

**CAMBODIA, TRADE, AND ENHANCED INTEGRATED
FRAMEWORK FOR TRADE RELATED TECHNICAL
ASSISTANCE**

**A paper contributed by the
Cambodian National Strategy Team**

Acronyms

AFTA	ASEAN Free Trade Area
ASEAN	Association of South East Asian Nations
BISC	Business Information Services Counters
CDC	Council for Development of Cambodia
DTIS	Diagnostic Trade Integration Study
EIC	Economic Institute of Cambodia
EPA	Export potential Assessment
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
HDIA	Human Development Impact Assessment
ICT	Information and Communication Technology
IF	Integration Framework
IFTF	Integrated Framework Trust Fund
IMF	International Monetary Fund
ITC	International Trade Centre
JICA	Japan International Cooperation Agency
LDC	Least-Developed Country
MDG	Millennium Development Goals
MOC	Ministry of Commerce
NGO	Non-Governmental Organization
NCT	National Core Team
NSDP	National Strategic Development Plan
PRSP	Poverty Reduction Strategy Papers
TRADE	Trade Related Assistance for Development and Equity
TRIPS	Trade Related Aspects of Intellectual Property Rights
TRTA	Trade Related Technical Assistance
TSI	Trade Support Institutions
UNDP	United Nation Development Program
US	United States
WTO	World Trade Organization

INTRODUCTION: CAMBODIA, POVERTY AND INTERNATIONAL TRADE

International trade is extremely crucial for Cambodia since it has been one of the key driving forces behind much of the poverty reduction that has already occurred over the past decade. Trade is important because it has enabled Cambodia to build on the peace and stability that has been established. It will go beyond the achievement of being able to feed poor people and to develop the country. In the face of a small domestic market and other issues that as a Least Developed Country, Cambodia suffers from, the promotion of diversified exports as well as well managed imports matter. International trade contributes to the poverty eradication, but as long as poverty reduction policies embrace and integrate international trade in their operational structure, i.e. the policy directions Cambodia takes now, like those articulated in the National Strategic Development Plan (NSDP), must substantially integrate the effect on trade, showing that there is a two-way relationship between trade and poverty reduction.

This paper is organized in four sections: the first section discusses achievements and opportunities as well as challenges and possible solutions in Cambodia in terms of poverty reduction, employment generation, and international trade. The second section looks at the history of the integrated framework (IF) for trade related technical assistance (TRTA) in Cambodia, after a brief general discussion on the IF. The third section gives a brief introduction to the Enhanced IF. After giving a snapshot of the ongoing Ministry of Commerce (MOC) owned and UNDP supported project Trade Related Assistance for Development and Equity (TRADE), the fourth section discusses the interlinkages between Enhanced IF and TRADE and in an attempt to make a case for the importance of Cambodia's inclusion in the Enhanced IF from a pro-poor trade policy making and implementation. The paper ends with a short conclusion.

POVERTY REDUCTION, EMPLOYMENT GENERATION, AND INTERNATIONAL TRADE IN CAMBODIA

Achievements and Opportunities

The success that Cambodia has achieved has been a product of many conscious efforts. Peace and stability is the very basis that allows development to occur in Cambodia like elsewhere as indicated in the Regional Report. This 'peace dividend' enables people and goods to travel around the countryside, to freely go about their business. It enables transport and energy services to be developed. It means that agriculture and irrigation can be improved – **so that Cambodian poor people can feed themselves**. It has meant that the UNDP and multi-donor projects and programmes like SEILA program, for example, can now deliver over 40 million dollars each year to rural areas to provide for the priorities that the local people themselves have identified as most important.

Peace and stability means Cambodia has been able to develop two major sectors, garments, and tourism that have driven the economy over the past 10 years, both directly and indirectly (through their forward and backward linkages). These sectors have resulted in many jobs and are still growing. Both of these are export oriented sectors.

With peace and stability in place, over the past decade, enormous efforts were deployed by the Royal Government and the Ministry of Commerce, as well as their partners within the country and the international community, to boost the economic and social development of Cambodia. Please see the following for the trends in the last five years:

Table 1

Cambodia's Economic Growth (% , 2000 prices)				
	2002	2003	2004	2005e
Agriculture	-2.8%	12.0%	-2.1%	11.9%
Paddy	-7.8%	22.3%	-12.3%	30.8%

Industry and Construction	17.7%	12.3%	16.5%	11.7%
Garments	21.2%	16.9%	24.9%	17.6%
Services	4.4%	0.1%	9.2%	7.0%
Tourism	18.8%	-10.3%	23.6%	16.9%
Total GDP	5.2%	7.0%	7.7%	13.5%

