLUSION

12. **Cambodia remains at low risk of debt distress.** The baseline projections and the standard stress tests show limited risk to external debt given that none of the indicators breach their thresholds. Downside risks to the baseline scenario include the materialization of contingent liabilities and issues arising from external arrears. The most extreme stress tests indicate that Cambodia's debt sustainability remains vulnerable to shocks in the exchange rate, economic growth, exports, and the fiscal position. This reinforces the importance of preserving macroeconomic stability and diversifying the economy and exports to increase resilience to external shocks, and the successful implementation of the revenue mobilization strategy.

[1] The authorities have requested IMF technical assistance on PPPs using the Fiscal Risk Assessment Model (P-FRAM), which will (i) evaluate the PPP management framework; (ii) provide capacity building in assessing fiscal risks and contingent liabilities arising from PPPs; and (iii) identify mitigating measures among other priorities currently under discussion. There is also an on-going technical assistance by development partners, with the ADB supporting Cambodia in establishing a legal and institutional framework for development of PPPs and the World Bank providing technical assistance to determine the size of contingent liabilities related to PPPs.

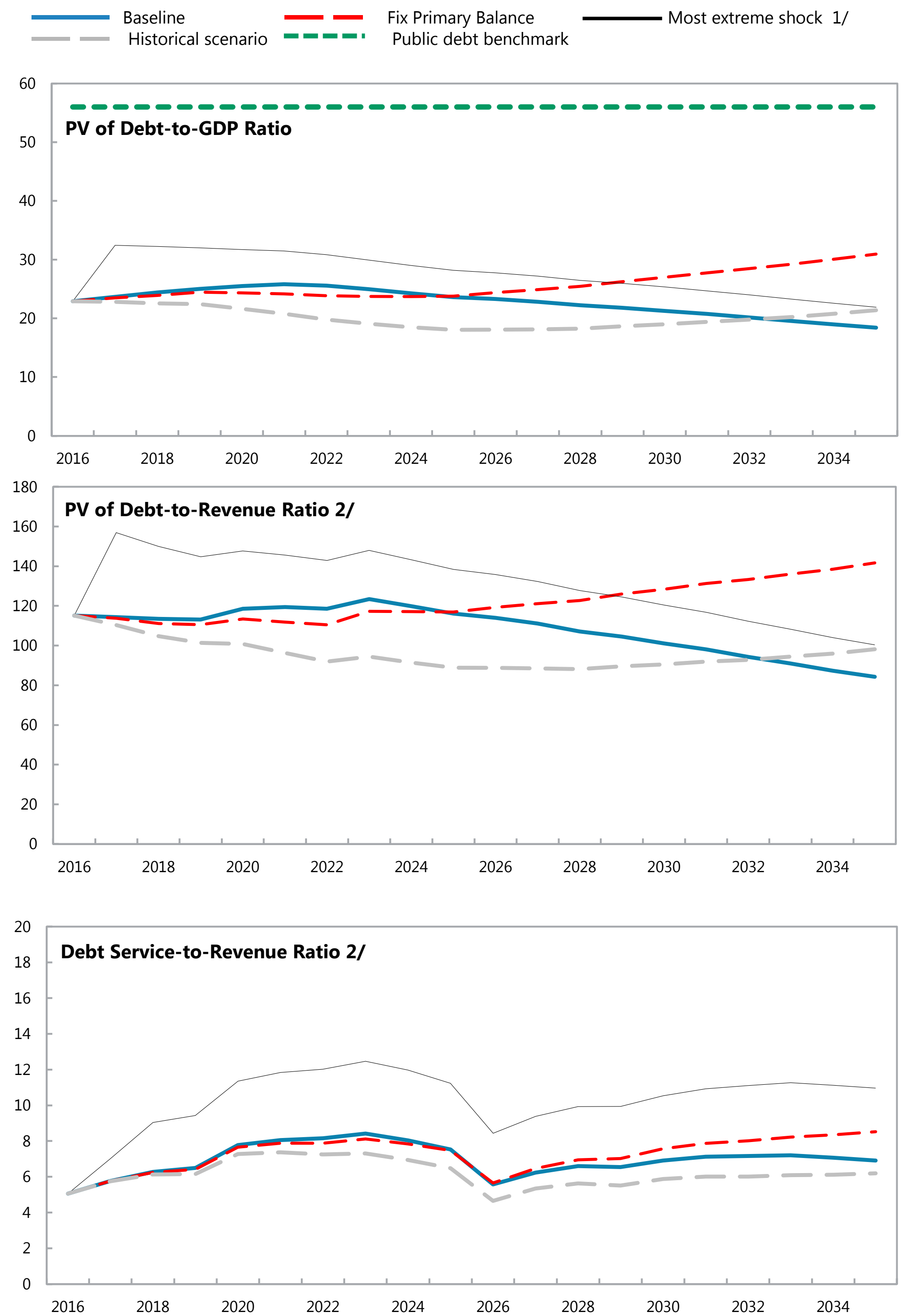
Figure 1. Cambodia: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2016-2035 1/



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

1/ The most extreme stress test is the test that yields the highest ratio on or before 2026. In figure b. it corresponds to a Exports shock; in c. to a Exports shock; in d. to a Exports shock; in e. to a Exports shock and in figure f. to a One-time depreciation shock.

Figure 2. EY36Cambodia: Indicators of Public Debt Under Alternative Scenarios, 2016-2035 1/



Sources: Cambodia authorities; and IMF staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio on or before 2026.
2/ Revenues are defined inclusive of grants.

Table 1a .Cambodia: External Debt Sustainability Framework, Baseline Scenario, 2013-2035 1/

(In percent of GDP, unless otherwise indicated)

