

High but Fragile Growth: Fostering SMEs development to improve Cambodia's economic resilience

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The views in this presentation are those of the author and do not represent the views of the NBC.

Introduction

■ Cambodia:

- ✓ ***Fast-growing economy:*** 8% per annum over the last two decades.
- ***But sensitive to external shocks:*** Possibility of negative growth rate for the 1st time since 1994 (IMF), double poverty rate (17.6%) and increasing unemployment rate from less than 1% to 4.8% as a result of Covid-19 (UNDP).
- ***How to improve Cambodia's economic resilience?***



CONTENT

- I Cambodia's economic progress
- II Cambodia's economic vulnerability
- III SMEs development and economic resilience
- IV Barriers to SMEs development
- V Conclusion

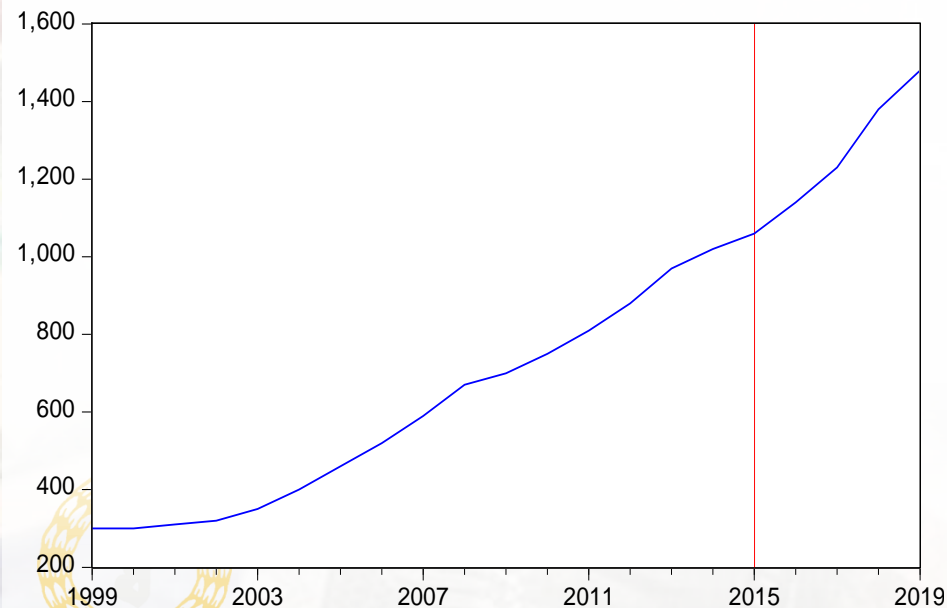


I- Cambodia's economic progress

■ Cambodia's progress:

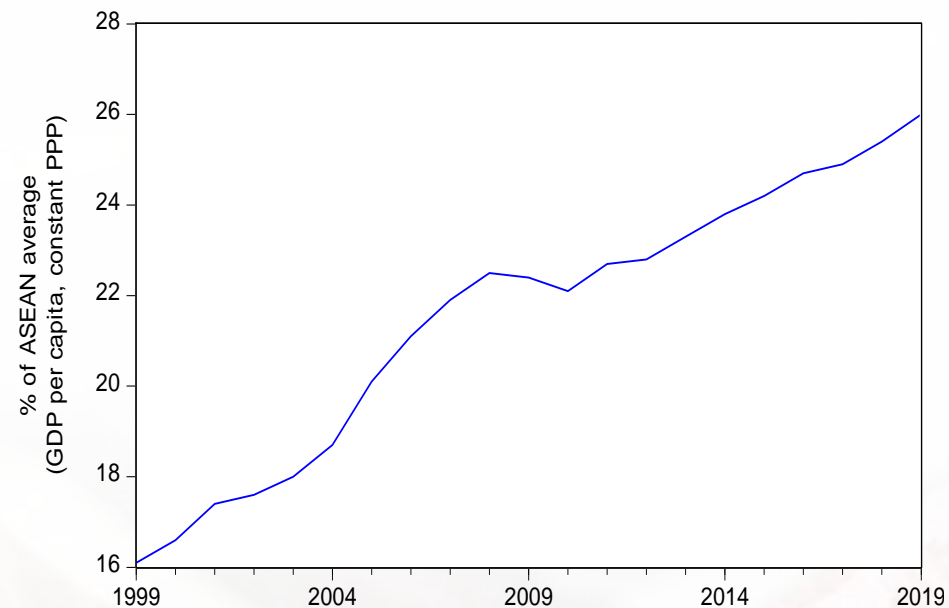
- Increase in GNI per capita by almost 5 times between 1999 and 2019, to be a lower-middle income country in 2015 and to catch up with ASEAN older member countries.

Cambodia's GNI per capita



Source: Author's graph, World Bank data

Catch up performance with ASEAN upper-income countries



Source: Author's calculation & graph, World Bank data

I- Cambodia's economic progress

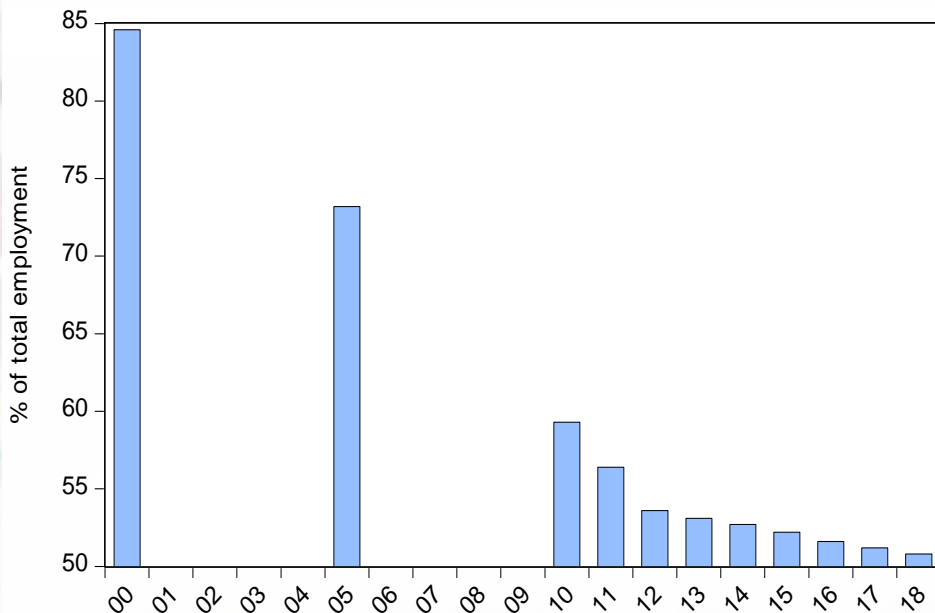
- Mainly supported by strong exports of garment-related products and rice, tourism and a recent construction boom.
 - ✓ Exports of textile, clothing and footwear increased by 11.5 times between 2000 and 2018, yet their share in total exports decreased from 85% to 73% (*Source: Atlas data*).
 - ✓ Rice export increased from 51 thousand tons in 2010 to 620 thousand tons in 2019 (*Source: UN Comtrade data*).
 - ✓ Numbers of tourists increased almost 18 times, from 0.4 million in 1999 to 6.6 million tourists in 2019, while international tourism receipts are multiplied by almost 23 times within the same period to equal 5.45 billion USD (*Source: World Bank data*).
 - ✓ FDI inflows increased from 0.1 billion USD in 1999 to 3.7 billion USD in 2019 (*Source: World Bank data*).