Source: NIS for 2002-2004, Cambodia Economic Watch, EIC, April 2006

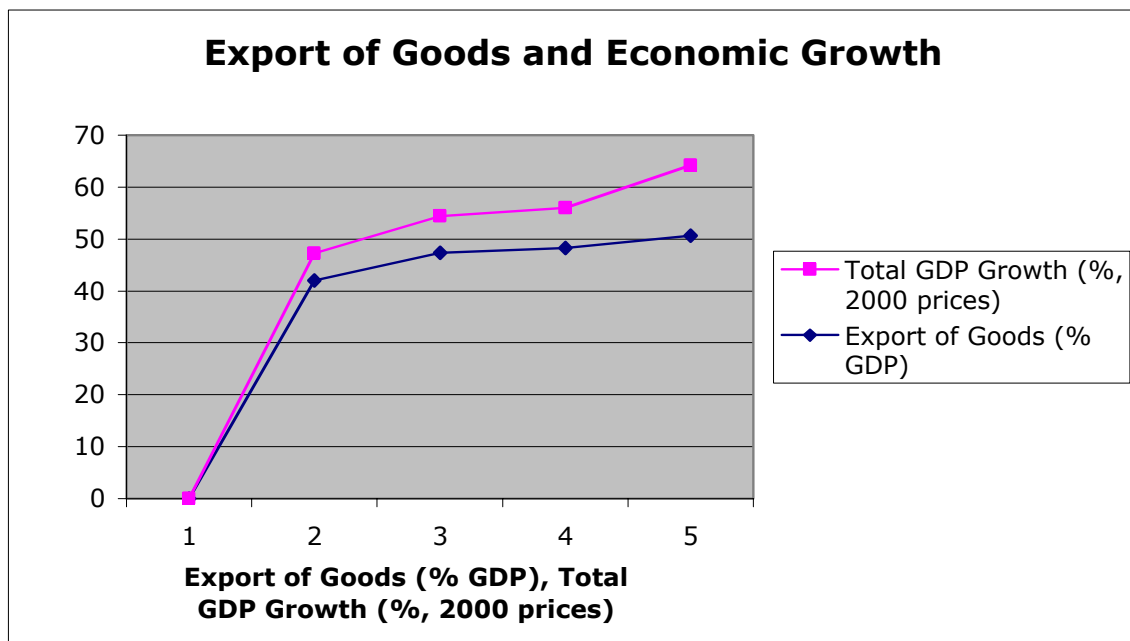
In addition to peace and stability, noticeable progress and achievements were reached in various areas:

- Policy reforms in the political, economic, financial, monetary, legal, institutional and governance domains
- Macro-economic stability
- Economic infrastructure
- Social improvements
- Global and Regional integration

The Ministry of Commerce, in particular, has undertaken several initiatives at the national and international levels in collaboration with other relevant government institutions and with wide support from key external partners, to develop the trade sector and create a conducive to legal and institutional environment for this purpose.

How Cambodia's embrace of globalization can also embrace the poor of this country. Cambodia's integration into the world economy has paralleled a strong growth rate of around 6% each year over the past decade and a rate of 13% last year (estimated). This was correlated with an increase in exports in goods: an increase from 42.1% to 50.7 as a percentage of GDP (please see the graph below). There has been a significant drop in poverty from 39% in 1993 to 28% in 2004 for comparable areas of the country, although the poverty rate for the entire country is around 35%. Cambodia's membership of the WTO and ASEAN gives hope for greater market access. The competition inspired by globalization can be a force for development and poverty reduction. Cambodia's membership to the WTO can enhance business efficiency, bring technological change, more jobs and better working conditions as well as higher incomes.

Graph 1

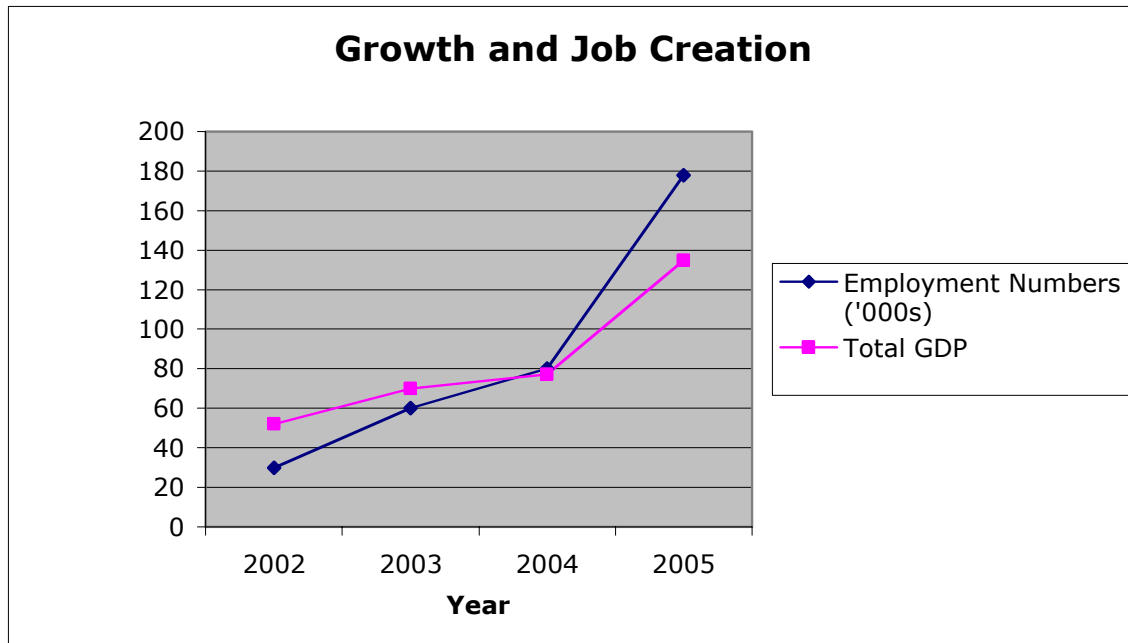


Source: Source: Tables 2.1 and, Table A1 Main Economic Indicators, Cambodia Economic Watch, EIC, April 2006

LDCs like Cambodia are vulnerable to the negative impacts of globalization due to their lower competitiveness. But while WTO accession is difficult for LDCs, there is flexibility in the transitional period to get ready for full competition. Therefore Cambodia should seek to extract most benefit from the unique position that LDCs have in the multilateral trading system. For instance, in the investment regime, or export subsidies areas Cambodia can easily put its negotiating position according to a solid development plan. Concerns on the levels of imports from China are inevitable, but ASEAN's policy to mutual reduce tariffs with China will also help stimulate the exports. Further, a deeper articulation and implementation of the suggested strategies at both domestic and international levels are essential. For example the ongoing restructuring and consolidation as well as technological upgradation in the garments sector should be closely studied and gaps and need are to be identified (as again suggested below in the context of the existing and potential export-oriented sectors) to reap the benefits of potentially high labor and capital productivity through the economies of scale. Despite its problem of one or two sector dependency in growth and exports, Cambodia has managed to avoid the phenomenon of 'jobless growth' that is widespread in the region. Tourism and the garment sector are the key export industries here. More than 300,000 workers mostly from the countryside have already directly benefited from jobs in the garments industry. In addition Cambodia managed to achieve steadily increasing labor productivity (as value added per worker), from 4.4% in 2002 to 6.6% in 2005, (Source *EIC Cambodia Economic Watch* 2006), while employment and growth are increasing in parallel in the same period.