	Actual			Historical 6/ Average	Standard 6/ Deviation	Projections									
	2013	2014	2015			2016	2017	2018	2019	2020	2021	2016-2021 Average	2026	2035	2022-2035 Average
External debt (nominal) 1/	**31.6**	**31.8**	**32.1**			**32.1**	**32.3**	**32.7**	**33.4**	**33.9**	**34.0**		**26.8**	**17.6**	
Of which: public and publicly guaranteed (PPG)	31.6	31.8	32.1			32.1	32.3	32.7	33.4	33.9	34.0		26.8	17.6	
Change in external debt	0.0	0.3	0.3			-0.1	0.2	0.4	0.7	0.6	0.0		-1.1	-0.8	
Identified net debt-creating flows	-2.1	-0.8	-0.4			-1.0	-1.8	-2.2	-2.8	-2.4	-2.2		-1.5	0.0	
Non-interest current account deficit	**12.0**	**11.8**	**10.3**	**7.6**	**4.1**	**10.4**	**9.5**	**8.9**	**7.7**	**7.9**	**8.0**		**9.0**	**10.5**	9.4
Deficit in balance of goods and services	9.7	10.6	9.8			9.0	9.7	10.4	10.9	10.9	10.7		8.6	8.4	
Exports	65.8	67.0	70.0			70.3	71.1	71.8	72.3	73.1	73.9		79.5	90.2	
Imports	75.5	77.6	79.7			79.3	80.8	82.2	83.3	84.0	84.6		88.1	98.7	
Net current transfers (negative = inflow)	-2.5	-3.5	-4.8	-6.4	3.1	-4.6	-5.4	-6.1	-6.7	-6.2	-5.7		-3.7	-2.3	-3.2
Of which: official	-1.9	-1.8	-1.7			-1.8	-2.6	-3.2	-3.7	-3.1	-2.6		-0.6	-0.3	
Other current account flows (negative = net inflow)	4.8	4.7	5.3			5.9	5.2	4.6	3.5	3.2	3.0		4.1	4.3	
Net FDI (negative = inflow)	**-12.0**	**-10.0**	**-9.2**	**-9.1**	**2.5**	**-9.1**	**-9.1**	**-9.1**	**-8.9**	**-8.9**	**-8.9**		**-9.1**	**-9.1**	-9.1
Endogenous debt dynamics 2/	**-2.1**	**-2.5**	**-1.4**			**-2.3**	**-2.1**	**-2.0**	**-1.6**	**-1.4**	**-1.4**		**-1.4**	**-1.3**	
Contribution from nominal interest rate	0.3	0.4	0.4			-0.2	-0.1	0.0	0.5	0.6	0.6		0.2	0.4	
Contribution from real GDP growth	-2.2	-2.0	-2.1			-2.1	-2.1	-2.0	-2.0	-2.0	-2.0		-1.7	-1.1	
Contribution from price and exchange rate changes	-0.3	-0.9	0.3			...	...	...	...	...	...		...	...	
Residual (3-4) 3/	**2.1**	**1.0**	**0.7**			**1.0**	**2.0**	**2.6**	**3.4**	**2.9**	**2.2**		**0.4**	**-1.4**	
Of which: Exceptional financing	-0.1	-0.1	-0.1			-0.1	-0.1	-0.1	-0.1	0.0	0.0		0.0	0.0	
PV of external debt 4/	...	...	21.7			22.5	23.3	24.1	24.8	25.2	25.2	24.2	21.6	14.7	
In percent of exports	...	...	31.0			32.1	32.8	33.6	34.2	34.5	34.2	33.6	27.1	16.3	
PV of PPG external debt	**...**	**...**	**21.7**			**22.5**	**23.3**	**24.1**	**24.8**	**25.2**	**25.2**	24.2	**21.6**	**14.7**	
In percent of exports	**...**	**...**	**31.0**			**32.1**	**32.8**	**33.6**	**34.2**	**34.5**	**34.2**	33.6	**27.1**	**16.3**	
In percent of government revenues	**...**	**...**	**126.9**			**125.3**	**129.3**	**132.3**	**135.2**	**137.7**	**137.8**	132.9	**111.0**	**68.9**	
Debt service-to-exports ratio (in percent)	**1.1**	**1.3**	**1.4**			**1.4**	**1.7**	**1.9**	**2.0**	**2.3**	**2.4**	1.9	**1.3**	**1.5**	
PPG debt service-to-exports ratio (in percent)	**1.1**	**1.3**	**1.4**			**1.4**	**1.7**	**1.9**	**2.0**	**2.3**	**2.4**	1.9	**1.3**	**1.5**	
PPG debt service-to-revenue ratio (in percent)	**4.9**	**5.0**	**5.7**			**5.4**	**6.6**	**7.4**	**7.8**	**9.1**	**9.5**	7.6	**5.5**	**6.3**	
Total gross financing need (Billions of U.S. dollars)	0.1	0.4	0.4			0.4	0.3	0.3	0.1	0.2	0.3		0.4	2.6	
Non-interest current account deficit that stabilizes debt ratio	12.0	11.5	10.0			10.4	9.3	8.5	7.1	7.3	8.0		10.1	11.3	
Key macroeconomic assumptions															
Real GDP growth (in percent)	7.4	7.1	7.0	7.0	2.9	7.0	6.9	6.8	6.8	6.5	6.3	6.7	6.4	6.8	6.6
GDP deflator in U.S. dollar terms (change in percent)	0.9	2.8	-0.9	3.8	4.0	1.8	1.1	1.7	1.9	1.9	1.9	1.7	2.1	2.2	2.1
Effective interest rate (percent) 5/	1.1	1.2	1.2	1.0	0.2	-0.6	-0.3	0.1	1.6	1.9	1.9	0.8	0.8	2.2	1.4
Growth of exports of G&S (U.S. dollar terms, in percent)	13.6	12.2	10.7	12.7	13.6	9.3	9.4	9.6	9.6	9.7	9.4	9.5	10.3	10.7	10.4
Growth of imports of G&S (U.S. dollar terms, in percent)	13.5	13.2	9.0	12.6	11.1	8.2	10.2	10.5	10.2	9.5	9.0	9.6	10.1	10.6	10.0
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	26.7	28.4	28.0	27.8	27.8	29.0	27.9	29.2	26.0	28.0
Government revenues (excluding grants, in percent of GDP)	15.1	17.1	17.1			18.0	18.0	18.2	18.3	18.3	18.3		19.4	21.3	20.1
Aid flows (in Billions of US dollars) 7/	1.0	1.0	0.8			0.5	0.8	1.0	1.2	1.1	1.2		0.7	0.7	
Of which: Grants	0.6	0.5	0.3			0.4	0.6	0.7	0.9	0.8	1.0		0.4	0.5	
Of which: Concessional loans	0.4	0.5	0.5			0.2	0.2	0.2	0.2	0.3	0.3		0.2	0.2	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			2.9	3.8	4.5	5.0	4.3	4.4		1.6	0.9	1.5
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			51.4	56.6	59.3	62.1	58.6	62.3		53.5	42.8	50.3
Memorandum items:															
Nominal GDP (Billions of US dollars)	15.2	16.8	17.8			19.4	20.9	22.7	24.7	26.8	29.1		43.7	94.4	
Nominal dollar GDP growth	8.4	10.1	6.0			8.9	8.1	8.6	8.7	8.5	8.3	8.5	8.6	9.2	8.8
PV of PPG external debt (in Billions of US dollars)			3.8			4.3	4.9	5.5	6.1	6.7	7.3		9.4	13.8	
(PVt-PVt-1)/GDPt-1 (in percent)						2.8	2.8	2.9	2.8	2.6	2.1	2.7	1.3	0.6	0.9
Gross workers' remittances (Billions of US dollars)	0.1	0.3	0.5			0.5	0.6	0.7	0.7	0.8	0.9		1.4	1.9	
PV of PPG external debt (in percent of GDP + remittances)	...	...	21.0			21.9	22.7	23.4	24.0	24.5	24.5		20.9	14.4	
PV of PPG external debt (in percent of exports + remittances)	...	...	29.7			30.8	31.6	32.3	32.9	33.1	32.8		26.1	15.9	
Debt service of PPG external debt (in percent of exports + remittances)	...	...	1.3			1.3	1.6	1.8	1.9	2.2	2.3		1.3	1.5	

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

1/ Includes both public and private sector external debt.

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

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

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

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

6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

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

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

Table 1b. Cambodia: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2016-2035

(In percent)

	Projections							
	2016	2017	2018	2019	2020	2021	**2026**	2035
PV of debt-to GDP ratio								
Baseline	23	23	24	25	25	25	**22**	15
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2016-2036 1/	23	21	21	21	21	20	**12**	-2.4
A2. New public sector loans on less favorable terms in 2016-2036 2/	23	24	26	28	29	30	**28**	22
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2017-2018	23	24	25	26	26	26	**23**	15
B2. Export value growth at historical average minus one standard deviation in 2017-2018 3/	23	28	38	38	38	38	**32**	18
B3. US dollar GDP deflator at historical average minus one standard deviation in 2017-2018	23	23	25	25	26	26	**22**	15
B4. Net non-debt creating flows at historical average minus one standard deviation in 2017-2018 4/	23	26	31	31	32	31	**26**	16
B5. Combination of B1-B4 using one-half standard deviation shocks	23	26	33	33	33	33	**28**	17
B6. One-time 30 percent nominal depreciation relative to the baseline in 2017 5/	23	33	34	35	36	36	**30**	21
PV of debt-to-exports ratio								
Baseline	32	33	34	34	34	34	**27**	16
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2016-2036 1/	32	30	29	29	29	27	**15**	-3
A2. New public sector loans on less favorable terms in 2016-2036 2/	32	34	36	38	40	40	**35**	25
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2017-2018	32	33	33	34	34	34	**27**	16
B2. Export value growth at historical average minus one standard deviation in 2017-2018 3/	32	44	65	65	64	62	**49**	24
B3. US dollar GDP deflator at historical average minus one standard deviation in 2017-2018	32	33	33	34	34	34	**27**	16
B4. Net non-debt creating flows at historical average minus one standard deviation in 2017-2018 4/	32	37	43	43	43	42	**33**	18
B5. Combination of B1-B4 using one-half standard deviation shocks	32	38	48	48	48	47	**37**	20
B6. One-time 30 percent nominal depreciation relative to the baseline in 2017 5/	32	33	33	34	34	34	**27**	16
PV of debt-to-revenue ratio								
Baseline	125	129	132	135	138	138	**111**	69
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2016-2036 1/	125	119	115	115	114	110	**60**	-11
A2. New public sector loans on less favorable terms in 2016-2036 2/	125	134	142	150	158	162	**144**	105
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2017-2018	125	132	139	142	144	144	**116**	72
B2. Export value growth at historical average minus one standard deviation in 2017-2018 3/	125	156	210	209	209	206	**163**	84
B3. US dollar GDP deflator at historical average minus one standard deviation in 2017-2018	125	130	136	139	141	141	**114**	71
B4. Net non-debt creating flows at historical average minus one standard deviation in 2017-2018 4/	125	147	170	171	172	171	**136**	76
B5. Combination of B1-B4 using one-half standard deviation shocks	125	146	180	181	181	180	**143**	79
B6. One-time 30 percent nominal depreciation relative to the baseline in 2017 5/	125	183	187	191	195	195	**157**	97