I- Cambodia's economic progress

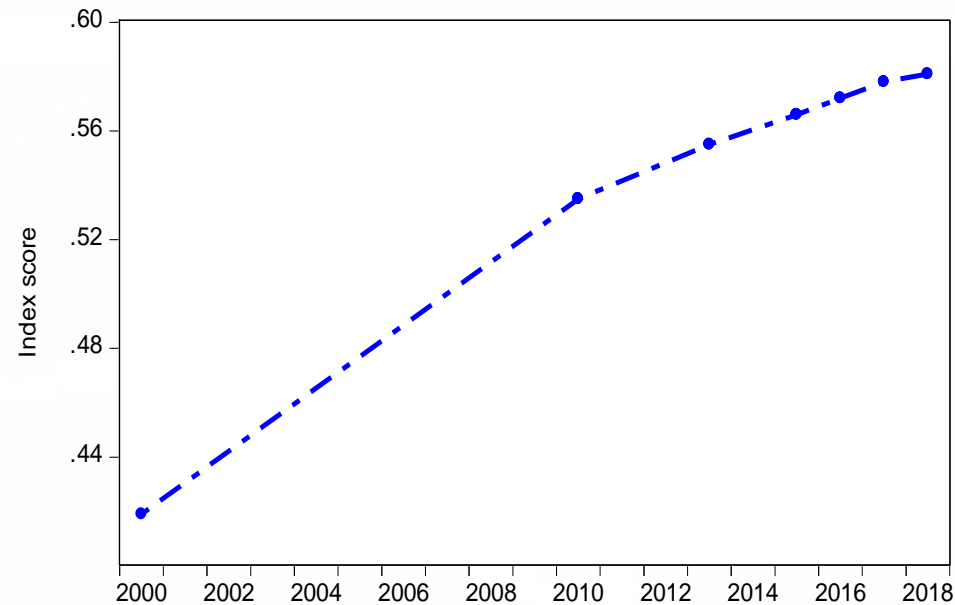
- Inclusive growth with decreasing poverty rate, share of vulnerable employment and increasing human capital development ratio.

Share of vulnerable employment



Source: Author's graph, World Bank data

Human Development Index



Source: Author's graph, UNDP data

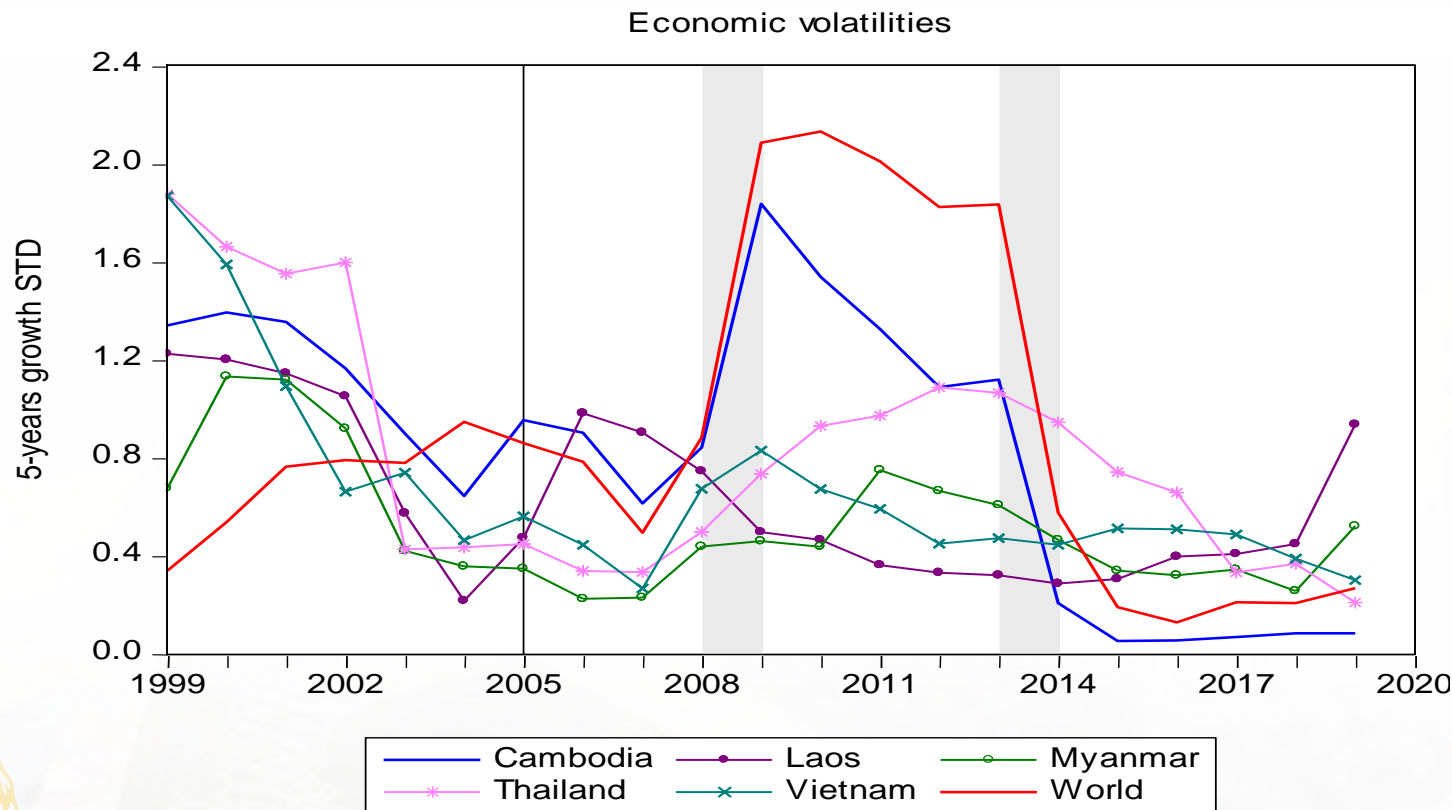
Note: HDI index varies from 0 to 1. Higher score means higher development.

- *Remarkable progress but with risks and challenges!*



II- Cambodia's economic vulnerability

- Cambodia's economy seemly expose to external risks higher than neighboring countries:
 - Close linkage between Cambodia's and global economic volatilities since 2005.



Source: Author's calculation & graph, WB data
Note: Series are standardized to have a zero mean



II- Cambodia's economic vulnerability

- The gap between the growth rate of the “damage” year and the rate averaged for the three previous years also shows that Cambodia is highly vulnerable to external shocks (*and Thailand as well*).