In the new quota-free era for textiles and clothing, Cambodia has gained despite the threat of China and India. The end of the Multi-Fiber Agreement in 2004 was a great concern as garments account for about 80% of Cambodian exports. So far however, the impact has been non-existent and positive. In fact, Cambodia has increased its exports both to the US and Europe since then. One of Cambodia's advantages is the linkage of trade with labour conditions, which has enhanced Cambodia's reputation and is an example for other countries. The *better factories* concept, led by Cambodia, is gaining credibility in the international arena. China and India will be a threat in a new quota-free era, especially after 2008, but other countries in the Region can also benefit from other international market opportunities such as better labour conditions, preferential treatment, and by finding their market niche outside India and China's competitive factors.

In addition, because of Cambodia's participation in ASEAN and the WTO, as well as several bilateral deals, trade barriers and price distortion have tended to decrease for Cambodia's agricultural exports. Contrary to what is feared, this, plus the increased agricultural imports have shown little effect on food security and rural livelihoods. ASEAN food security deal has been helped by reserves to be shared among its ten members in case of need.



Source: CDC Various Economic Reports, quoted in Cambodia Economic Watch, EIC, April 2006

CHALLENGES AND POSSIBLE SOLUTIONS

It is known that poverty in rural areas is higher than in the cities and towns. This means that Cambodia must pay special policy attention to rural areas and economic sectors if it is to fully benefit from trade and investment ties and reach the Cambodia Millennium Development Goals. However, in the absence of trade and trade related development policies that would prioritize development in policy formulation integration into the world economy may generate further poverty and inequalities. Therefore (a) the pro-poor policies should be in place, (b) the impact of market access (increased imports due to trade liberalization), legal and regulatory reform, and policy space that would be limited because of the obligations that Cambodia would accept should be regularly analyzed and necessary measures should be put in place.

This further requires (a) assessment of different options for accession into the WTO, ASEAN and bilateral deals; (b) development and/or improvement of policy alternatives for pro-poor trade enhancement; (c) prioritization of policy obligations; (d) successful implementation of pro-poor trade policies; and (e) effective monitoring. The donor communities' assistance in this area, in line with the Paris Declaration is essential especially for countries like Cambodia.

The most important issue for Cambodia's competitiveness in the international arena is its supply capacity and lowering the cost of doing business in Cambodia. 80 per cent of Cambodia's population is the population is rural, linked to the subsistence agriculture. An estimated 80% of these are poor. Manufacturing employment constitutes less than nine percent of the workforce. Informal sector is extremely large rendering the tax base limited. Access to finance, trade, and investment is extremely poor. The low supply capacity and high cost of doing business in other potential areas in Cambodia partially stems from the fact that the country has a very low (lowest in East Asia) infrastructure coverage. Poor people's access to infrastructure (including financial infrastructure), as micro-financial and other types of productive infrastructure and resources and including ICT have not reached the rural areas where poor people concentrate. Because of poor infrastructure the final product quality becomes also poor (except perhaps in garments and tourism), limiting the export market access and making import competition very difficult. In order to benefit the Cambodian people in this era of expanded trade, Cambodian Government to identify, prioritize, implement, and

monitor bold policies that include investments in infrastructure, *including legal infrastructure*, higher education and research and development for competitiveness.

Poor infrastructure makes diversification of production and export base extremely difficult, since such potential sectors like light manufacturing assembly, agroindustry, packaging, outsourcing, etc. heavily depend on solid infrastructure. 80% of Cambodia's merchandise exports depend on garments almost 90% of the garments workforce are women. Cambodia's dependency on garments and tourism makes it extremely vulnerable to external shocks in the world market and climate.

While food security has not been negatively affected even after radical changes in the trade and investment policies, measures should be taken to make food security sustainable in the long term. However, 'trade barriers' especially non-tariff trade barriers are tough subject for negotiation. Cambodia, which is situated between two big agricultural exporters -Vietnam and Thailand -, is subject to trade barriers in international markets and price distortions in regional markets due to cross-border trade between these two neighboring markets.