Table 1c. Cambodia: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2016-2035 (continued)

(In percent)

Debt service-to-exports ratio								
Baseline	1	2	2	2	2	2	**1**	1
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2016-2036 1/	1	2	2	2	2	2	**1**	0
A2. New public sector loans on less favorable terms in 2016-2036 2/	1	2	2	2	2	3	**2**	2
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2017-2018	1	2	2	2	2	2	**1**	1
B2. Export value growth at historical average minus one standard deviation in 2017-2018 3/	1	2	3	3	4	4	**2**	3
B3. US dollar GDP deflator at historical average minus one standard deviation in 2017-2018	1	2	2	2	2	2	**1**	1
B4. Net non-debt creating flows at historical average minus one standard deviation in 2017-2018 4/	1	2	2	2	3	3	**2**	2
B5. Combination of B1-B4 using one-half standard deviation shocks	1	2	2	3	3	3	**2**	2
B6. One-time 30 percent nominal depreciation relative to the baseline in 2017 5/	1	2	2	2	2	2	**1**	1
Debt service-to-revenue ratio								
Baseline	5	7	7	8	9	10	**5**	6
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2016-2036 1/	5	6	7	7	8	8	**4**	2
A2. New public sector loans on less favorable terms in 2016-2036 2/	5	7	7	8	10	10	**8**	8
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2017-2018	5	7	8	8	10	10	**6**	7
B2. Export value growth at historical average minus one standard deviation in 2017-2018 3/	5	7	8	10	11	12	**7**	9
B3. US dollar GDP deflator at historical average minus one standard deviation in 2017-2018	5	7	8	8	9	10	**6**	7
B4. Net non-debt creating flows at historical average minus one standard deviation in 2017-2018 4/	5	7	8	9	10	11	**6**	7
B5. Combination of B1-B4 using one-half standard deviation shocks	5	7	8	9	11	11	**6**	8
B6. One-time 30 percent nominal depreciation relative to the baseline in 2017 5/	5	9	11	11	13	14	**8**	9
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	26	26	26	26	26	26	**26**	26

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

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.
3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).
4/ Includes official and private transfers and FDI.
5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.
6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Table 2a. Cambodia: Public Sector Debt Sustainability Framework, Baseline Scenario, 2013-2035

(In percent of GDP, unless otherwise indicated)

	Actual			Average 5/	Standard Deviation 5/	Estimate	Projections						
	2013	2014	2015			2016	2017	2018	2019	2020	2021	2016-21 Average	2035
Public sector debt 1/	32.1	32.3	32.5			32.4	32.7	33.0	33.6	34.2	34.5		21.9
of which: foreign-currency denominated	31.6	31.8	32.1			32.1	32.3	32.7	33.4	33.9	34.0		18.4
Change in public sector debt	0.0	0.2	0.3			-0.1	0.2	0.3	0.6	0.5	0.3		-0.7
Identified debt-creating flows	0.0	-1.3	-0.8			-0.2	0.1	0.5	0.6	1.4	1.4		-1.4
Primary deficit	2.2	0.8	0.6	1.7	1.7	2.6	2.8	3.1	2.8	3.4	3.4	3.0	0.1
Revenue and grants	19.0	20.1	19.0			19.9	20.7	21.5	22.1	21.5	21.6		21.7
of which: grants	3.9	3.0	1.9			1.9	2.6	3.3	3.8	3.1	3.3		0.6
Primary (noninterest) expenditure	21.2	20.9	19.6			22.5	23.5	24.6	24.9	24.9	25.0		21.8
Automatic debt dynamics	-2.1	-2.1	-1.4			-2.9	-2.7	-2.6	-2.2	-2.1	-2.0		-1.4
Contribution from interest rate/growth differential	-2.8	-2.7	-2.5			-2.8	-2.8	-2.6	-2.2	-2.1	-2.0		-1.4
of which: contribution from average real interest rate	-0.6	-0.6	-0.4			-0.7	-0.7	-0.5	-0.1	0.0	0.0		0.1
of which: contribution from real GDP growth	-2.2	-2.1	-2.1			-2.1	-2.1	-2.1	-2.1	-2.1	-2.0		-1.4
Contribution from real exchange rate depreciation	0.7	0.6	1.1			-0.1	0.1	0.0	0.0	0.0	0.0		...
Other identified debt-creating flows	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0
Debt relief (HIPC and other)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0
Residual, including asset changes	0.0	1.5	1.1			0.1	0.1	-0.2	0.0	-0.8	-1.0		0.6
Other Sustainability Indicators													
PV of public sector debt	...	...	22.1			22.9	23.6	24.4	25.0	25.5	25.8		18.4
of which: foreign-currency denominated	...	...	21.7			22.5	23.3	24.1	24.8	25.2	25.2		14.7
of which: external	...	...	21.7			22.5	23.3	24.1	24.8	25.2	25.2		14.7
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...
Gross financing need 2/	3.3	2.1	1.9			4.0	4.3	4.8	4.5	5.3	5.3		1.5
PV of public sector debt-to-revenue and grants ratio (in percent)	...	...	116.1			115.2	114.4	113.5	113.1	118.6	119.4		84.8
PV of public sector debt-to-revenue ratio (in percent)	...	...	129.2			127.3	131.1	133.9	136.6	139.0	140.9		87.2
of which: external 3/	...	...	126.9			125.3	129.3	132.3	135.2	137.7	137.8		69.7
Debt service-to-revenue and grants ratio (in percent) 4/	3.9	4.2	5.1			5.1	5.8	6.3	6.5	7.8	8.1		6.9
Debt service-to-revenue ratio (in percent) 4/	4.9	5.0	5.7			5.6	6.6	7.4	7.8	9.1	9.5		7.1
Primary deficit that stabilizes the debt-to-GDP ratio	2.2	0.6	0.3			2.7	2.6	2.8	2.1	2.9	3.0		0.8
Key macroeconomic and fiscal assumptions													
Real GDP growth (in percent)	7.4	7.1	7.0	7.0	2.9	7.0	6.9	6.8	6.8	6.5	6.3	6.7	6.8
Average nominal interest rate on forex debt (in percent)	1.1	1.2	1.2	1.0	0.2	-0.6	-0.3	0.1	1.6	1.9	1.9	0.8	2.2
Average real interest rate on domestic debt (in percent)	-0.6	-2.7	-1.0	-3.4	3.0	-3.9	-2.7	-2.7	-2.7	-2.7	-2.8	-2.9	1.5
Real exchange rate depreciation (in percent, + indicates depreciation)	2.4	2.1	3.9	-1.3	4.0	-0.2	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	0.8	3.1	1.3	3.9	3.4	4.4	3.1	3.0	3.1	3.1	3.1	3.3	3.4
Growth of real primary spending (deflated by GDP deflator, in percent)	7.4	5.7	0.2	1.4	2.7	22.9	11.6	12.0	7.9	6.6	6.7	11.3	6.9
Grant element of new external borrowing (in percent)	...	...	...	...	...	26.7	28.4	28.0	27.8	27.8	29.0	27.9	26.0

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

1/ Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also whether net or gross debt is used.

