

# Imf and the economic growth in cambodia economics essay



**ASSIGN  
BUSTER**

IMF and the struggle increase economic growth in Cambodia. Since emerging from the very darkest period in its history (POL POT regime) almost for four years, Cambodia has traversed a long way. From below ground zero, the country bounced back to rebuild the devastated economy and institutions. After the signing of Paris peace accord in 1991, Cambodia eventually had a formal election in 1993 and Cambodia has took a very important step to change its economy from plan economy to the free market. It was time that Cambodia opened its door to the foreign investors, and enterprises and companies are private own. Regarding the investment law which enacted in 1994, Cambodia attracted many foreign investment companies that created many jobs for Cambodian people. From 1993 up until now, the main export of Cambodia is garments follow by agricultural products. Tourism is also said to be the second largest export industry. Even though Cambodia is a foreign aid dependency country with nearly one third of its national budget coming from ODA (Official Development Assistance), growth in Cambodian economy has run at over 6% per annum, on average, since the early 1990s. According to the IMF, the income per capita in 2008 was \$823. Recently, Cambodia has found the gas and oil reserve which estimated to be beneficial for Cambodian economy. Oil production is expected to begin in 2011. The start of oil production in 2011 will give Cambodia an additional source of export revenue to reduce its large current account deficit and provide the funding to boost spending on the inadequate infrastructure and health and education systems. In 1999, Cambodia has successfully affiliated to ASEAN. This accession helps Cambodia to cooperate with the countries in the region in order to improve its economy by joining in AFTA, CLV development triangle, GMS, CLMV...etc. As one of the CLMV countries, Cambodia can enjoy positive

<https://assignbuster.com/imf-and-the-economic-growth-in-cambodia-economics-essay/>

regional effect in East Asia through two transmission mechanisms. First, transfer of development experience from Japan and second is the flow of investment from Japan. In addition to the member of ASEAN, Cambodia finally joined WTO in 2004. WTO membership will enable Cambodia to receive non-discriminatory MFN status in international trade, and WTO concurrence is expected to bring substantial trade and FDI benefit to Cambodia. Even though there is a good sign on economic growth, Cambodia economy is still in struggle since Cambodia lack of human resources and as well as infrastructure to improve the economy. Despite the recent heady growth rate, poverty remains widespread and about one third of population are living under the poverty line. Corruption has become a grass root in Cambodian culture that contributes to the unfair contribution of growth between the rich and the poor. The gap between the rich and poor is still high. According to the IMF report, the growth rate has fallen back by 2.7% in 2009 in response to the economic downturn. Both the garment and tourist industries were undermined by the global recession. In the first 5 months of 2009 for instance, clothing exports to the US, which is Cambodia's dominant export market, dropped 27% from the same period of 2008. According to the Labor Ministry, around 93 garment and shoe factories closed in the first 11 months of 2009, resulting in the loss of 38, 190 jobs and a further 60 factories employing 35, 337 people were forced to temporarily suspend operations, The construction sector meanwhile was weakened by the bursting of a property bubble that undermined the banking system by boosting non performing loans. The IMF has expressed concerns over the deterioration in the health of the banking sector and has urged the central

bank to strengthen its supervision of the financial system. Regarding Foreign Direct investment, Data from the UNCTAD indicate that FDI in 2008 was \$815 mn. This was below the \$867 mn level in 2007 and represented 37.9% of gross fixed capital formation. The total stock of FDI (book value) at the end of 2008 was \$4.637 bn, which was equal to 41.5% of GDP and was 193.5% above the level of 2000. In summary, owing to the latest IMF consultation, In a press release on December 8 that outlined the highlights of the just released Article IV Consultation Report, the IMF noted that after a decade of high economic growth, the economy was undermined by the global economic downturn, which led to a reduction in garment exports, foreign direct investment inflows and tourist receipts. The economy was also restrained by the collapse of the property bubble, which slowed the construction sector and had negative implications for the banking sector. The economy contracted by an estimated 2.7% in 2009. The weak economy prompted a major fall in imports that narrowed the current account deficit, and stymied inflation. Growth was expected to resume in 2010 with an increase of 4.3% in response to a rebound in the global economy which will spur garment exports.