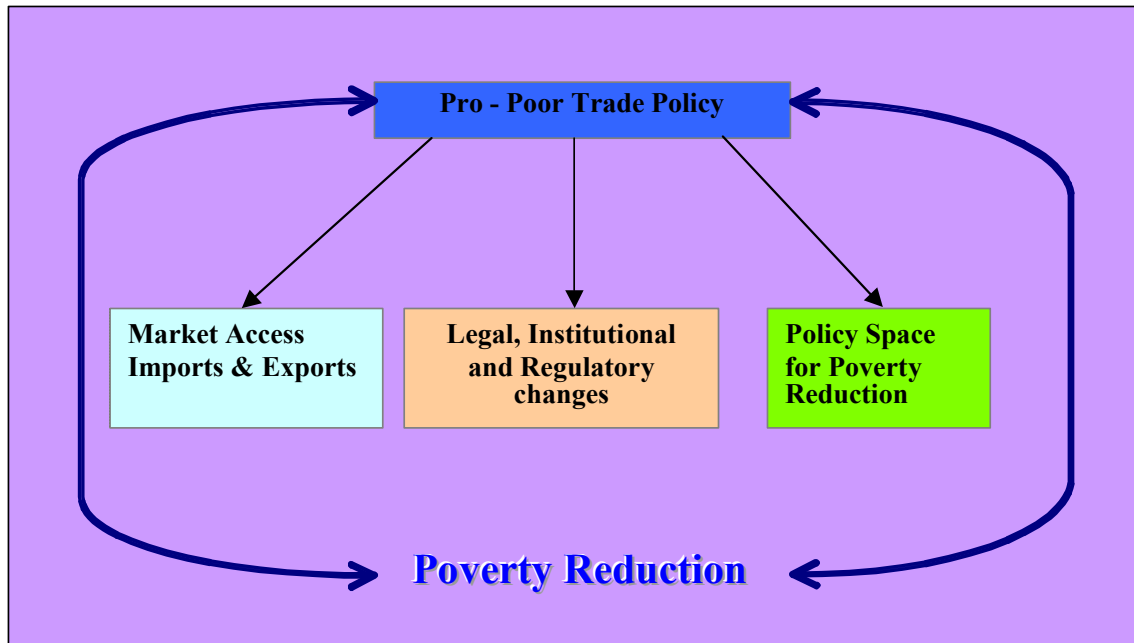
The threat to food security and one or two (low value added) product dependency in an environment like this must be countered with sustainable policies related to trade and investment that will help Cambodia move up in the value chain in its productive forces and exports. Like many countries in the Region, Cambodia has been offering not only low-cost, labour-intensive manufactures but also in the future, higher value-added, high-tech goods must be included in the export menu to climb up the value added ladder in international trade. In the garment sector, Cambodian workers have a reputation as a skilled and reasonably paid workforce. They produce up to US\$2 billion worth of garments each year for US and European markets. More than 200 foreign factories have been established. In the longer term, with the establishment of special economic zones, it is hoped that the country will attract more foreign investment – as indicated above, in the assembly of electronic goods, in spare part production, and in digital technology jobs etc.

To achieve poverty reduction in a competitive environment, a unique mix of 'trade and trade-related development measures have to be devised. For Cambodia, new sustainable jobs can be achieved through the Royal Government's Rectangular Strategy, which emphasizes the need to attract foreign investment, better infrastructure, the development of the agricultural and industrial sectors, and the mainstreaming of trade into development strategies. To identify gaps and needs of the existing export oriented sectors such as garments and tourism, and to promote and diversify exports (according to the list given above and others), the Government has already reformed trade policy and set up a fund to help Cambodian businesses meet international market standards. The new and existing initiatives such as the Integrated Framework II, the National Export Strategy, and applied the Trade Sector Development Programme have set out to identify the bottlenecks and opportunities like the determination of diversification sectors, such as outsourcing, packaging, and light manufacturing assembly. The crucial point here is that the existing as well as new sectors should (a) be geared towards employment generation, and (b) ensure that the poor people have sufficient and sustainable access to productive resources, both financial and physical. Increasing supply capacity through enhanced infrastructure, soft and hard, is the key to reap the benefits of sustainable market access opportunities.

Like in many developing countries and LDCs, trade policy shows its impact on poverty reduction through market access (both exports and imports), legal and regulatory changes and obligations, and changed policy space due to different trade policy (preferences, such as reduced tariffs affecting the fiscal position of countries, etc.), the transmission mechanism should be well understood for every country as a new WTO member, especially for Cambodia. For this purpose the following flow chart might be instructional. In the first instance the trade related development policies such as industrial, services, and agriculture, should be well formulated for short, medium and long term. Mechanisms to flourish existing sectors and potential sectors for identification should be identified. In the meantime, human development impact should be assessed. In addition capacity building for trade development in both government and the private sector should be devised. Whilst Cambodia has been successful in this new era, Cambodia must find the best possible way to ensure progress is

sustained. One-size-fits-all types of policies are not suitable, especially for Least Developed Countries, like Cambodia that are trying to integrate into the world economy with a narrow export base.

Chart 1



Source: Mumtaz Keklik, *Human Development Impact Assessment of Trade Policies*, Regional Center in Colombo Publications, April 2005

INTEGRATED FRAMEWORK FOR TRADE RELATED TECHNICAL ASSISTANCE

Integrated Framework for trade-related technical assistance-Phase 1 - pre-WTO Accession

Before going into history of the IF Cambodia in Cambodia, it should be noted that the main goal of the IF is to enhance LDC trade capacity to integrate into the multilateral trading system in order to reduce poverty. The mandate of the IF is threefold:

- to mainstream trade into LDCs' national development plans such as Poverty Reduction Strategy Papers (PRSPs);
- to assist in the coordinated delivery of trade-related technical assistance in response to needs identified by LDCs;
- to develop the capacity of LDCs to trade, including through capacity building and addressing supply constraints.

Cambodia has completed the first phase of the Integrated Framework with the production and national validation of the Diagnostic Trade Integration Study (DTIS) in 2001 and launched it in early 2002. This was achieved with the overall leadership of the Government, especially the Ministry of Commerce. It was the product of and followed by a very successful set of many consultations with all stakeholders. The technical input & content was produced under the leadership of the World Bank, with other agencies and donors contributing substantially to this effort.

UNDP led the process of agency & donor coordination (with JICA was the lead donor facilitator), harmonization, and alignment, as well as provided substantive inputs and funding

both from UNDP's own resources and the IF Trust Fund (total approx 538.000USD) through the *Capacity Building for pro-poor Trade reforms -IF Phase I - WTO accession* project.

The first phase was quite successful in terms of both process and product. In addition to the production of a highly influential DTIS and its TRTA Action Matrix, the process included the establishment of IF institutional bodies, consultations with stakeholders and donor coordination and generated not only a coordinated platform for action but also great interest and support in trade related issues in the country by the private sector, NGOs, academia, other ministries and the donor community at large.