2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

3/ Revenues excluding grants.

4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 2b. Cambodia: Sensitivity Analysis for Key Indicators of Public Debt 2016-2035

							Projections									
	2016	2017	2018	2019	2020	2021	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035
PV of Debt-to-GDP Ratio																
Baseline	23	24	24	25	25	26	23	23	22	22	21	21	20	20	19	18
A. Alternative scenarios																
A1. Real GDP growth and primary balance are at historical averages	23	23	23	22	22	21	18	18	18	19	19	19	20	20	21	21
A2. Primary balance is unchanged from 2016	23	24	24	24	24	24	24	25	25	26	27	28	28	29	30	31
A3. Permanently lower GDP growth 1/	23	24	25	26	27	28	29	29	30	30	31	31	32	33	33	34
B. Bound tests																
B1. Real GDP growth is at historical average minus one standard deviations in 2017-2018	23	25	27	28	29	30	30	30	30	30	30	30	30	30	29	29
B2. Primary balance is at historical average minus one standard deviations in 2017-2018	23	24	25	26	26	26	24	23	23	22	22	21	20	20	19	19
B3. Combination of B1-B2 using one half standard deviation shocks	23	24	24	25	26	27	26	26	25	25	25	24	24	24	23	23
B4. One-time 30 percent real depreciation in 2017	23	32	32	32	32	31	28	27	26	26	25	25	24	23	23	22
B5. 10 percent of GDP increase in other debt-creating flows in 2017	23	31	31	32	32	32	28	28	27	26	25	24	24	23	22	21
PV of Debt-to-Revenue Ratio 2/																
Baseline	115	114	114	113	119	119	114	111	107	105	101	98	94	91	87	84
A. Alternative scenarios																
A1. Real GDP growth and primary balance are at historical averages	115	110	105	101	101	96	89	88	88	90	91	92	93	94	96	98
A2. Primary balance is unchanged from 2016	115	114	111	111	113	112	119	121	123	126	128	131	133	136	139	142
A3. Permanently lower GDP growth 1/	115	115	116	117	125	128	140	142	142	145	146	148	149	152	153	156
B. Bound tests																
B1. Real GDP growth is at historical average minus one standard deviations in 2017-2018	115	119	123	126	135	138	148	148	146	145	143	142	139	137	135	133
B2. Primary balance is at historical average minus one standard deviations in 2017-2018	115	116	116	116	121	122	116	113	109	106	103	100	96	92	89	85
B3. Combination of B1-B2 using one half standard deviation shocks	115	115	113	114	121	123	126	124	121	120	118	116	113	110	107	105
B4. One-time 30 percent real depreciation in 2017	115	157	150	145	148	146	136	132	128	124	120	117	112	108	104	100
B5. 10 percent of GDP increase in other debt-creating flows in 2017	115	149	146	143	148	148	138	134	129	125	120	116	111	106	102	98
Debt Service-to-Revenue Ratio 2/																
Baseline	5	6	6	6	8	8	6	6	7	7	7	7	7	7	7	7
A. Alternative scenarios																
A1. Real GDP growth and primary balance are at historical averages	5	6	6	6	7	7	5	5	6	6	6	6	6	6	6	6
A2. Primary balance is unchanged from 2016	5	6	6	6	8	8	6	6	7	7	8	8	8	8	8	9
A3. Permanently lower GDP growth 1/	5	6	6	7	8	8	6	7	8	8	9	9	9	10	10	10
B. Bound tests																
B1. Real GDP growth is at historical average minus one standard deviations in 2017-2018	5	6	7	7	8	9	7	7	8	8	9	9	9	9	9	9
B2. Primary balance is at historical average minus one standard deviations in 2017-2018	5	6	6	7	8	8	6	6	7	7	7	7	7	7	7	7
B3. Combination of B1-B2 using one half standard deviation shocks	5	6	6	7	8	8	6	7	7	7	7	8	8	8	8	8
B4. One-time 30 percent real depreciation in 2017	5	7	9	9	11	12	8	9	10	10	11	11	11	11	11	11
B5. 10 percent of GDP increase in other debt-creating flows in 2017	5	6	7	8	9	9	6	7	9	8	9	9	9	9	8	8

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

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.

2/ Revenues are defined inclusive of grants.

INTERNATIONAL MONETARY FUND

CAMBODIA

September 28, 2016

STAFF REPORT FOR THE 2016 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By

Asia and Pacific Department
(In consultation with other departments)

CONTENTS

FUND RELATIONS

(As of August 31, 2016)

Membership Status

Joined December 31, 1969; accepted the obligations under Article VIII, Sections 2, 3, and 4 on January 1, 2002.

General Resources Account:	**SDR Million**	**Percent Quota**
Quota	175.00	100.0
Fund holdings of currency (Exchange Rate)	153.13	87.50
Reserve Tranche Position	21.88	12.50

SDR Department:	**SDR Million**	**Percent Allocation**
Net cumulative allocation	83.92	100.00
Holdings	88.34	105.27

Outstanding Purchases and Loans: None

Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
ECF [1/]	Oct. 22, 1999	Feb. 28, 2003	58.50	58.50
ECF [1/]	May 06, 1994	Aug. 31, 1997	84.00	42.00

[1/] Formerly PRGF.

Overdue Obligations and Projected Payments to the Fund [2/]
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2016	2017	2018	2019	2020
Principal					
Charges/Interest		0.00	0.00	0.00	0.00
Total		0.00	0.00	0.00	0.00

[2/] When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Multilateral Debt Relief Initiative

As part of the Multilateral Debt Relief Initiative (MDRI), the IMF Executive Board on January 5, 2006, approved relief on 100 percent of debt incurred by Cambodia to the IMF before January 1, 2005. This resulted in the forgiving of all of Cambodia's outstanding debt to the IMF, a total of SDR 56.8 million (about US$82 million). The authorities intend to spend the resources over a number of years, initially on rural irrigation projects. The National Bank of Cambodia (NBC) transferred the full MDRI proceeds to the Ministry of Economy and Finance effective March 2006.

Safeguards Assessment

A voluntary safeguards assessment of the NBC was completed in January 2010 at the request of the authorities, which updated the previous March 2004 voluntary assessment. The update assessment found that the NBC had taken steps to strengthen aspects of its safeguards framework; however, important recommendations proposed in 2004 were still outstanding, and some new risks had emerged in the area of external audit.

Exchange Rate Arrangement and Payments System

Cambodia's exchange regime is classified as *other-managed arrangement*. The *de jure* regime is a *managed float*. The official exchange rate, which is expressed in riels per U.S. dollar, applies to all official external transactions conducted by the central government and state enterprises, and is used for accounting purposes by the NBC. It is determined by the foreign exchange market, with the official rate adjusted to be within 1 percent of the market rate on a daily basis.

Cambodia accepted the obligations of Article VIII, Sections 2, 3, and 4 on January 1, 2002. Cambodia maintains an exchange system that is free of restrictions on the making of payments and transfers for current international transactions.