Assessment of economic vulnerability to global economic shock

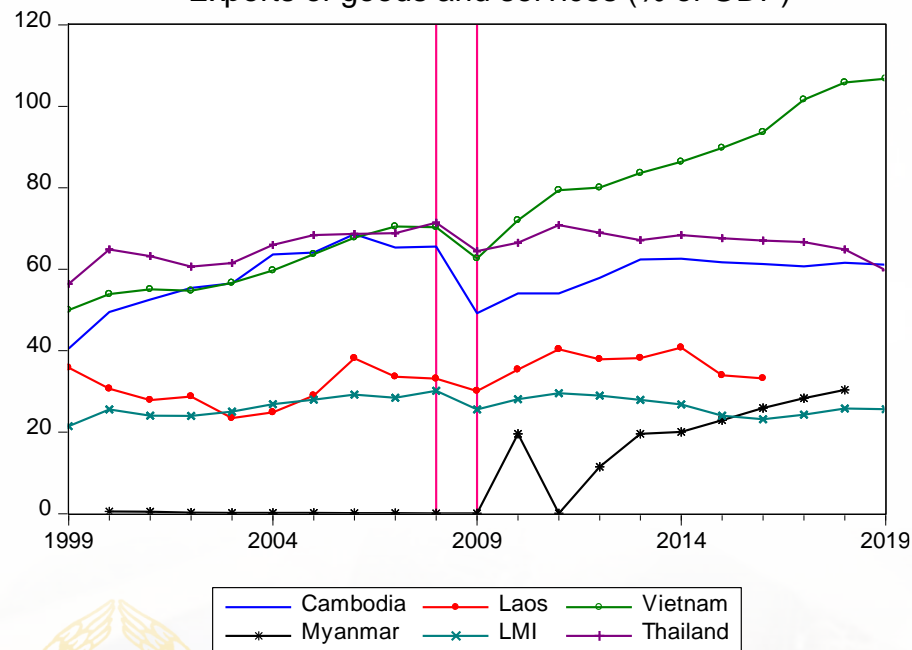
Countries	2006-2008 average	2009	Change	2017-2019 average	2020	Change
Cambodia	9.2	0.1	-9.1	7.1	-2.8	-9.9
Laos	8.0	7.5	-0.5	6.0	0.2	-5.8
Vietnam	6.6	5.4	-1.2	7.0	1.6	-5.4
Myanmar	11.8	10.6	-1.2	6.6	2	-4.6
Thailand	4.0	-0.7	-4.7	3.5	-7.1	-10.6
LMI	6.0	4.9	-1.1	5.0	NA	NA

Source: Author's table using World Bank and IMF data, adapted from Khuong Vu (2020)

II- Cambodia's economic vulnerability

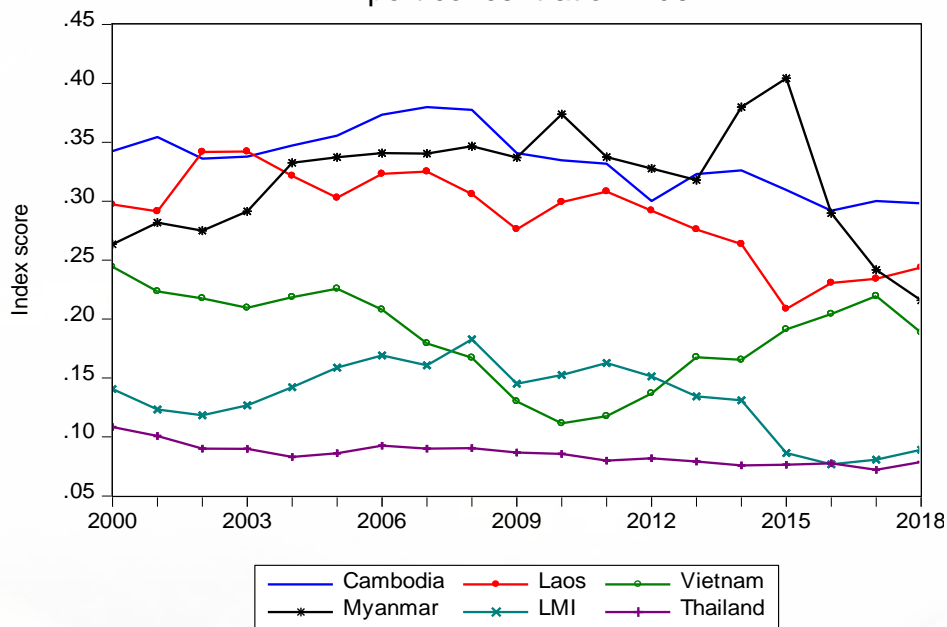
- Due to highly dependence on external demands:
 - Strong reliance on exports with low diversification.

Exports of goods and services (% of GDP)



Source: Author's graph, World Bank data

Export concentration index



Source: Author's graph, UNCTAD data

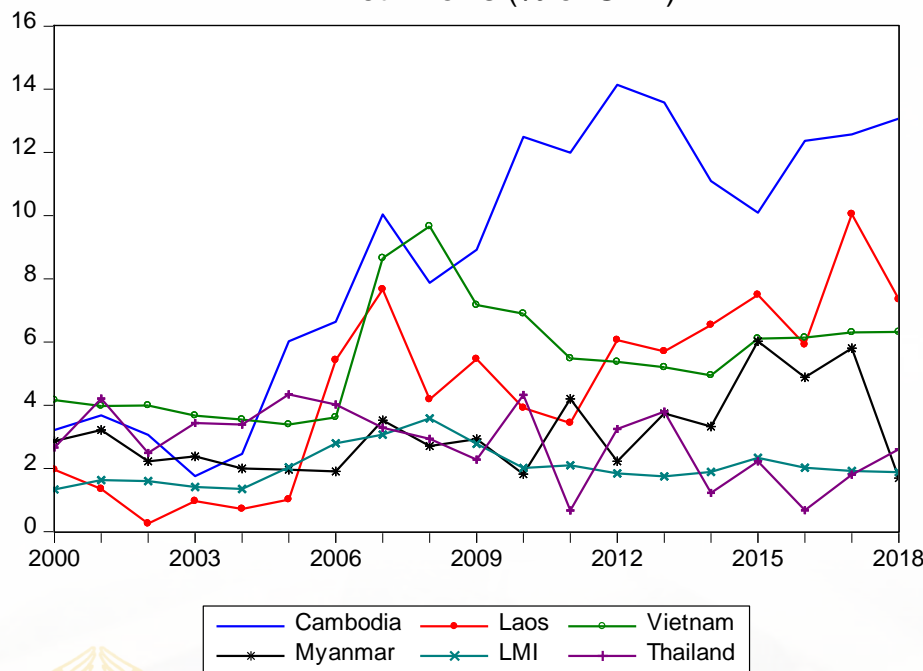
Note: Index score varies from 0 to 1. Higher index means higher export concentration.



II- Cambodia's economic vulnerability

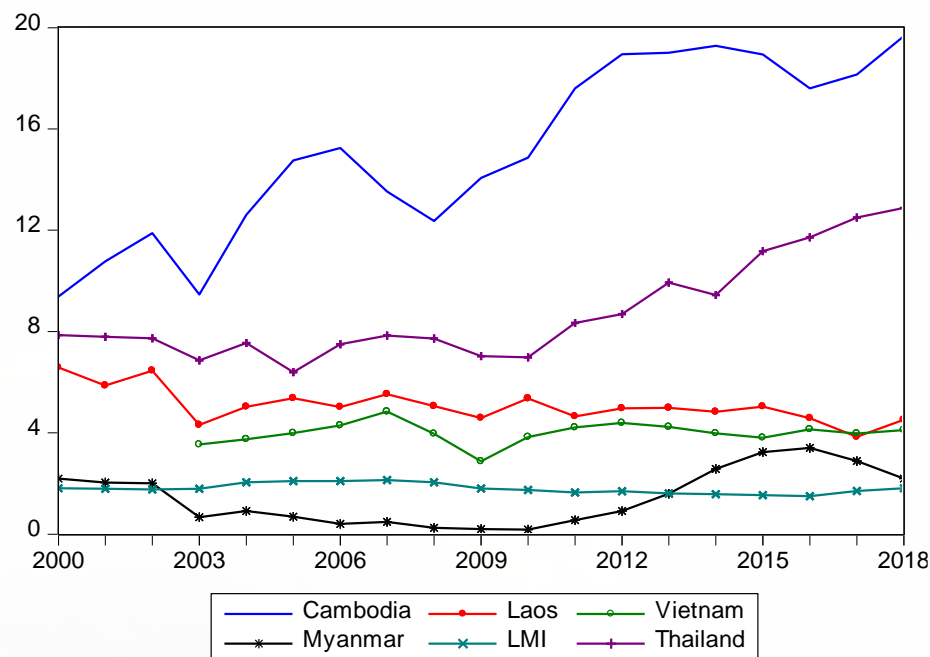
- Strong reliance on FDI inflows and international tourism receipts.