Enhanced IF – Post WTO accession

A short background:

Scaling up aid for trade is important as indicated in the Millennium Project Report; UN SG Report for September Summit. Increased aid for trade is especially crucial for countries like Cambodia, where official aid is declining. Linked to the Doha Development Round and the achievement of MDGs (especially Goal 8), scaling up aid for trade includes an 'enhanced IF, including expanding its resources and scope and making it more effective.' This is something discussed and decided by the September 25 World Bank-IMF Development Committee Communique. This may mean that the IFTF could plausibly increase from current \$30 million to \$400 million over the next few years resulting in a current one-time support of \$1 million per country for Window II to \$3 million per country for all 50 LDCs.

Most Recent Developments

Against this backdrop, a Task Force on enhanced IF was established and convened on 2 May 2006. The Task Force endorsed the mission of the IF. As the background and the decisions taken provide fundamental improvement in the concept and philosophy, it would be much more useful to present some of the key parts of the Chairman's Report to as a direct quotation in the following (italic and bold are added):

The point of departure for the substantive discussions of the Task Force was the Hong Kong Ministerial Declaration, which reaffirmed the commitment "to effectively and meaningfully integrate LDCs into the multilateral trading system," noted that the Ministers attached "high priority to the effective implementation of the Integrated Framework" and recognised the "urgent need to make the IF more effective and timely" Ministers required the Task Force to report back to the IF Steering Committee by 30 April 2006 so that an enhanced IF could be launched by 31 December 2006. It was agreed that the enhanced IF should comprise three specific elements:

- 1. Increased, additional, predictable financial resources to implement Action Matrices;*
- 2. Strengthened in-country capacities to manage, implement and monitor the IF process; and*
- 3. Enhanced IF governance.*

The Task Force recognized the importance of trade liberalization and the fact that such liberalization should lead to improved economic conditions in the LDCs and assist in meeting the Millennium Development Goal of reducing poverty by half. However there was also a recognition that trade liberalization in itself would not bring about such improvements unless it was handled in a sustainable manner and integrated into a country's overall development strategy.

The Paris Declaration on aid effectiveness was seen as very important in this process, and our recommendations draw on these principles.

The Main Conclusions of the Task Force

The Task Force recognized that the IF has had positive results in a number of LDCs and that it was important to capture and build on the strengths of the existing arrangements to improve its effectiveness and efficiency. The Task Force identified four critical issues:

- There needs to be much stronger ownership of the IF by the LDCs and the donors. In part this is a capacity problem. Capacity needs to be developed and strengthened in the LDCs to facilitate greater ownership. Similarly, donors need to give much greater prominence to these issues and to provide more resources.*
- There is a gap that needs to be filled between the diagnostic and submission of "bankable projects". In addition, the diagnostic work of the IF needs to be more dynamic, with the DTISs and Action Matrices being updated on a regular basis.*
- Responsibility for management and implementation must be more focussed. Currently it is spread wide and thin. Everyone, yet no one is responsible. There needs to be a much clearer management and governance structure.*
- There is a need for adequate funding, provided in a predictable manner, to meet the objectives of the IF.*

(SOURCE: AN ENHANCED INTEGRATED FRAMEWORK

'Report of the Chairman of the Task Force on an Enhanced Integrated Framework, Including Recommendations,' Communiqué, WTO, 29 June 2006)

ENHANCED IF AND CAMBODIA – POST WTO ACCESSION

Integrated Framework for trade-related technical assistance-Phase 2

Cambodia was the first IF country to finish the DTIS and the first phase of the IF and move to the second phase. The second phase started with the selection of different recommendations to be operationalized by variety of donors. For example, the World Bank embarked a large project on Trade Facilitation, an area which has been emphasized by the DTIS as a priority area to be enhanced in Cambodia. The Bank's Trade Facilitation Project that is being implemented jointly by the Bank and the Ministry of Commerce has a budget of about \$11 million. The other example is the ITC's proposal on the silk and agrobusiness. In 2003, the UNDP and the Ministry of Commerce, designed a project called Trade Related Assistance for Development and Equity (TRADE)-IFII as part of the second phase of the IF. The TRADE Project was designed after a series of very stakeholder extensive consultations and included ITC as one of the main partners in one of its four components.

With its full and efficient implementation of both Phases 1 and 2 IF for TRTA provides the best trade policy making methodology for poverty reduction.

As indicated above, the Enhanced IF Task Force reported that in many cases the first phase (Cambodia being the best one, as it was repeatedly emphasized in the discussions, according to informal communications with the UNDP representation in the Enhanced IF activities) was very successful in coming up with recommendations and needed projects through the TRTA Action Matrix. However, the recommendations coming out of the DTIS was not fully and in many cases even partially implemented. The best case example is, again, Cambodia. Main reasons for this 'failure' in the second phase is twofold: there was not sufficient coordination among donors towards implementation, and financial sources to follow up for implementation

and ensure sustainability was not there. Therefore the implementation of the recommendations that are coming from the Task Force is crucial for pro-poor trade policy making, but sufficient financial resources should be provided by the IF agencies and donors. Enhanced IF is designed to achieve this end result.

Enhanced IF and Trade Related Assistance for Development and Equity (TRADE)

The TRADE Project (end 2004-2008) is owned and implemented by the Ministry of Commerce and supported by UNDP. Tapping into Enhanced IF resources is important for ensuring that great majority of pro-poor policies are implemented and there is a buy in from the economic policy makers on the importance of trade being an integral part of poverty reduction. However, it is also important to guarantee that these vital changes and transformations in the area of trade as a cross-cutting area do take place. This second point is extremely important in Cambodia where as of 2005 50% of GDP comes from goods exports.