Article IV Consultation

Cambodia is on the standard 12-month Article IV consultation cycle. The last Article IV consultation discussions were held in Phnom Penh during June 22–July 3, 2015. The Executive Board considered the staff report (IMF Country Report 15/307) on October 26, 2015.

Financial Sector Assessment Program (FSAP)

The joint IMF-World Bank FSAP mission took place in March 2010 and the assessment was completed in October 2010.

Technical Assistance

Technical assistance is currently focused on bank supervision, monetary operations, tax policy, and administration including customs administration, macro-fiscal and revenue forecasting, financial sector supervision, and macro-financial statistics. Delivery is through a resident advisor at the NBC, peripatetic experts, and short-term visits from headquarters.

Resident Representative

The IMF Resident Representative in Phnom Penh (Ms. Yong Sarah Zhou) was appointed in July 2015. Mr. Faisal Ahmed, former Resident Representative, assumed the post for the Cambodian IMF office from July 2011 to July 2015.

IMF-WORLD BANK COLLABORATION

(July 2016)

The Bank and the IMF teams for Cambodia, led by Mr. Mathew Verghis (Practice Manager GMFDR) and Ms. Jain-Chandra (IMF Mission Chief for Cambodia), maintain a close working relationship and have an active dialogue on a range of macroeconomic and structural issues.

Recent key areas of cooperation and coordination include:

- **Macroeconomic policy advice to the authorities.** The IMF and the World Bank staffs have consulted each other on key macroeconomic policy messages to the authorities to avoid sending conflicting messages. Bank staff share and discuss the bi-annual Country and East-Asia and Pacific Economic Updates. IMF staff share policy notes and analytical background notes related to Article IV consultation missions. The World Bank and IMF staff regularly meet with policymakers from the Ministry of Economy and Finance and the National Bank of Cambodia to timely address emerging issues related to macroeconomic performance and management.

- **Financial sector reform and FSAP.** The World Bank and the IMF teams have worked closely together while undertaking the 2010 FSAP. In line with the FSAP recommendations, technical assistance missions supporting financial sector resilience are now ongoing and close coordination between the IMF and the World Bank continues. The IMF and the World Bank Group (WBG) jointly co-organized the Macro-Prudential and Financial Stability Workshop for all Cambodian financial regulators. The World Bank and the IMF teams currently are working together to support capacity building through knowledge sharing and south-south exchanges on monetary statistics, monetary policy, and financial stability for the Ministry of Economy and Finance and the National Bank of Cambodia.

- **Public financial management and tax and customs administration reform.** Both institutions are working closely together under the Public Financial Management Reform Program (PFMRP) including 2014–18 revenue mobilization strategy as well as tax and customs administration reform. Both teams are members of the Development Partner Committee (DPC) of the PFMRP, a coordination mechanism for all Development Partners' support for the PFMRP under a Sector Wide Approach, and share information on the work done in this area. The Phase 1 launch of the FMIS on July 20, 2015 marks a major milestone toward the full implementation of a comprehensive transaction processing, improved financial control, and an improved and more transparent financial report generation facility. In addition, the IMF and the World Bank are closely communicating in the context of the preparation of a tax policy review (IMF) and an assessment of tax incentives (World Bank, under an ongoing Public Expenditure Review).

- **Trade facilitation and private sector development**. Both institutions are providing technical support to GDCE/MEF on customs and border reform, regulatory reform, and streamlined import and export procedures. The WBG Trade Related-Assistance in Cambodia program (TRAC) has contributed to enhanced information/improvements in the areas of nontariff measures (NTM), phytosanitary standards, improved trade logistics, trade repository, investment incentive policy, and integration into regional production networks. The WBG Trade Facilitation Facility (TFF) supported the GDCE/MEF to develop Cambodia National Single Window (CNSW) blueprint.

- The Trade Development Support Program (TDSP) continues to support the implementation of a trade sector wide approach (Trade SWAp) expansion of ASYCUDA to 58 customs checkpoints across the geography, covering 95 percent of imports and exports transactions; support to MAFF on SPS automation system; and technical assistance to MOC on certification of country origin automation, trade-marks registration system, business registration automation system, and trade training research institution (TTRI). TSDP also supports the private sector development on export training, value chain study, labor and commercial dispute resolution through the arbitration council foundation (ACF) and the national council arbitration of Cambodia (NCAC). Cambodia gained ranking 56 places in the Logistics Performance Indicators (LPI) in 2010–16, and abolished unnecessary certificates of origin (CO) required by the importing countries.

- **Article IV consultations.** IMF Article IV consultations regularly share their macroeconomic data with the World Bank and hold working sessions to try and reconcile macroeconomic data sets. The collaboration is closest on the debt sustainability analysis, a joint product, but extends more broadly into other areas of the consultation as well. World Bank staff are also invited to attend key meetings. The IMF also joined in some of the WB capacity building TA missions on contingent liabilities. Both institutions are considering using the TA mission findings to further strengthen the DSA analysis.

- **Structural reforms.** The IMF staff and the World Bank teams have worked together to share views on a range of other issues, including structural reforms for improving investment climate, economic diversification, customs modernization, and rural development. The World Bank and IMF staff have worked together to encourage the authorities to speed up civil service reforms to improve public sector performance on public service delivery as well as to boost competiveness.

Based on the above partnership, the World Bank and the IMF share a common view about Cambodia's macroeconomic and structural reform priorities. These include:

- **Sustaining growth.** Growth remains robust although there are signs of deceleration. While decelerating, the garment sector together with construction, and services, in particular finance and real estate, continues to propel growth. Overall macroeconomic management remains appropriate but there are emerging challenges to external competitiveness, partly derived from U.S. dollar appreciation and rising wages. Improving the business climate, reducing infrastructure, energy, and skills bottlenecks, promoting private sector development and economic diversification, improving governance and the delivery of public services and supporting rural development continue to be essential to promote self-sustaining and inclusive growth.

- **Managing public finances and debt.** Fiscal policy remains the main instrument for macroeconomic management given high dollarization. Prudent fiscal management is, therefore, critical and needs to be underpinned by continued improvements in revenue collection, prioritized spending, and better monitoring of contingent liabilities, including through the budgetary and public debt management framework and further progress in budgetary transparency.

- **Safeguarding financial system stability and improving the effectiveness of monetary policy.** Implementing the key recommendations of the 2010 FSAP remains critical to safeguarding financial stability. These include implementing a moratorium on new bank licenses, strengthening coordinated supervision, developing the foreign exchange market, improving the supervisory capacity, enhancing efficient and stable payment system, improving quality of financial data, and encouraging a close coordination among financial regulators. Financial stability risks from the buoyant real estate markets need to be managed through strengthened supervision and improved data collection. Developing an interbank market remains a necessary step for a transition to more effective and market-based monetary policy operations.

- **Improving governance.** Both the World Bank and IMF have stressed the critical role of governance in improving the quality of service delivery and fostering private sector development, which is the engine of growth.

- **The teams are committed to continue the close cooperation going forward.** The table below details the specific activities planned by the two country teams over the next 12-month period along with their expected deliveries.