FDI net inflows (% of GDP)



Source: Author's graph, World Bank data

International tourism receipts (% of GDP)



Source: Author's calculation & graph, World Bank data



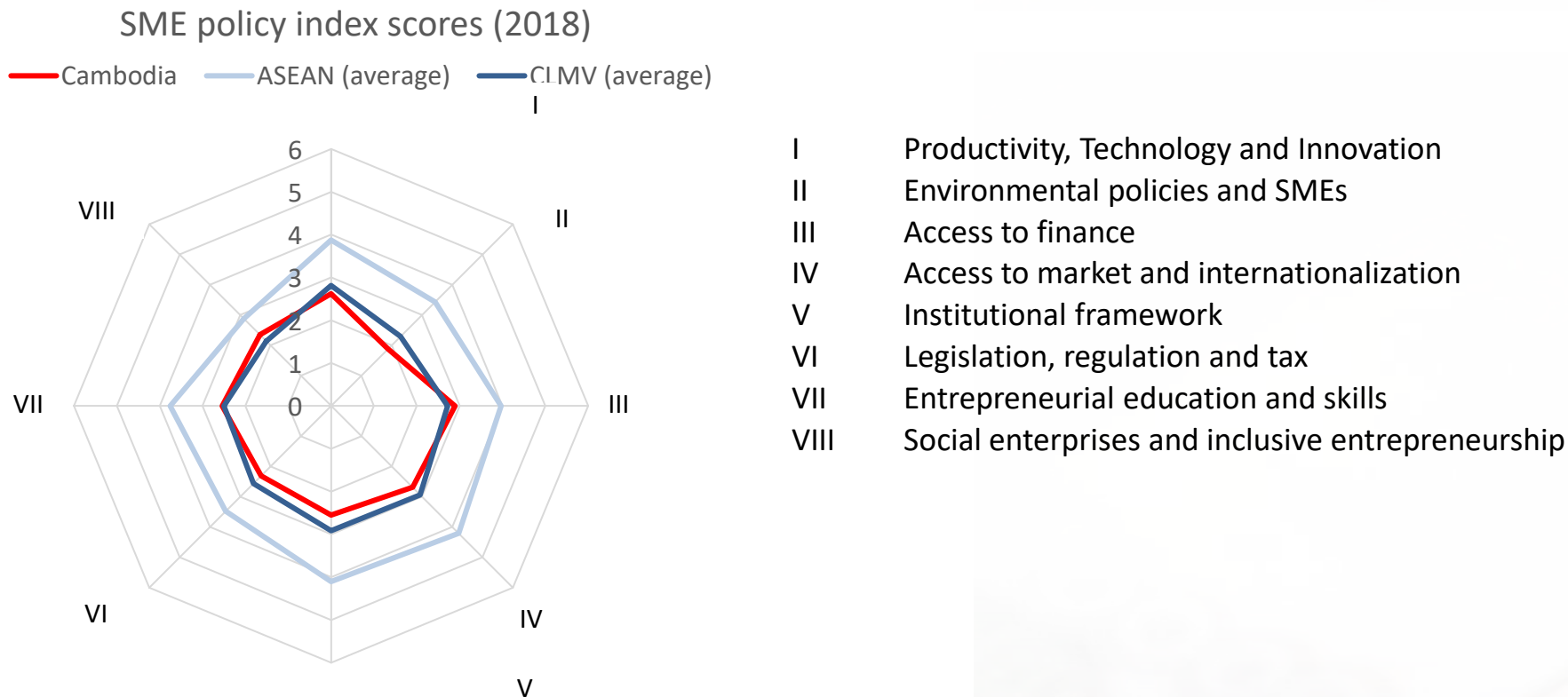
III- SMEs development and economic resilience

- SMEs stimulate domestic demand through job creation, industrial base expansion and competition, a driving force behind a resilient national economy (Shinozaki, 2014).
- The development of SME sector could lead to a dispersal of economic activities to small towns and rural areas, reducing income inequality and promoting rural development (Perkins et al., 2001; Palley, 2002).
- In the later stages of development, SMEs can form industrial clusters and position themselves near large and exporting firms, enabling them to link with large firms and acquire new knowledge and technology (Huang, 2003).



III- SMEs development and economic resilience

- A remarkable progress of SME sector over the past two decades, but several constraints remain.

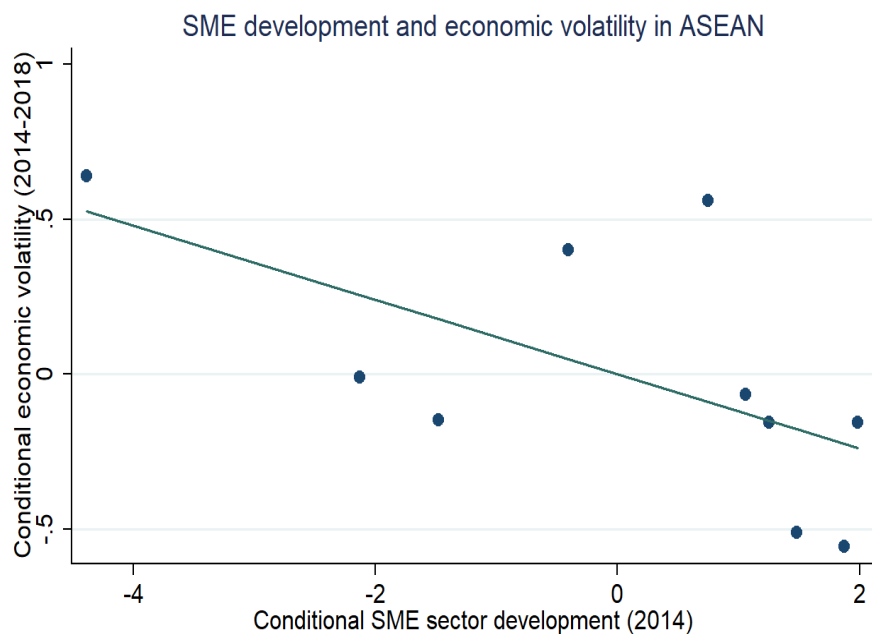


Source: Author's graph using data from ERIA-OECD report (2018)



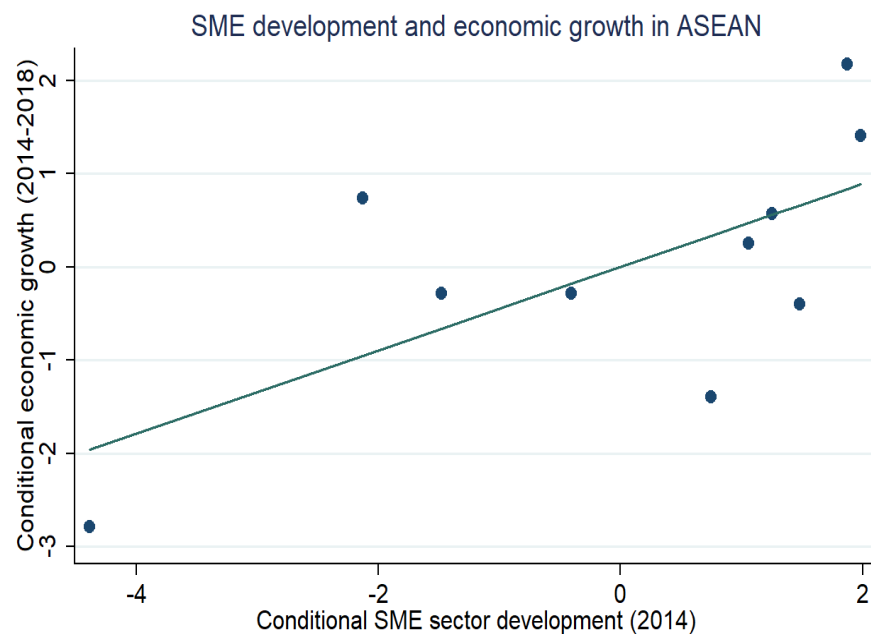
III- SMEs development and economic resilience

- A significant correlation between SME sector development and economic resilience in ASEAN: Countries with a strong SME development tend to experience a less volatile growth.
- A positive correlation between SME sector development and economic growth.
 - SMEs development could promote a strong and resilient growth.