In line with the spirit of the Enhanced IF, the TRADE-IFII project pursues four priority objectives: (i) Assess the trade-related technical assistance gaps that will provide a common and coordinated action platform addressing the human development needs of Cambodia through regularly updating the Diagnostic Trade Integration Study (DTIS) and its Trade Related Technical Assistance Matrix (TRTA); (ii) Enhance national capacity in pro-poor trade policy formulation and implementation including cross-sectoral and decentralized capacity; (iii) Conduct and institutionalize a Human Development Impact Assessment (HDIA) of Cambodia's integration into the world economy through qualitative and quantitative methods, in a participatory approach with a view to establishing national trade policy and private sector development strategies that place poverty eradication at center; and (iv) Building on Cambodia's increased international trade integration, enhance the country's supply and marketing capacity in selected export potential sectors with employment generation and poverty reduction potential (such as those indicated in the first section); create an enabling environment to facilitate Cambodia's access to the Aid for Trade personified by the Enhanced IF, as it gets established. The Project is building on the achievements of Phase I and the conclusions of the IF National Trade Event on Trade and Poverty held in October 2003 in Phnom Penh.

According to its priority objectives the TRADE Project has the following four Components (summary titles):

1. The Regular Updating of the DTIS and its TRTA Matrix;
2. Capacity Building on the linkages between Trade and Human Development;
3. Human Development Impact Assessment (HDIA) of Cambodia's Integration into the World Economy through, among others, her Accession to the WTO;
4. Identification and Needs Assessment of Employment Generating Export Oriented Sectors;
5. Enhancement of regulatory environment to be more conducive for the startup and development of Micro and SMEs.

It should be noted that despite the fact that the Project was formulated quite a bit before the idea of Enhanced IF was put on the table as a modality for aid for trade, the TRADE Project was inspired by the three 'lessons learned' indicated under the rubric of 'recommended specific elements' in the direct quotation above. Further, all of the components correspond to the main recommendations (or as it is entitled critical issues) of the Enhanced IF Task Force. This will be discussed further, but now let's turn to the details of the four components. It should be noted and strongly emphasized that the four components of the project are interlinked and designed around a participatory trade policy development strategy. Extensive consultations and participatory process with several stakeholders, including other sectoral ministries, the private sector, the donor community, and civil society organizations are part and parcel of UNDP's activities in this area.

Component 1: The Regular Updating of the DTIS and its TRTA Matrix:

As explained above the first DTIS is considered as a great success in terms of process --- especially its inclusiveness---, methodology, and product. However, the issue date of the document is January 2002. In the meantime, Cambodia has gone through a relatively fast transformation. The high growth and investment rates, the country's accession to the WTO, and the legal and regulatory reforms that have been undertaken are just a few achievements that the country has shown.

In addition, there is a need to pay sufficient attention to the key aspects of trade and human development using the DTIS and TRTA Action Matrix methodology: its attention to poverty and inequalities should be central, the fact that Cambodia has acceded to the WTO needs to figure prominently, rendering some of the analyses not-so-useful, updated DTIS(s) should pay sufficient attention to the sectoral issues, according to the vision indicated in Component 4 below.

As indicated above, the methodology and process were appreciated very much by the major stakeholders, mainly the Government, and many useful aspects has been utilized from by the Government and other stakeholders Therefore, in the TRADE Project, it would be most appropriate to use the same methodology and process to influence the policy discourse (or permanently transform it) towards a more human development oriented policy making and outcomes.

The updated DTIS and its TRTA already aim to provide:

- Trade sector assessment to identify gaps and needs;
- A tool for the Government to prioritize required actions;
- A coordination platform for donor support and dialogue with the government;
- A system of monitoring, regular updating and eventual course redirection, and
- A set of recommendations for policy alternatives.

For this purpose, this first component attempts at putting in place mechanisms that will allow the Royal Government to regularly (once a year) update the DTIS and its TRTA Action Matrix. The first step has been taken and, following an extensive series of consultations, the first update of the DTIS will take place in the coming months. The table of contents of the updated DTIS, including both cross-sectoral and sectoral issues, has been prepared, writing team has been put together, both individual and common consultations with different stakeholders have taken place, and the DTIS team aims at completing the first draft for national validation around end November. The drafting process has been extremely consultative and collaborative with all of the stakeholders.

Component 2: Capacity Building on the linkages between Trade and Human Development:

The main purpose of this component is to identify the necessary capacity gaps that exist in the Ministry of Commerce (MOC) and four or five other Ministries (Ministry of Women's Affairs, Ministry of Agriculture, Ministry of Rural Development, Ministry of Industry and Mining, and Council for Development of Cambodia (CDC)). The basic idea behind it is to enhance the human development and poverty reduction oriented trade policy making within the Royal Government of Cambodia (RGC). The first step towards this goal is to set up (or revitalize) an 'IF Core Group' with the participation of qualified individuals from other relevant Ministries. The IF Core Group will be a part of the MOC structure. Members of the Group will be all Cambodian Nationals. The Core Group ---currently only three recruited from the Ministry of Commerce--- members will receive training in the first instance. During and following their training period, they will also work for the implementation of the several components of the TRADE Project. They will also be active in bringing the main findings and recommendations on board in their respective Ministries and Departments.

In time the IF Core Group will be the main body to conduct the regular updates of the DTIS, as well as Impact Assessments and sectoral work.