Cambodia: Joint Managerial Action Plan, 2016–17			
Title	**Products**	**Provisional and Actual Timing**	**Expected and Actual Delivery Date**
	A. Mutual Information on Relevant Work Programs		
The World Bank's Work program in the next 12 Months	**Macroeconomic monitoring** • Semi-annual East Asia and Pacific economic updates • Cambodia Economic Update	Ongoing	Once every six months: tentatively in Apr. and Oct.
	Financial sector • FSAP follow-up technical assistance to implement IFRS roadmap for accounting and auditing practices in financial institutions. FSAP follow-up technical assistance to implement crisis management framework • FSAP follow-up technical assistance on prudential regulations and risk-based supervision in order to promote financial stability • FSAP follow up technical assistance on development in financial sector to promote financial inclusion agenda in Cambodia including micro-insurance	Ongoing	Two or three missions a year.
	• TA on AML/CFT, payment system road map, and financial education	Ongoing	June 2017
	Public sector management • Public Financial Management Reform Program (PFMRP) • Public administration reform (PAR) potential technical assistance support envisioned • Public Expenditure Review (PER under elaboration, to cover tax incentives, public investment management and key sectors such as agriculture and education • Preparation for Cambodia's systematic country diagnostic looking into sources of growth including drivers of growth and key constraints and bottlenecks	Ongoing	
	Trade and Private Sector Development • Trade Related Assistance in Cambodia (TRAC under Bank Execution) • Trade Dev. Support Program (TDSP under Recipient Execution) • Trade Logistic Blueprint and Connectivity • Customs modernization and reform • Nontariff measure (NTR) and trade repository • Investment incentive policy • SPS automation system, • Certification of country origin automation, • Trade mark registration and Intellectual Property Rights • Business registration automation system		
The IMF's Work Program in the next 12 Months	**Macroeconomic policy analysis and advice** • 2016 Article IV consultation • Policy notes on request	July 2016 Ongoing	October 2016
	Technical assistance • Fiscal sector: Tax administration, macro-fiscal capacity building, PFM • Financial sector: FSAP follow-up work, resident banking supervision advisor, consolidated supervision, foreign exchange market, liquidity management, data improvement • Statistics: National accounts, price, balance of payments • Budgetary reform including program-based budgeting • International public sector accounting standards	Ongoing	
Joint Products in the next 12 months	**B. Agreement on Joint Products and Missions** • Debt sustainability analysis	2016 Article IV consultations	During Article IV consultations

RELATIONS WITH THE ASIAN DEVELOPMENT BANK

(August 2016)

As of June 30, 2016, Cambodia has received $2.38 billion in Asian Development Bank (AsDB) lending, grants, and technical assistance, including: (i) 80 Asian Development Fund (ADF) loan projects and programs for $1,928.3 million with low interest; (ii) 2 Ordinary Capital Resources (OCR) loans for $83.0 million; (iii) 21 ADF grants for $255.71 million; and (iv) 2 special fund grants for $6.0 million. Cumulative disbursements to Cambodia for sovereign and non-sovereign lending and grants are $1,670.0 million.

The sector composition of active lending, grants, and technical assistances totaling $1,071.1 million comprises: (i) Agriculture, Natural Resources and Rural Development $284.2 million (27 percent); (ii) Transport and Communications $197.8 million (18 percent); (iii) Water Supply and Urban Infrastructure $181.5 million (17 percent); (iv) Multisector $137.0 million (13 percent); (v) Education $101.4 million (9 percent); (vi) Industry and Trade $83.0 million (8 percent); (vii) Energy $45.0 million (4 percent); (viii) Public Sector Management (PSM) $30.1 million (3 percent); and (ix) Health, Nutrition and Social Protection $10.0 million (1 percent).

The AsDB Cambodia Country Partnership Strategy (CPS), 2014–2018, endorsed by the Board on November 28, 2014, aligns with Cambodia's strategic planning cycle and the priorities reflected in the Rectangular Strategy for Growth, Employment, Equity and Efficiency, Phase III (RSIII) and the National Strategic Development Plan (NSDP, 2014–2018). Consistent with the Royal Government of Cambodia's economic reform priorities, the impact of the CPS will be reduction in poverty and vulnerability. The CPS embeds the three strategic agendas of the Midterm Review of Strategy 2020 into all AsDB operations: (i) inclusive economic growth; (ii) environmentally sustainable growth; and (iii) regional cooperation and integration (RCI).

The 2014–18 CPS builds on two strategic pillars for AsDB's activities in Cambodia: (i) rural-urban-regional links, and (ii) human and social development, and one facilitating pillar: PSM. Expanding rural-urban-regional connectivity is an integrated approach to developing those areas where most poor people live and focuses on transport and economic corridor development to link national value chains with the region and the world. This pillar develops rural-urban-regional infrastructure (including irrigation and water management, rural electrification, rural roads, rural water supply, urban infrastructure, road maintenance, and trade facilitation) and supports the commercialization of farms and competitiveness of agribusiness through improved connectivity. The second pillar, targeted human and social development, supports access to, and the quality of, secondary education, and targeted skills development through technical and vocational education and training linked to evolving demands of the labor market. PSM covers decentralization and deconcentration and public financial management reforms and acts as facilitating pillar to improve country and sector governance and mitigate project-level fiduciary risks.

AsDB has been a leading development partner of the finance sector in Cambodia since 1999. A comprehensive approach was required to rebuild the financial system in a devastated economy that had no finance sector. The Third Financial Sector Program (FSP) (2011–2014) supported implementation of recommendations of the 2010 Financial Sector Assessment Program (FSAP) and initial stages of the government's Financial Sector Development Strategy (FSDS), 2011–2020. After successfully rebuilding the basic foundation of the banking industry under the First and Second FSP, the Third FSP supported the sector's expansion to cover the important subsectors of nonbanking services and capital markets, and to boost investor's and beneficiaries' confidence in the system with a stronger legal and regulatory framework, necessary infrastructure, and better quality of services, including consumer protection. The Inclusive Financial Sector Development Program (2014-2020) consists of three subprograms as part of implementation of the FSDP 2016–2025 and combined with substantial TA, will support capacity development for several relevant government institutions. First, the program is supporting the completion of a draft national strategy for financial inclusion for rural areas, agriculture, and SME development. The program is also enhancing financial stability and confidence, which represents a key prerequisite for financial inclusion. Finally, the program is supporting finalization of draft laws and lay the foundation for strengthening financial system infrastructure.

Under the CPS 2014–2018, AsDB's private sector operations focus on finance sector development, including private equity, transport, agribusiness, water supply and sanitation, and trade and supply chain finance for SMEs. Investments in synergy with AsDB's public sector assistance is supported, and TA is facilitating project development, reducing entry barriers, improving governance, and develop capacity.

AsDB has assisted the government to review existing policies, laws, regulations, and institutional arrangements for Public Private Partnerships (PPPs) and supported development of the Policy Paper on PPPs For Public Investment Project Management. Under a capacity development technical assistance project, AsDB is currently helping to build the institutional capacity of government agencies which will be involved in developing future PPPs. Through a project preparatory technical assistance, AsDB has in early 2016 started to support the government in establishing a legal and institutional framework for development of PPPs, and will help to develop a pathfinder PPP project pipeline and pilot project.

Asian Development Bank: Loans/Grants Commitments and Disbursements to Cambodia, 1992–2016

(In millions of U.S. dollars, as of June 30, 2016)

No.	Year	Loan/Grant Approvals [1]	Contract Awards/ Commitment	Disbursements
1	1992	69.4	0.0	0.0
2	1993	0.0	4.4	5.4
3	1994	28.2	35.9	12.2
4	1995	45.1	28.1	35.9
5	1996	105.0	15.3	32.1
6	1997	0.0	41.5	10.7
7	1998	40.0	29.1	29.3
8	1999	88.0	17.0	26.2
9	2000	109.6	114.4	50.8
10	2001	75.2	40.7	48.3
11	2002	116.5	64.4	78.9
12	2003	98.3	61.9	73.3
13	2004	65.0	62.4	76.7
14	2005	52.0	96.4	84.5
15	2006	69.8	44.3	55.1
16	2007	72.1	82.5	70.1
17	2008	84.1	140.7	137.7
18	2009	144.5	59.8	82.7
19	2010	160.8	64.3	71.4
20	2011	70.0	128.6	122.3
21	2012	275.5	79.5	60.5
22	2013	148.0	149.7	238.6
23	2014	226.0	104.0	98.7
24	2015	130.0	129.5	114.7
25	2016	0.0	66.1	54.0
	TOTAL:	**2,273.0**	**1,660.3**	**1,670.0**

Source: Asian Development Bank as of June 30, 2016.