IMF is one of the institutions in the Breton Wood system. As we have already known that the IMF doesn't make project loans and, in particular, it doesn't make loan to finance population on family planning programs. The IMF loans are intended to help the borrower countries stabilize their economic situation and cover chronic deficit in their balance of payment. Generally, a country's central bank is the borrower and recipient of the IMF funds. In the case of Cambodia, Cambodia has been one of the main recipients of the IMF

technical assistances (TA) over the past decades. TA in Cambodia was delivered under the umbrella of the Technical Cooperation Assistance Program (TCAP). The content of the Cambodian TCAP was designed jointly by the authorities, other donors, and the IMF provided a comprehensive program of TA, covering key areas of reform related to economic policy, including fiscal and banking sectors, statistic and legal reform. Over a decade after signing of the Paris Peace Accord in 1991, Cambodia was still facing many major economic challenges. Tax revenues were very low, the banking system was fragile and a fundamental civil and administrative reform was necessary to improve good governance. In the fiscal area, TA aimed at (i) strengthening tax policy and administration including human resources and improving the design of the tax system;(ii) Strengthening customs administration in order to maximize the return from pre-shipment inspection, enhance enforcement capabilities, modernize and streamline procedures; and (iii) strengthening budget management to improve the quality of budget formulation and execution, along with the design and implementation of effective internal and external audits. These objectives were pursued mostly by three long term resident experts in budget management, customs administration, and tax administration and these three experts accounted for over half of total TA delivered under TCAP. In addition, the overall objective of TA in banking sector reform was to help create a robust and efficient banking system through bank relicensing, strengthening regulations, and improving bank supervision. TA in economic statistics was meant to strengthen the capacity to produce statistics for economic policy making and private investment planning by improving national accounts, price and foreign trade data, and balance of payments, <https://assignbuster.com/imf-and-the-economic-growth-in-cambodia-economics-essay/>

government finance and money and banking statistic. The objective of TA in the legal area was to improve the financial sector legal framework. Three years after the start of the TCAP, the impact of TA in these different areas varies considerably. The banking sector reform has been largely deemed a success. The relicensing program implemented by the National Bank of Cambodia (NBC) revamped the banking system by reducing the number of banks from 31 to 17, helping to restore the banking sector soundness. In response, public confidence in the banking system appears to be gradually improving, reflected in a 22 per cent increase in the deposit base during 2002 and further gains in 2003. 6 Furthermore, loan spreads narrowed in 2003 as competition in the market appears to be increasing. Besides TCAP, every year the IMF always conduct the annual article IV discussion with Cambodia. The discussion mainly covers the area of Macroeconomic and financial policies. According to the recent press release, as in August 30 to September 10, 2010, an IMF mission from Washington, D. C visited Cambodia. The IMF mission has projected that real GDP growth will reach 4.5% to 5% in 2010, a significant turnaround from 2009. However, significant risks continue to cloud growth prospects. The fragility of the global recovery exposes Cambodia's narrow export base with its reliance on the U. S and European markets.

In the aftermath of global financial crisis, many challenges have been arising for the International Monetary Fund as well as Cambodian government to deal with. However, what the IMF have done for Cambodia are not anything new, for it has been working in Cambodia for quite a long time. Anyway, we can classify what the IMF has for and achieved in Cambodia into three main

categories: surveillance, IMF-supported programs, and technical assistance/capacity building.

In the surveillance area, the IMF has monitored the financial and economic policies of Cambodia and provided necessary recommendation on macroeconomic and financial policy to the Royal government of Cambodia. In doing so, the IMF has kept track of Cambodia's economic development and regularly consulted with the government of Cambodia in finding the solution to the problem. For instance, recently, through the surveillance activities in Cambodia, it has observe that the Cambodian banking system is being in problem as the result of global economic downturn, and therefore, it has recommended the RGC to strengthen it banking system. This recommendation was done through a mechanism that has been used by the IMF called Article IV Consultation. In that report of that consultation, the IMF's executive director pointed out like this " Immediate priorities should include strict enforcement of the new asset classification regime, prompt implementation of corrective action plans, development of a comprehensive bank restructuring framework, and increased supervision capacity."

Regarding the technical assistance/capacity building program, the IMF assists Cambodia as well as other low-and middle income countries to manage their economies effectively by providing practical guidance and training on how to upgrade institutions, and design appropriate macroeconomic, financial, and structural policies. In connection to such TA and capacity buildings, the IMF has made great achievements in Cambodia. For example, the IMF has

provided technical assistances to National Bank of Cambodia (NBC) in banking supervision, restructuring of banking system, balance of payment and monetary statistics, operation in foreign exchange and international reserve management, and information and computerization systems. Besides, the IMF has also helped the Ministry of Economy and Finance in fiscal policy management, and it has also assisted the Department of Custom and Excise in strengthening custom administration. Moreover, the IMF has also aided the Cambodian's Ministry of Justice and the Ministry of Commerce to prepare insolvency law. Furthermore, the Ministry of Planning and the National Institute of Statistic has also received technical assistance from the IMF in preparation of national account and government's finance statistics.

Relating to IMF-supported programs or lending programs, the IMF offers credit to the members who have trouble meeting their international payments and cannot find sufficient financing on affordable term. The main objective of this program is to help a country restore macroeconomic stability by rebuilding their international reserves, stabilizing their currency and paying for import. Cambodia like many other low-income countries has received a lot of concessional loan from IMF to develop their economy and reduce poverty. For instance, just to recall the year 1996, in that year the IMF provided a 41 million USD to the Royal government of Cambodia under the enhanced structural adjustment facility (ESAF) mechanism.

