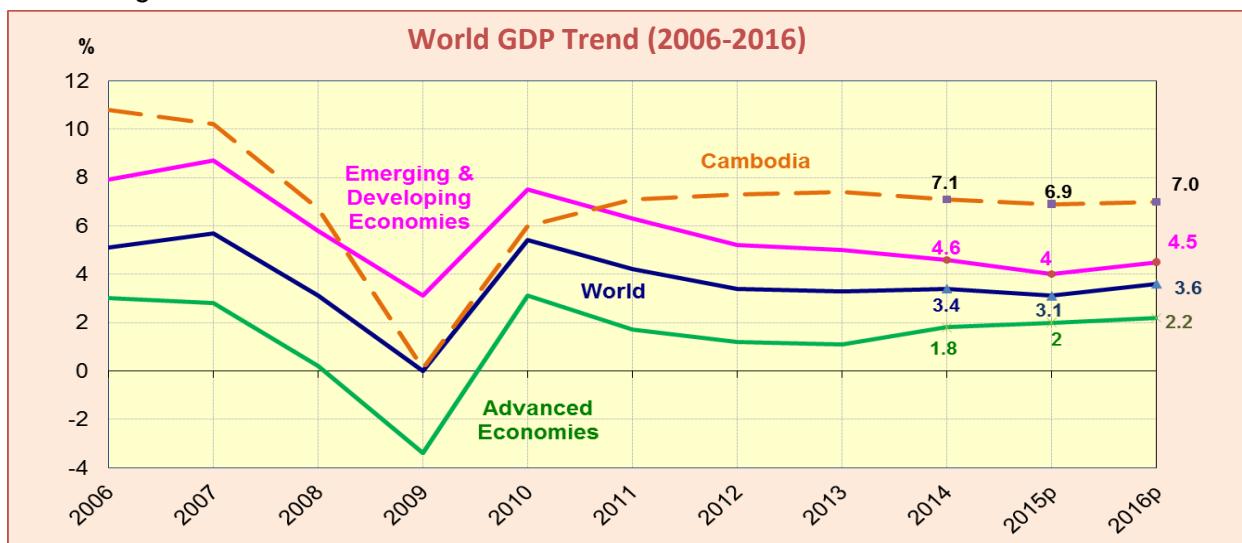


Cambodia's 2015 Macroeconomic Development and Prospect

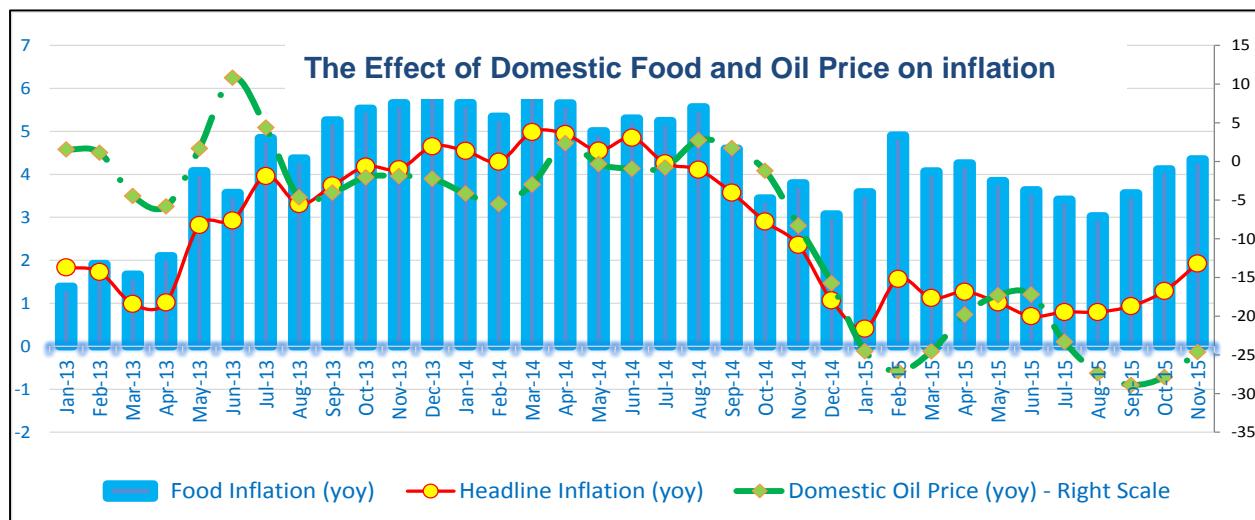
- In 2015, the global economy continues experiencing an uneven and slower growth. For developed economies, United States grew robustly while for Europe and Japan growth remained tepid. Meanwhile, developing and emerging countries' economies have slowed down from the last five years. The aforementioned slow growth and volatility in some major economies poses uncertainty and downside risk to the world economy in the near future. The economies in transition, such as the United States whose growth remains precarious and which is expected to continue raising the federal fund rate next year after sustained economic recovery, could cause further reversal of capital flow out of emerging countries. At the same time another economy in transition, China, growth has slowed down gradually due to structural reform toward domestic based consumption and the effect of this decline could spread to various regions in the world.