[1] Approvals include OCR Loans, ADF Loans, and Grants only.

STATISTICAL ISSUES

(September 2016)

Assessment of Data Adequacy for Surveillance

General. Data provision is broadly adequate for surveillance. Extensive technical assistance (TA) has been provided by the IMF, United Nations Development Programme, Asian Development Bank (AsDB), and World Bank, as well as by bilateral partners, leading to substantial capacity improvements. Despite the progress made in improving data statistics, several shortcomings in macroeconomic data still hamper timely and comprehensive analysis.

National accounts. Despite improvements in recent years, weaknesses remain in the quality and timeliness of national accounts data. The quality of GDP estimates remains hampered by the lack of comprehensive and reliable source data on a production and expenditure basis, in part due to resource constraints and weak data collection techniques. In November 2011, a TA mission assessed current methodologies used to compile national accounts estimates and provided support with the development of the quarterly national accounts estimates. In February 2014, another TA mission was conducted mainly to assist the National Institute of Statistics (NIS) processing the results of Cambodia's first ever 2011 Economic Census of Cambodia (EC2011) for improving GDP estimates. The purpose of the EC2011 was not particularly focused on national accounts, hence TA concluded further improvements are needed to convert EC2011 data into national accounts data following the System of National Accounts (SNA) concepts and definitions. The TA mission also assessed the implementation of the previous mission recommendations and found that progress has stalled partly due to resource constraints. Statistics Sweden has been assisting the NIS for improving the national accounts compilation. In February 2015, a TA mission assessed current data compilation and dissemination practices and made recommendations on these issues. An assessment/diagnostic mission will be conducted in December 2016.

Price statistics. The compilation of the consumer price index (CPI) suffers from insufficient geographic coverage. An updated CPI series was introduced starting in April 2012. Geographic coverage of the series has been expanded to include Phnom Penh plus five provinces. An STA TA mission visited Phnom Penh in April 2012 to assist with updating/improving the CPI. The authorities indicated a need for assistance with developing a producer price index (PPI), but no funds have been allocated to support the compilation of an ongoing PPI.

Government finance statistics (GFS). The Ministry of Economy and Finance began implementing reforms to the government accounting system and budgetary nomenclature in 2007, based on the Government Finance Statistics Manual (GFSM) 2001, with the assistance of the IMF. To facilitate policy dialog, the authorities should consider shifting from the Tableau des opérations financières de l'État (TOFE) based on GFSM 1986 to a GFSM 2014-based budget formulation and reporting framework. Over the past three years, progress has been made, and the authorities submit annual and monthly GFS data for budgetary central and local governments on a cash basis to the IMF's Statistics Department. Going forward, the priority is to improve data compilation, namely to compile financial balance sheet, and extend institutional coverage to include data for extrabudgetary entities and social security funds. Next steps include: (i) improving the CoA to allow automatic compilation of GFSM 2014 summary statements and detailed tables in the FMIS; (ii) mapping available source data on PAE to GFSM 2014 classifications; and (iii) reporting to the World Bank-IMF Public Sector Debt Statistics database. A mission is planned by December 2016 to work on the implementation of the next steps.

Monetary and financial statistics. The NBC reports monetary data using the standardized report forms for the central bank and other depository corporations on a regular monthly basis. The NBC received TA during the FSAP on the compilation of financial soundness indicators (FSIs). In September 2015, another TA mission provided support for establishing procedures for compiling FSIs. The NBC now compiles monthly core FSIs and several encouraged FSIs, and has begun reporting them to the IMF on a regular basis since February 2016. Some data deficiencies and inconsistencies continue to pose a challenge to the compilation of FSIs, including deficiencies on sectoral classification.

External sector statistics. Cambodia's quarterly balance of payments and international investment position (IIP) are compiled by the NBC according to the Balance of Payments Manual, fifth edition (BPM5). Data present some relevant shortcomings in terms of coverage, accuracy, and timeliness. Balance of payments and IIP are compiled relying on estimation methods. Inward foreign direct investment (FDI), a relevant component of Cambodia's external transactions and positions presents large gaps, especially in regard to real estate acquisitions by nonresidents, which are not included in FDI although data are available. General Department of Customs and Excise (GDCE) produce monthly and quarterly trade data. Monthly data are regularly provided to NBC to be used to estimate balance of payments trade figures. A number of technical assistances has been provided under the Project on Improvement of External Sector Statistics, funded by the government of Japan. Recent progress has been made, especially in enhancing the International Transactions Reporting System (ITRS) and in preparing draft FDI survey. A TA mission on FDI data collection will be conducted in September 2016.

Data Standards and Quality

Cambodia participates in the IMF's General Data Dissemination System. No data ROSC are available.

Cambodia: Table of Common Indicators Required for Surveillance

(As of September 2016)

	Date of Latest Observation	Date Received	Frequency of Data[1]	Frequency of Reporting[1]	Frequency of Publication[1]
Exchange Rates	8/15/2016	8/15/2016	D	D	W
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[2]	6/2016	7/2016	M	M, 3 week lag	N/A
Reserve/Base Money	6/2016	7/2016	M	M, 3 week delay	M
Broad Money	6/2016	7/2016	M	M, 3 week delay	M
Central Bank Balance Sheet	6/2016	7/2016	M	M, 3 week delay	M
Consolidated Balance Sheet of the Banking System	6/2016	7/2016	M	M, 3 week delay	M
Interest Rates3 (Loan and Deposit rates-7/21?)	5/2016	7/2016	M	M, 2 month lag	M
Consumer Price Index	6/2016	7/2016	M	M, 2–4 week lag	M
Revenue, Expenditure, Balance and Composition of Financing[4]—General	5/2016	7/2016	M	M, 4–6 week lag	M
Revenue, Expenditure, Balance and Composition of Financing[4]—Central	5/2016	7/2016	M	M, 4–6 week lag	M
Stocks of Central Government and Central Government-Guaranteed Debt[6]	5/2016	7/2016	M	M, 3 month lag	A
External Current Account Balance	3/2016	7/2016	Q	Q, 3-5 month lag	Q
Exports and Imports of Goods and Services	6/2016	7/2016	M	M, 3 week lag	M
GDP/GNP	2015	7/2016	A	A, 6 month lag	A
Gross External Debt	2015	7/2016	A	A, 6 month lag	A
International Investment Position	N/A	N/A	N/A	N/A	N/A

[1] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A), Irregular (I), and Not Available (N/A).

[2] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.

[3] Deposit and loan rates.

[4] Foreign, domestic bank, and domestic nonbank financing.

[5] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

[6] Including currency and maturity composition.

MAIN WEBSITES OF DATA

National Bank of Cambodia (www.nbc.org.kh)

Exchange rates
Balance of payments

Ministry of Economy and Finance (www.mef.gov.kh)

Government budget
Fiscal revenue, expenditure, and financing

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

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

Statement by Mr. Mazrunisham Omar, Executive Director;
and Mr. Suasdey Chea, Advisor to the Executive Director on Cambodia
October 19, 2016

1. The Cambodian authorities would like to express their gratitude for the constructive discussions and exchange of views with staff on macroeconomic developments and policy recommendations during the 2016 Article IV consultation. The authorities appreciated the discussions on the need to effectively contain growing macro-financial risks, maintain fiscal sustainability, and enhance their financial sector and structural reform agendas for more sustainable and inclusive growth. The authorities broadly agree with staff's assessment and would take staff's recommendations into consideration when formulating future policies.