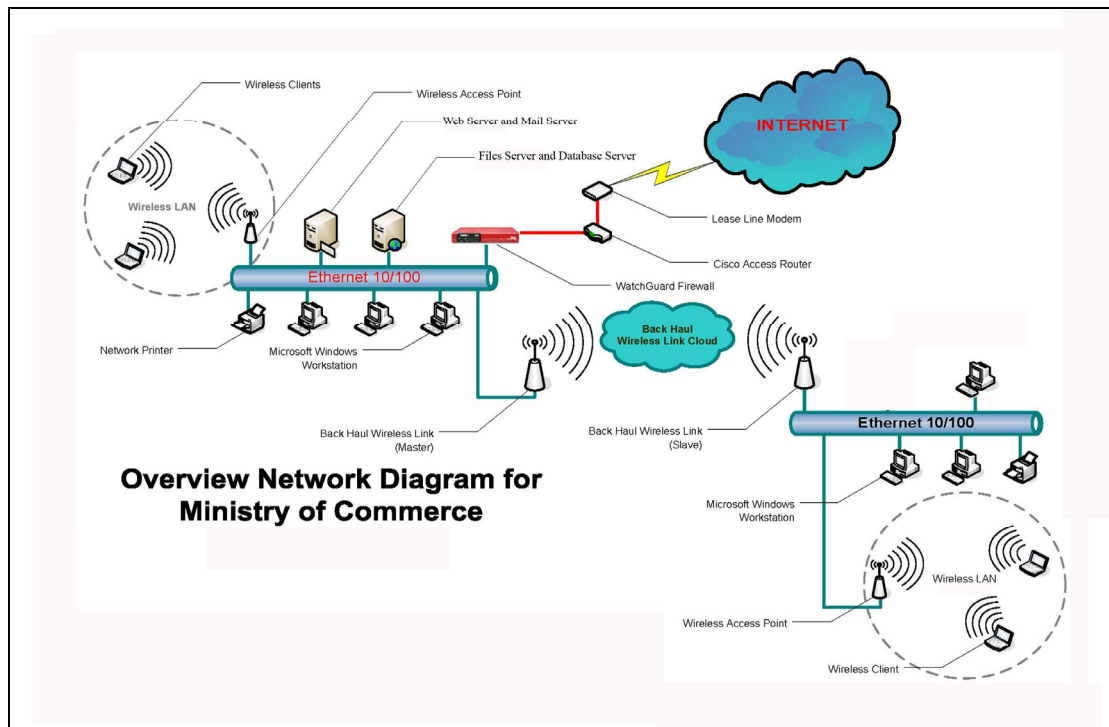
As indicated, one of the most important investments for increased competitiveness and enhanced market access is the Information and Communication Technology (ICT). This will guarantee enhanced access to 'unknown' markets (for example those in the South, which could be less 'demanding' in terms of standards) by providing (real) timely information on price, quantity demanded, product quality etc. It would also greatly improve the inter-ministerial information sharing and transparency in Cambodia, as trade is a multi-sectoral area.

Cambodia, though there is a national ICT strategy being developed, is in dire needs capacity building and development in the area of international trade. One of the most significant aspects of Enhanced IF will and should be to establish both intra and inter electronic connectivity infrastructure and, as such, decrease the red-tape and increase efficiency in both domestic and international trade. In the absence of an 'e-Governance' with a solid ICT strategy coordination among key ministries and entities in the country renders international and domestic trade inefficient to say the least.

International trade is all about information. In addition to the coordination aspect (which is in between two general approaches: National Capacity and Global Positioning), closely following, collecting, storing, analyzing, and conveying trade related information to traders requires as it was the case in countries like Malaysia and Estonia, among others a solid ICT base. As indicated in the *Digital Opportunity Initiative Final Report* "...concentration on the deployment of ICT to improve global positioning allows countries to use ICT to make the overall investment climate more attractive and to facilitate increased competitiveness in sectors and products in which the country may already have, or can create, a competitive advantage. Malaysia and Singapore have deployed ICT-enabled strategies to increase their global and regional positioning. They have seen dramatic increases in foreign investment (and most likely in trade as a result of adopting this strategy <http://www.opt-init.org/framework/pages/2.3.3.html>). Establishing and improving ICT infrastructure in a country with such a young and vibrant population would guarantee both national capacity and global positioning aspects.

For Cambodia, the starting point is very basic (perhaps in the following order): hardware and software infrastructure in the Ministry of Commerce, following and building on other country initiatives such as Singapore or Pakistan making information collection and storage functional and efficient, generating (starting with the MOC) as best practice in Cambodia to be used by other relevant Ministries, private sector, think tanks, and most importantly by the traders. This would be the first set of measures that could be taken. In the second instance, a portal that would be managed by the MOC and updated daily by MOC and other focal points would access, collect, store, and distribute statistics and information about products, demand, price, location, timing etc., to the traders. The development process of this ICT infrastructure is envisaged to be scalable and sustainable on resources and skills.

On the basis of the above synopsis, the TRADE Project team is in the process of generating a proposal to the international community.



Component 3: Human Development Impact Assessment (HDIA) of Cambodia's Integration into the World Economy through, among others, her Accession to the WTO

Cambodia has formally acceded to the WTO on 13 October 2004. While this was a success for an LDC, it also brought the Country in a path where she needs to liberalize its foreign trade at a pace which may be too fast for an LDC like Cambodia. In addition, the conditions under which the Country entered into the WTO may not allow Cambodians to reap the potential benefits that the Accession could bring. For example they have bound the tariff rates at a quite lower level than they could have (final bound is 19 percent for all goods, while the applied rate is 16.4 percent). Also they have eliminated the export subsidies, which is not a necessary move for an LDC under the WTO. Further, while they have promised to put in place policy mechanisms such as duty drawbacks, so far there is no indication of such mechanisms. Cambodia is also criticized for having a 'TRIPS Plus' deal out of its Accession to the WTO. Finally, potentially beneficial WTO agreements are being implemented at a slower rate than expected, as regulatory and legal mechanisms are not yet in place.