As mentioned in previous mini-compositions, the International Monetary Fund has played very important role in global financial system. Its primary role is to help member countries maintain exchange rate stability by providing short term loan to those countries that are in balance of payment

<https://assignbuster.com/imf-and-the-economic-growth-in-cambodia-economics-essay/>



difficulty due to trade deficits or other factors. It was created at the end of World War II with an aim to support the global economic structure and financial order. To accomplish this task, the IMF has actively assist Cambodia and many other member states, especially the developing ones, through surveillance, technical assistance/capacity building and supporting program. Despite many success has been made, there are still problem that can be considered as the obstacle for the IMF in Cambodia, but here I am going to raise only two main issues to discuss.

The first problem that challenge IMF is the negative consequence of global economic downturn that puts Cambodia' economy in a dangerous place. As we have already known Cambodia economy depends heavily on garment, construction, and tourism sector. These sectors are the most hit by the crisis as they largely rely on foreign market and capital. For instance, according to a study conducted by the United Nations in Cambodia in 2009, about 20-30 percent of workers in garment sectors, construction sites and tourism sector have lost jobs since late 2008.

This make Cambodia's economic growth rate to decline dramatically from double digits in the years prior to the crisis to only 0. 1 percent in 2009. This reflect that the IMF, as well as other Multilateral Financial Institutions such as World Bank and Asian Development Bank, to work harder in order to help promote the Cambodian economy in the wake of the global economic downturn. This is not an easy task for the IMF to deal with because the countries, such are the

United States, which are the major financial contributors to this organization, are also in financial difficulty due to the impacts of the crisis.

The second problem is not related to any other factors, but it is because of the procedures of the IMF itself. Before providing loan to Cambodia or any other countries who are in demand for financial assistance, the IMF first demand Cambodia and those countries to make reform such as reducing public spending, devalue their national currency and privatization . These demands, to a large extend, are consider by the Cambodian government and other assistance recipient government as new burden on their economy rather than something that can help them out of the problem. Hence, those governments do not want to rely on the IMF, they seek to obtain financial assistance from other sources. For instance, instead of follow the demand by the IMF in the sector that the Royal government of Cambodia found not important but would actually harmful the Cambodia's, the government would turn to seek the assistance from China instead.

Having experienced almost three decades of ravaged civil wars, Cambodia's economy was greatly devastated. The Royal Government of Cambodia (RGC), with the technical and financial assistances from international development partners has been working very hard in reconstructing the war-torn economy. Among those development partners, the International Monetary Fund has also played a very active one. As we have discussed in the previous mini-compositions, the IMF has made significant contribution to the development of Cambodia.

Like other development partners, the IMF gets involve in the Cambodia's development in three main mechanisms. First of all, the IMF has monitored the financial and economic policies of Cambodia and provided necessary recommendation on macroeconomic and financial policy to the government. Second, it assists Cambodia as well as other low income country to manage their economies effectively by providing practical guidance and training on how to upgrade institutions, and design appropriate macroeconomic, financial, and structural policies. Last but not least, the IMF offers credit to Cambodia and other members who have trouble meeting their international payments and cannot find sufficient financing on affordable term. The main objective of this program is to help a country restore macroeconomic stability by rebuilding their international reserves, stabilizing their currency and paying for import. Through these mechanisms, Cambodia and many other developing countries have benefited greatly from the IMF.

Though everyone agrees that the IMF provides a lot of benefit to recipient countries, many of them do not happy with the IMF. The problem is that the assistance that the IMF offers to Cambodia as well as other low income countries always comes along with conditions. In order to be able to receive IMF's assistance, the recipient countries must agree with the IMF to accept the policies suggested by the IMF. Indeed, the policy suggested by the IMF are the ones already implemented successfully in some recipient countries. With this reason the IMF may expect that those policies must be plausible for every recipient country. However, in reality the same policy does not guarantee the same result for different country. Some policies might work well in some countries, but they might failed if applied to Cambodia or other

countries else. For instance, one would expect that increase interest rate for deposit would increase the amount of deposit in financial institutions. Of course, this is true for those countries in which the financial or banking system is popular among the

people. However, in Cambodia this policy will never work, for the majority of Cambodian people do not deposit their money in banks, but they just keep their money at home instead. Based on this sense, some possible disagreements between the government and the IMF arise. This makes the Royal government of Cambodia and other recipient countries prefer the assistance from other development partner to the assistance from IMF. For instance, the Cambodian government values the assistance from China the most because when provides assistance to Cambodia, China does not link with any conditions.

In short, in spite of considerably succeed in various aspects of development in Cambodia, IMF has been faced and continues to face many challenges. However, the presence of IMF as the global financial governance is still very important.