- In this context, strengthening the country's and regional economic fundamentals is crucial in enhancing economic and financial stability as well as improving regional safety net, with the objective of maintaining sustainable economic growth. In the pursuance of this objective, at the end of 2015, the members of Association of Southeast Asian Nations (ASEAN) will formally establish the ASEAN Economic Community (AEC) as was planned. Situated in the region with strong and integrated economies, Cambodia has been developing herself by implementing comprehensive reform programs and other economic policies over the years. Evidently, Cambodia's economic growth is expected to remain strong in 2015, buoyant by increasing textile exports, lower oil price, and increasing domestic demand; especially, construction, real estate and consumption. The robust economic growth this year lifted Cambodia economic status to lower-middle income country in 2016. This historic achievement reflected the earnest efforts of the Royal Government in preserving social safety, political stability, and the successes of developing her economy over time. In the short to medium-term, Cambodia's economy is expected to sustain robust growth amid old and emerging challenges such as: i). erosion of export competitiveness due to the U.S dollar appreciation, increased minimum wage in the garment sector, and increased competition after the implementation of

Trans-Pacific Partnership (TPP)¹ and free trade agreement between Vietnam and European Union, economic liberalization in Myanmar, ii). Impact of economic slowdown in China and the Euro Area, and iii). Capital outflows from the region and tighter financial condition.

- In order to contribute to the Government's goals of growth, employment, equity and efficiency as stated in the Rectangular Strategy Phases III, the National Bank of Cambodia has implemented policies and measures to maintain price and exchange rate stability, develop the banking sector and human resources, enhance financial integration in the region, and also enhance financial safety net in the region. So far, the well maintained price stability has contributed to macroeconomic stability that provided favorable environment that stimulate consumption and encourage investment. The achievement of price stability in 2015 was the result of prudent implementation of monetary policy which provided optimal level of liquidity to support the development of economic activities and inflation management, the stability of price and the positive external factors such as low imported inflation and the drop in world crude oil price. With the expectation that the volume of crude oil supply is stable and the demand for crude oil remaining low, crude oil price is expected to be low in 2016 which will contribute to lower inflation in the region and in Cambodia. This year, the regional currencies have depreciated substantially against USD, especially, Thai Baht, Malaysian Ringgit, and Vietnamese Dong, which is also a factor contributing to the depreciation of Riel against the USD. In response, the National Bank of Cambodia has cautiously intervened in the foreign exchange market to smoothen the exchange rate of Riel against USD. Maintaining of the exchange rate stability, in this context, tends to both retain purchasing power of those who have income in Riel and to further improve the public confidence on the use of Riel. It is important to note that the policy of smoothing the exchange rate plays a crucial role in anchoring the price stability in Cambodia.