Source: Author's calculation & graph, World Bank and ERIA-OECD data

Note: Correlation between variables is conditional on each country's level of development, proxied by the log of GDP per capita in 2014 at constant PPP. Correlation is significant at 5% level.



Source: Author's graph & calculation, World Bank and ERIA-OECD data

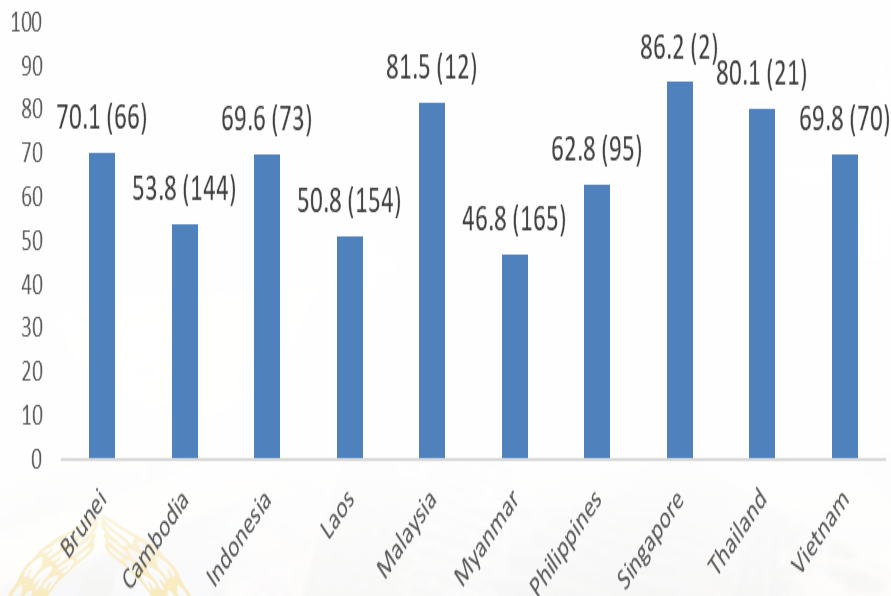
Note: Correlation between variables is conditional on each country's level of development, proxied by the log of GDP per capita in 2014 at constant PPP. Correlation is significant at 5% level.

IV- Barriers to SMEs development

i-/ SMEs formalization: Regulations and coordination improvement

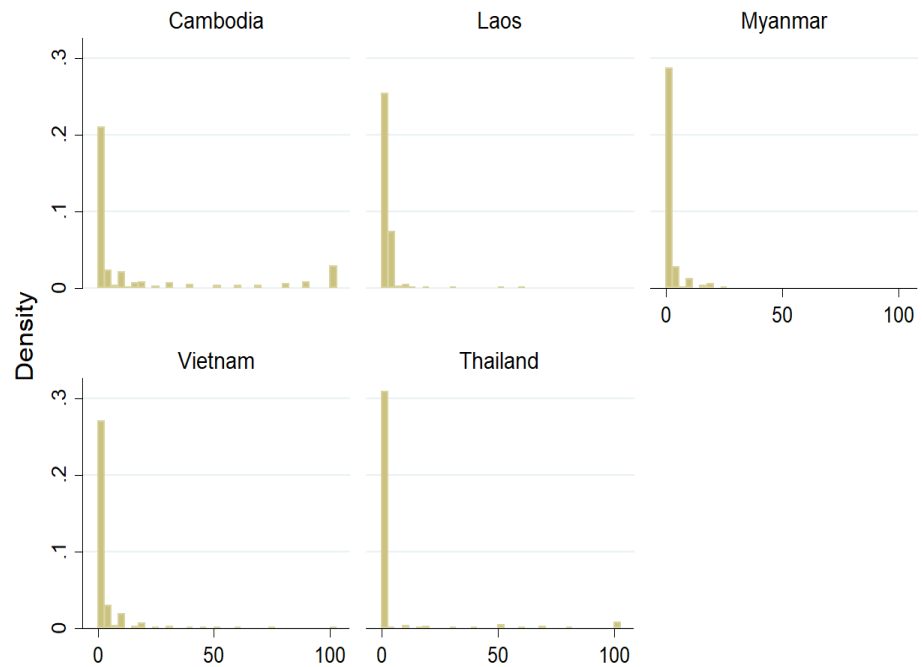
- Significant improvement of investment climate, but still behind several countries in the region.

Doing Business score (Rank)