Recent Economic Development and Outlook

2. Cambodia's economy remains strong, with growth projected to be around 7.0 percent in 2016 and 2017, among the highest in Asia. Rapid economic growth has been supported by significant increase in integration with the global economy and more importantly, has been accompanied by an impressive decline in poverty from 50 percent in 2005 to 18 percent in 2012 and improved income distribution. Cambodia has successfully transitioned to a lower-middle income status this year. This growth momentum is expected to remain robust, underpinned by strong garments exports, as well as real estate and construction activities. Cambodia's transformation is guided by the Royal Government of Cambodia's Rectangular Strategy Phase III (RS III) and the National Strategic Development Plan 2014-2018, the implementation of which is on track.

3. Headline inflation picked up to 3.2 percent at end-2016 from 2.6 percent in 2015, due to higher food and oil prices. Nonetheless, headline inflation is projected to remain low and average around 3 percent over the medium term.

4. Credit growth remains high, but has moderated from 34 percent in 2014 to 30 percent in 2015, and is projected to continue slowing to around 25 percent in 2016 and 2017. The authorities share staff's views on the need to moderate the pace of credit growth to preserve financial stability while at the same time are mindful of the need to support growth. In this regard, the authorities are strengthening the financial regulatory framework, including the macro-prudential policy and crisis management frameworks. The National Bank of Cambodia (NBC) has recently introduced a Basel III-compliant liquidity coverage ratio to strengthen liquidity regulations and align them with international standards.

5. On the external front, the authorities expect the current account deficit to narrow to 9.7 percent in 2016 from 10.6 percent of GDP in 2015, due to reduced imports following the completion of major hydropower projects, low commodity prices and increasing remittances.

Over the medium-term, the current account deficit is projected to narrow further to around 8 percent of GDP, supported by the completion of several hydropower projects, and increased export and tourism receipts. Gross official reserves have increased to US$8 billion at end-August, covering 4.6 months of total imports. The authorities are encouraged by sustained FDI inflows and are committed to implement reforms to further enhance the business environment and prioritize public investments in agriculture and transportation infrastructure to promote economic diversification.

6. The authorities' welcome staff's assessment that the growth outlook is broadly positive but agree that it is subject to downside risks, particularly arising from the rapid credit growth and the uncertain external environment. China's rebalancing, which is expected to result in lower growth in the near-term, appreciation of the US dollar, weaker growth in Europe and a sharper-than-anticipated tightening in global financial conditions could impact the economy and the financial system. The authorities remain vigilant of the downside risks and continue to undertake measures and reforms to enhance macro-financial stability and ensure sustainable growth.

Fiscal Policy

7. Fiscal deficit is projected to widen to 2.6 percent of GDP in 2016 from 1.6 percent of GDP in 2015, due to higher capital spending and public sector wage bill. Tax revenue performance remains strong, and is projected to increase to 14.9 percent of GDP in 2016 from 14.6 percent in 2015. This is supported by the authorities' efforts in strengthening enforcement of the Revenue Mobilization Strategy (RMS), which resulted in improvement of tax and customs administration.

8. Over the medium term, the authorities are determined to prioritize expenditure and further strengthen revenue mobilization and governance. They remain strongly committed to the implementation of the RMS and recognize the need to rationalize investment incentives and will further review other tax policies. On expenditures, the authorities are reviewing the public expenditure framework and agree on the importance of developing a medium term fiscal framework to improve expenditure allocation efficiency. Meanwhile, the wage bill increases are being implemented cautiously to allow for capital expenditure for infrastructure investment.

9. The authorities have been continuously working on improving the monitoring of contingent liabilities, particularly from public-private partnerships. In connection with this, the authorities have designated a contingency fund account for contingent liabilities related to enterprises in the power sector.

10. While public debt has increased moderately, staff's Debt Sustainability Analysis indicates that Cambodia's risk of debt distress remains low. The authorities are open to

developing the bond market, and are committed to maintaining adequate government deposits, in order to ensure debt sustainability and secure stronger fiscal buffers, as well as to ensure macroeconomic stability over the longer term.

Monetary Policy

11. Cambodia's monetary system is characterized by a high degree of dollarization and cash-based economy that limits the NBC's ability to implement monetary policy effectively. The stabilization of the exchange rate against the US dollar continues to serve as an important nominal anchor to help keep inflation low and stable. At the same time, the NBC is fully committed to developing the interbank and money markets as well as the foreign exchange market to promote the use of the local currency (Khmer Riel) in order to allow for a more effective and flexible monetary policy framework. With regards to de-dollarization, policies and action plans are being developed to promote greater use of the local currency, and reduce dollarization in the long term.

12. The reserve requirement ratio remains an important instrument of monetary and prudential policy. It has been kept unchanged since the end of 2012 with the ratios of 12.5 percent for the foreign currency deposits and 8 percent for the local currency. Since 2013, in line with the Fund's past recommendations, the NBC issued negotiable certificate of deposits (NCDs), both in US dollar and Khmer Riel, to help develop the interbank market. This has also helped facilitate banks' liquidity management and market-based monetary policy operations. In addition, reserve requirement on banks' foreign borrowing was re-imposed in March 2015 in order to better manage short-term capital inflows to the banking system.

Financial Stability

13. Cambodia has experienced a significant increase in financial deepening, with credit growth averaging nearly 30 percent (year on year) over the past three years. Despite the strong credit growth, core financial soundness indicators remain healthy with adequate capitalization levels and high profitability, while credit quality remains sound. The distribution of credit has been to a large extent, directed to productive sectors but the authorities recognize growing exposure to the real estate and construction sectors which represent potential pockets of vulnerabilities to financial stability.

14. Mindful of the risks, efforts are on-going to strengthen the financial regulatory and supervision frameworks, and recently, several pre-emptive measures were introduced to enhance the resilience of the financial system and rein in credit growth, including the re-introduction of the reserve requirement on bank borrowing from non-residents, raising the minimum registered capital of banking and financial institutions, and implementing a Basel-III compliant liquidity coverage ratio. The NBC is also working on strengthening regulations

on asset classification and provisioning, and plans to upgrade solvency regulation. The NBC is also considering imposing prudential measures on institutions deemed to be engaged in excessive risk-takin. Going forward, the authorities will continue to closely monitor developments on this front and take necessary prudential actions to curb credit growth and maintain a sound financial system. The authorities are, however, mindful of the impact of these measures on growth.

15. The authorities are keenly aware that the microfinance sector is becoming more systemically important and have stepped-up efforts to enhance the supervisory framework for microfinance institutions. The NBC remains committed to a risk-based supervisory approach that is consistent with the FSAP recommendations. To help enhance the crisis management framework, the MoU on establishing information sharing was signed between the Ministry of Economy and Finance, the NBC, and Securities Exchange Commission of Cambodia (SECC) in 2014. The authorities have also continued to build capacity for their staff, and welcome further technical assistance from the Fund in this area. The authorities are committed to working closely with the Fund on identifying risks, improving data collection and enhancing the crisis resolution framework for the financial sector.

Continuing the Reform Agenda

16. In addressing structural bottlenecks, the authorities remain focused on public investments in roads, railways, bridges and irrigation to further promote rural development and enhance inclusive growth. Public investment in these infrastructure projects will help crowd in private investment. Over the near term, the completion of several hydropower projects will provide affordable electricity to the general population and contribute to enhancing Cambodia's business climate and competitiveness. Building on the improvements in maternal health, early childcare and primary education programs in the rural areas, the authorities will continue to remain actively engaged in the improvement and prioritization of education and healthcare development. Moreover, the authorities are working on promoting technical and vocational training, in order to address skill mismatches, which in turn will strengthen productivity and further promote inclusive growth.

Conclusion

17. Overall, the Cambodian authorities are committed to preserving macroeconomic and financial stability, promoting sustainable and inclusive growth, and stand ready to implement any measures deemed appropriate. The authorities are highly appreciative of the Fund's continued support in providing high-quality policy advice and technical assistance, particularly in fiscal, monetary and financial sector policies. Going forward, the authorities will continue to further improve their macroeconomic policy and financial sector regulatory frameworks in line with the Fund's policy recommendations.