¹ The Trans-Pacific Partnership Agreement (TPP) is a free trade agreement currently has 12 member countries: Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, United States, and Vietnam; expected to be signed in early February 2016.

- The wider use of local currency in the economy is a critical factor in improving the effectiveness of Monetary Policy implementation. In this regard, the National Bank of Cambodia has been continuously promoting the usage of Riel of the Royal Government in a prudent manner and follow market based approach by introducing incentives on the use of Riel, enhancing cash management, improving the quality and safety of banknotes, and raising public awareness on the importance of the use of local currency. In brief, the effort of the Royal Government on the promotion the use of Riel has gradually boosted the demand of Riel in market. However, money in circulation and deposit in Riel are relatively small compared to that of USD in M2's composition; for this reason, all relevant ministries and institutions needs to contribute more to promote wider use of Riel. While the demand for local currency is increasing, the NBC continues to absorb US dollars in order to maintain exchange rate stability and increase the international reserve to an adequate level that will serve the purpose of monetary policy and enhance investors' trust on the resiliency of Cambodia's economy. As a manager of an international reserve, the NBC invest the funds in a conservative and efficient manner in diversified currencies and investment and investment product to ensure optimal risk return profile. It is worth mentioning that the IMF has recently decided to officially include RMB into SDR basket in late 2016. This will enable the NBC and other central banks to diversify their international reserves investment.

- Based on the comprehensive financial development policy, the banking sector continues to grow rapidly with improved competitiveness, efficiency, and integration in the region and the world, while playing an important role in promoting financial inclusion and sustainable economic growth. Supervisory and regulatory framework has strengthened in accordance with international standards to maintain safe and sound banking system. Meanwhile, financial infrastructures also has been enhanced including; development of interbank market through increasing the demand of Negotiable Certificate of Deposit to provide better liquidity management, development of payment system to facilitate a safe and efficiency payment and also to receive real time fund status and also to settle inter-bank. Moreover, in the context of rapid growth in banking sector, CAFIU² have been strengthening its capacity to analyze and monitor questionable transaction of individual report to guarantee that banking sector in Cambodia can be free from money laundering and terrorist financing activities. Efficiency of the work has been highly commended by FATF³ and CAFIU have also become a member of Egmont⁴.

- To support the government policies in alleviating poverty by more than 1 percent per year and to comply with ASEAN initiatives in post-2015, the National Bank of Cambodia has

² Cambodia Financial Intelligent Unit (CAFIU) governed by the Law on Anti-Money Laundering and Combating the Financing of Terrorism, promulgated in 2007.

³ Financial Action Task Force (FATF) is an inter-governmental body established in 1989 by the Ministers of its 34 member jurisdictions. The objectives of the FATF are to set standards and promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and other related threats to the integrity of the international financial system.

⁴ Egmont Group of Financial Intelligence Units (Egmont Group FIUs) provides a forum for FIUs around the world to improve cooperation in the fight against money laundering and the financing of terrorism. The Egmont Group has evolved over the years and is currently (2015) comprised of 151 member FIUs.

implemented policies to promote financial inclusion, which means widening the availability of formal financial services with reasonable prices. Recently, adult population who has accessed to financial services accounted for half of the total adult population. The development of economic and financial sectors and increasing adult population has been encouraging rapid credit growth, in particular, credit to construction and real estate sectors and manufacturing. In this context, coupled with the risk of international financial market volatility, the National Bank of Cambodia consequently imposed some major pre-emptive macro-prudential measures, such as the enhancement of capital and liquidity position, reserve requirement on non-resident borrowing in order to manage risks on time and effectively. Furthermore, the National Bank of Cambodia is studying the possibilities of introducing other necessary measures to strengthen financial stability. Meanwhile, Credit Sharing Information System has also been enhanced to improve transparency and to contribute to reducing credit risk in the banking sector. Besides, Financial Stability Committee, which was established by the National Bank of Cambodia since 2011, closely monitors the risks that affect the financial stability in Cambodia on a macro level.