Source: Author's graph using data from "Doing business" report 2020

Percent of senior management time spent on dealing with government regulations

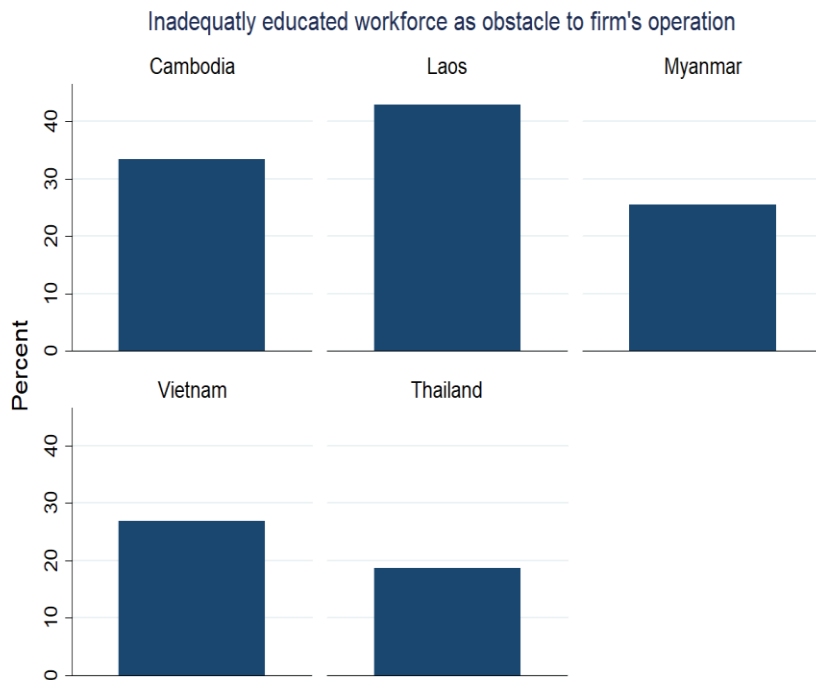


Source: Author's graph using World Bank enterprise surveys data in 2015 and 2016

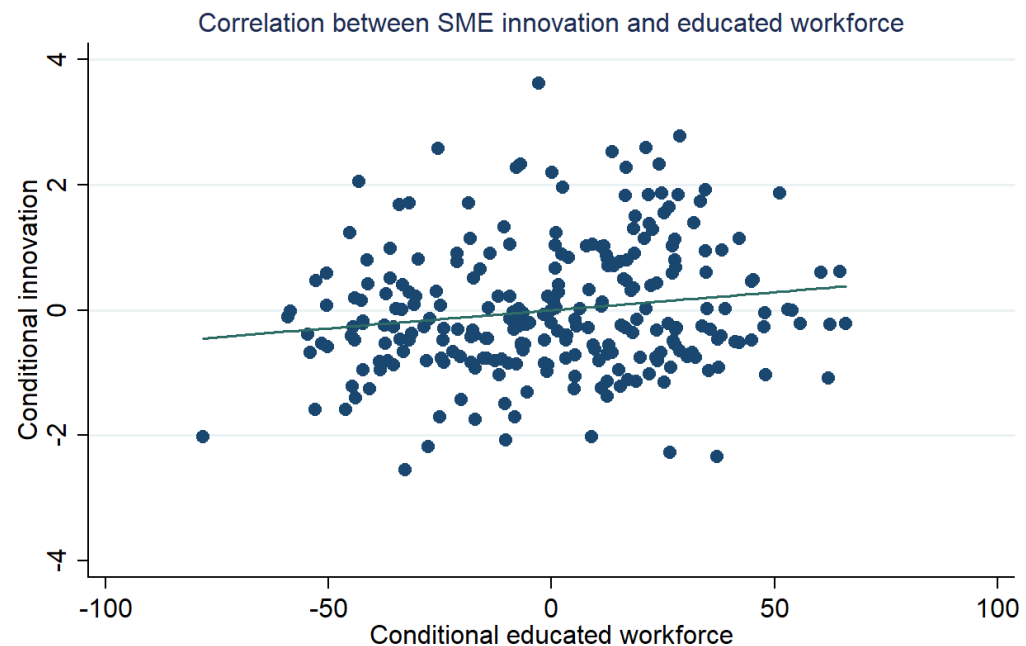
IV- Barriers to SMEs development

ii-/ Education and skill development

- Lack of skills: Prominent challenges in Cambodia
- Lack of educated workforce may limited firms' innovation and development.



Source: Author's calculation & graph using WB enterprise surveys in 2016



Source: Author's calculation & graph using WB Cambodian enterprise survey in 2016

Note: The correlation is significant at the 5% level after controlling for firm size, number of year in operation, experiences of top managers, industry, region, size of locality, usage of technology, size of last year's investment, export-orientation.

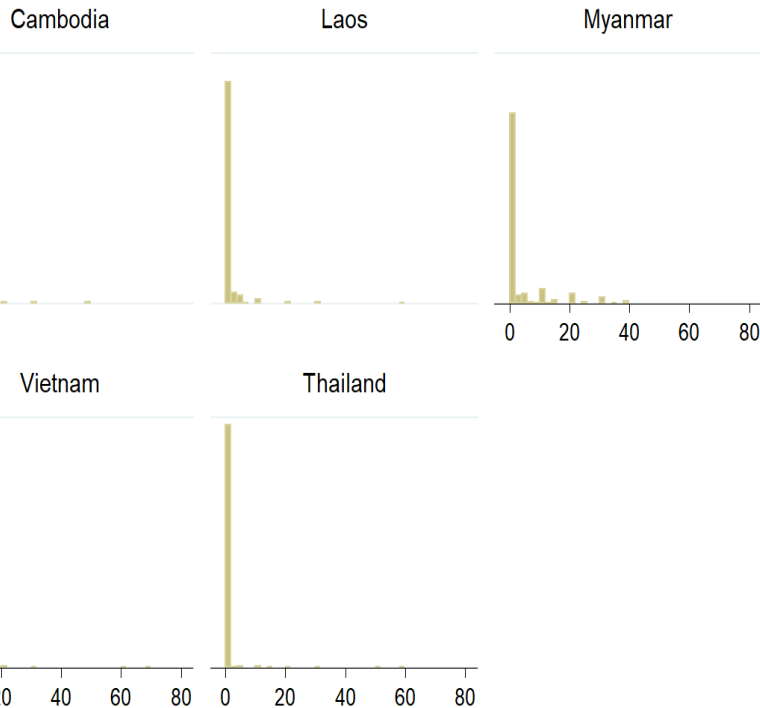


IV- Barriers to SMEs development

iii-/ Infrastructure development

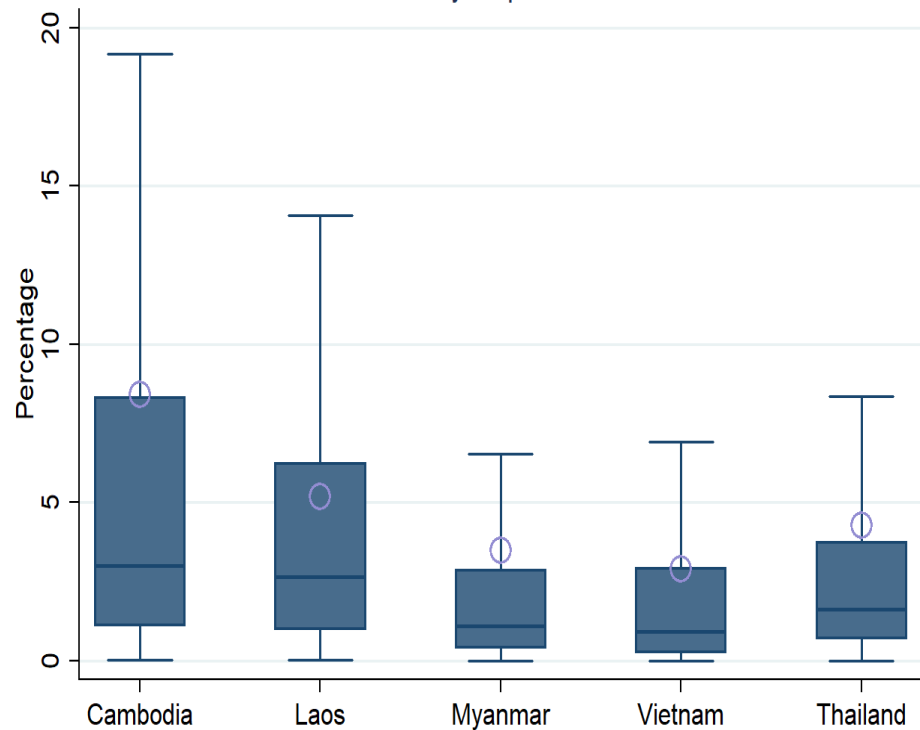
- Slightly higher loss due to power outage.
- Higher electricity costs and higher variability as well: A possible large gap in electricity access across the country (urban vs rural).

Loss as percentage of total annual sales due to power outages



Source: Author's graph using World Bank enterprise surveys in 2015 and 2016

Costs of electricity as percent of total sales

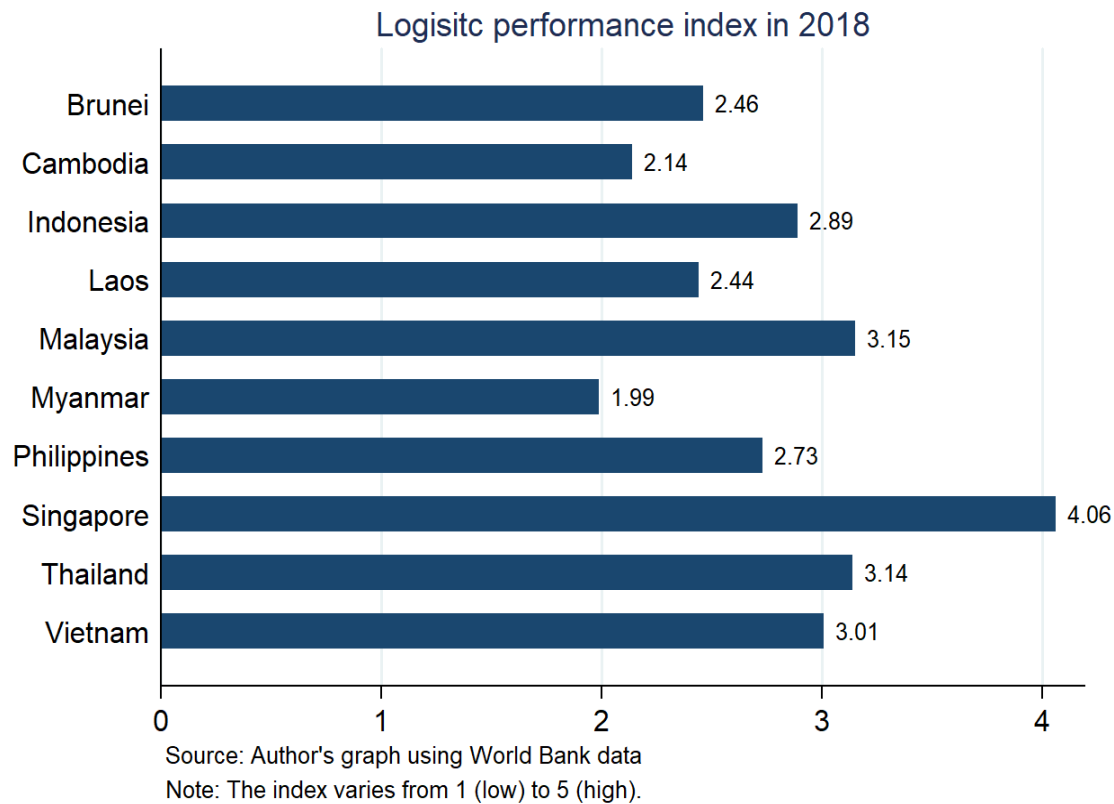


Source: Author's calculation & graph using World Bank enterprise survey data in 2015 and 2016

IV- Barriers to SMEs development

iii-/ Infrastructure development

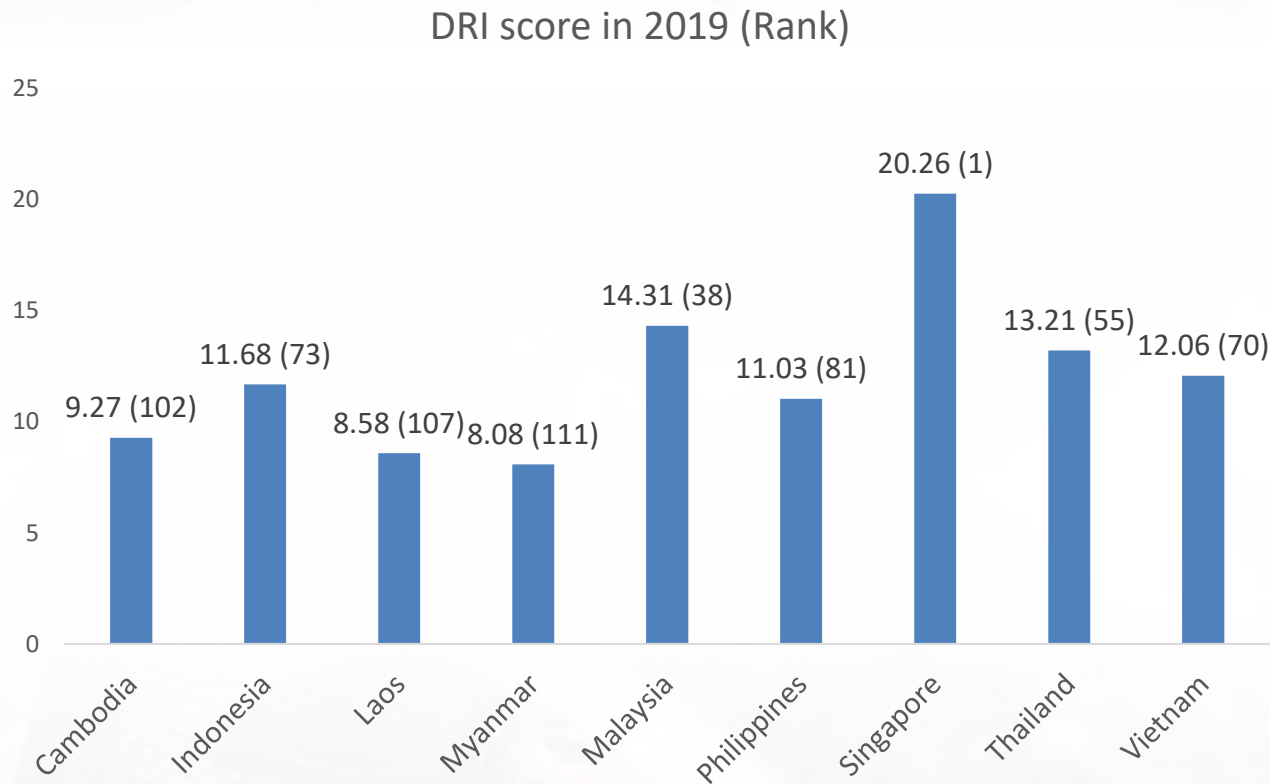
- Higher transportation and logistics costs than in neighboring countries.



IV- Barriers to SMEs development

iv-/ Digitalization

- Cambodia still lags behind several countries in terms of digital readiness: 8th in ASEAN and 102nd out of 141 countries.



Source: Author's graph using data from CISCO.

Note: The maximum score is 25. There are data available on 141 countries.

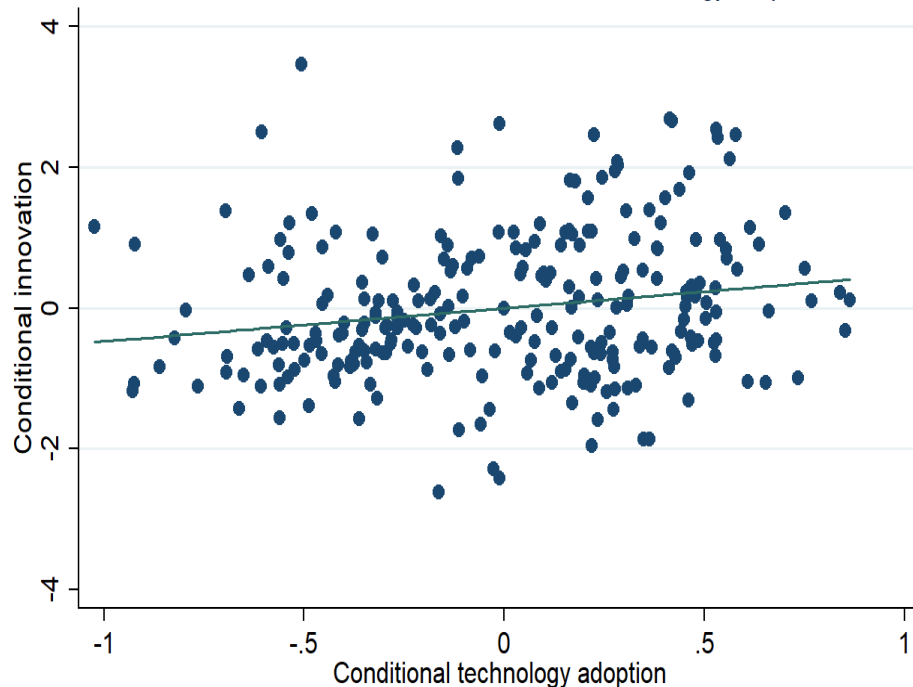


IV- Barriers to SMEs development

iv-/ Digitalization

- Technology adoption is positively correlated with innovation and sale performance of Cambodian SMEs, but the adoption rate is still low.

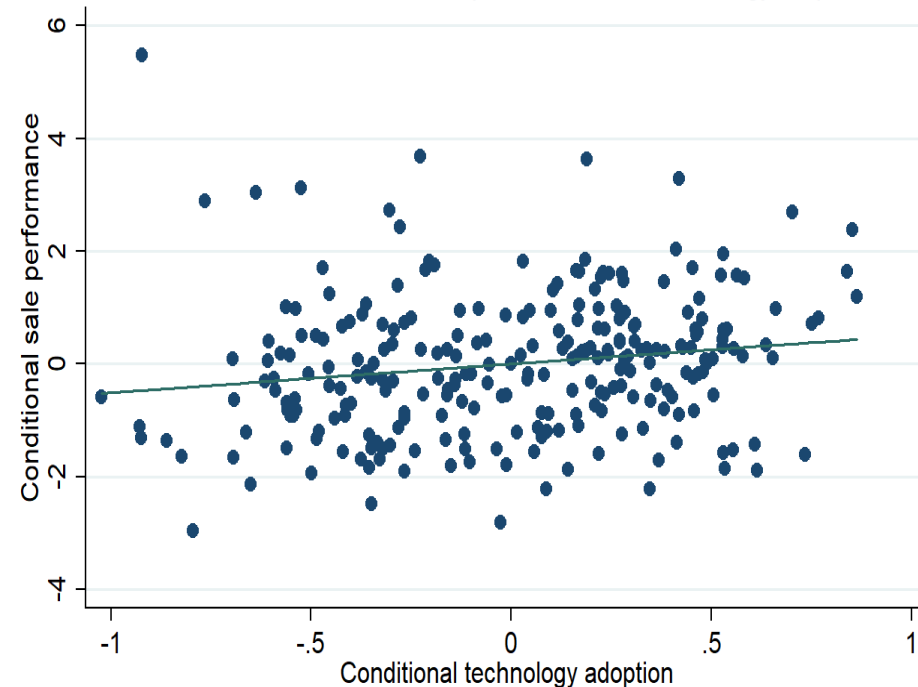
Correlation between SME innovation and technology adoption



Source: Author's calculation & graph using WB enterprise survey in 2016

Note: The correlation is significant at the 1% level after controlling for firm size, number of years in operation, experiences of top managers, industry, region, size of locality, size of last year's investment, export-orientation.

Correlation between SME sale performance and technology adoption



Source: Author's calculation & graph using WB enterprise survey in 2016

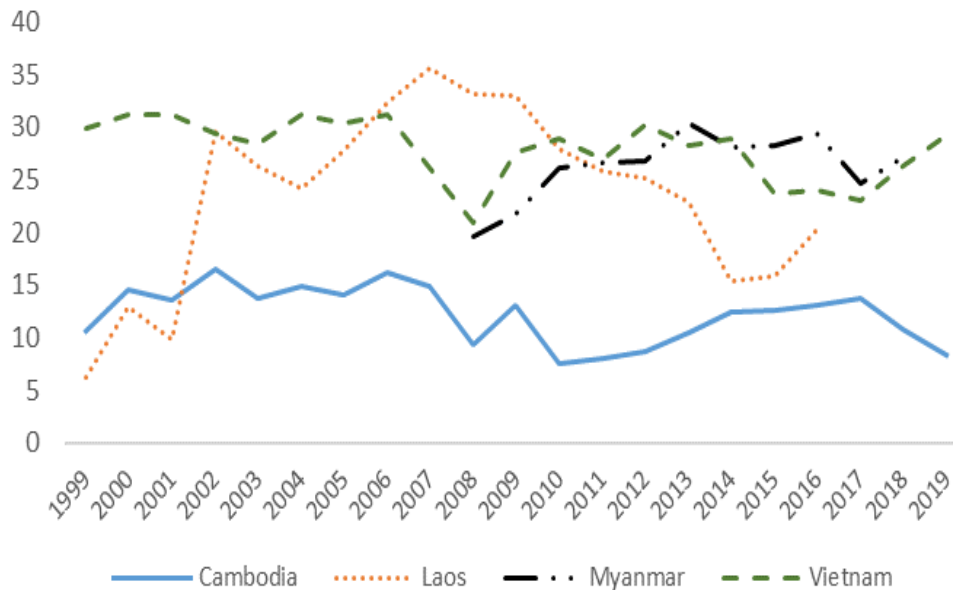
Note: The correlation is significant at the 5% level after controlling for firm size, number of years in operation, experiences of top managers, industry, region, size of locality, size of last year's investment, export-orientation.

IV- Barriers to SMEs development

v-/ National savings and riel usage

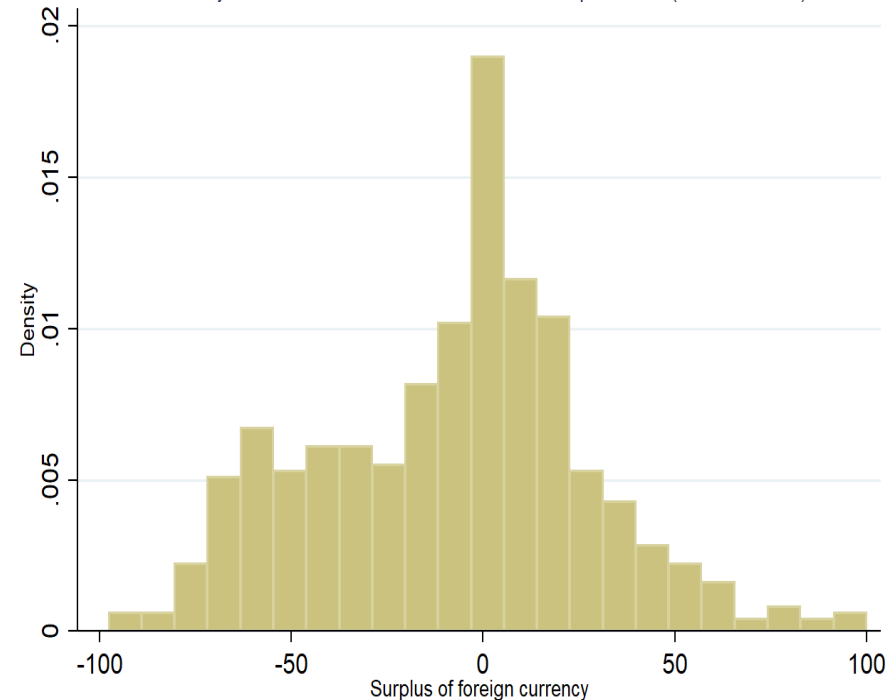
- Low saving rate in Cambodia would make it difficult to boost domestic investments.
- Reliance on foreign savings in the form of FDI is volatile.
- Dollarization exposes SMEs to foreign exchange rate risks, which may affect their incentives in borrowing to expand their business.

National Savings Ratio (% of GDP)



Source: Author's calculation & graph using WB data
Note: National saving is defined as the sum of investment rate and current account balance

Currency mismatch between SME's revenues and expenditures (% of total sales)



Source: Author's graph using NBC-JICA survey 2017

V- Conclusion

- High growth but fragile to external shocks as a result of strong reliance on external demands and with a narrow economic base.
- Fragility could be costly for a sustainable development.
- Fostering SMEs development to improve Cambodia's economic resilience: i-/ More local job creations and thus more domestic demands, ii-/ Attracting FDI in higher value-added sectors and thus more diversified economic base.
- Barriers to address: SMEs formalization, youth skills improvement, infrastructure development, facilitation of digital transformation, promotion of national savings and riel usage, among others.



Thank you for your attention!