The basic idea behind this is to conduct a Human Development Impact Assessment (HDIA) of Cambodia's Accession to the WTO (in the first instance, to be expanded to AFTA and bilateral deals) and come up with policy alternatives that could be used to enhance opportunities and mitigate potential challenges. It is also important to note that such participatory and post-assessment trade policy making should be institutionalized in the policy making mechanism.

The vision of the specific HDIA methodology is that changes in trade policy is shows its impact through three main mechanisms: Market access (agriculture, industry NAMA, and services agreements), Legal, Institutional and Regulatory Changes (financial services, intellectual property rights, public services), and Policy Space (fiscal impact, industrial policy). In all three areas, a comprehensive and participatory Impact Assessment will be conducted using qualitative and quantitative impact assessment methods. The analysis will look at the impact on critical human development variables, such as gender equality, poverty reduction, environmental integrity, etc. The analysis will come up with policy alternatives, and it will be regularly repeated once the institutional capacity is in place (i.e. the IF Core Group is established and mainstreamed into the system as a permanent body).

Component 4: Identification and Needs Assessment of Employment Generating Export Oriented Sectors

As well known, Cambodia has a very high dependency on the garments sector in its foreign exchange income out of exports. Total garments exports in value terms accounts for around 80 per cent of the total exports and contributes to 17 per cent of the country's GDP. This is a very alarming situation, especially given the fact that the outcome of the end of the Agreement on Textiles and Clothing may not produce favorable outcomes for the sector, especially after the full quota elimination by the big player China, in 2008.

The export diversification and increasing the value added in the existing export sectors are crucial for Cambodia. There is an existing National Export Strategies document, which is somewhat welcomed by the Government, as well as other work in the area, but all of them have been coming up with focusing the usual exportable goods and services.

The basic idea behind this component is to identify the sectors and their needs, that are (a) existing export sectors, but there is a lot of room for improvement in their value added generation (such as garments and silk etc.); and (b) currently not export sectors, but there is a great potential identified using different methods (like the Export potential Assessment, EPA, which was implemented in Vietnam and Laos and able to make some useful recommendations affecting the Governments' sectoral priorities). The major building block of the methodology of identification and needs assessment is the potential that the sector shows in generating sustainable levels of employment.

So far, the project team and consultants have identified and worked on Silk Sector with ITC. Other potential sectors include agrobusiness and packaging. This component will heavily depend on the outcomes of the initial updating of the DTIS (first component), especially the Chapter Five on the Export Potential Assessment.

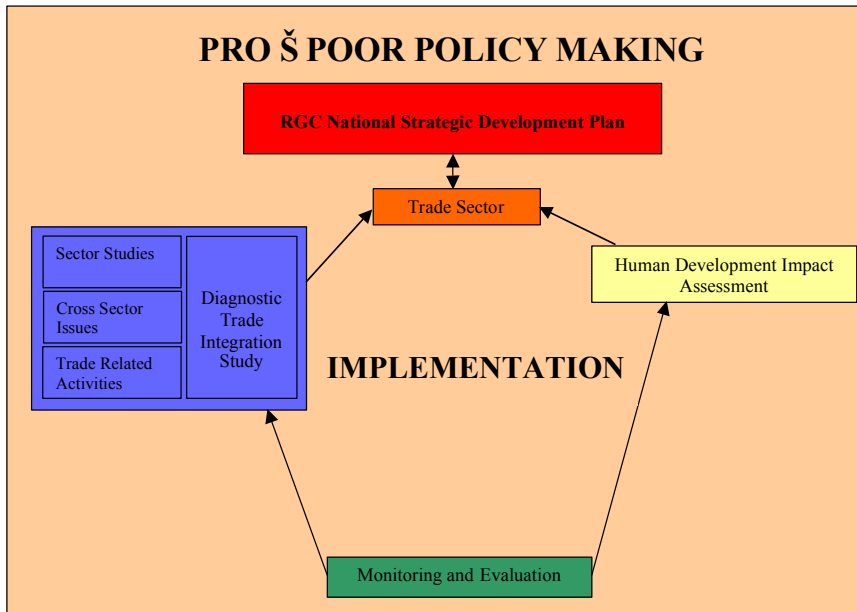
In later stages, the project will take out one or more sector(s), analyze its value chain, and contribute to one or more of the components of the value chain, as an on the ground pilot application.

Component 5: Enhancement of regulatory environment to be more conducive for the startup and development of Micro and SMEs.

As a LDC, Cambodia acceded to WTO without being in full compliance with the WTO rules in a number of areas. In order to fulfil these commitments; Cambodia has embarked on updating and drafting regulatory frameworks to be conducive for the development of Micro and SMEs and international investment. There are three major activities for this components:

1. National Action Plan developed for Commercial Dispute Resolution laws implementation
 - Design and conduct a legal and regulatory review of existing commercial dispute resolution laws; i.e. arbitration, mediation and conciliation, including implementation (decrees) recommendations formulation;
 - Draft and finalize the National Action Plan, including resource mobilization strategy;
 - Facilitate national consultations to include government representatives, private sector, civil society and donors;
2. Enhanced capacity of the commercial court to carry out its mandate
 - Finalize the Commercial Court law draft; develop the implementation decrees for implementation and dissemination of the law;
 - Develop a Commercial Court Technical Assistance mobilization plan to support the establishment of the commercial court;
 - Develop curriculum and conduct training for judges and relevant parties of the court;
3. Business Information Services Counters (BISC) model promoted and implemented
 - Conduct needs assessment, stock taking of available business information, and analysis of existing business information delivery systems
 - Collect and develop information contents well tailored for dissemination;
 - Design and conduct a training on communication and marketing for MFI branches;

Chart 2



Source: Modified from HE Sr. Minister Cham Prasidh's Presentation on 'Pooling Resources Towards Capacity Building Cambodia's Supply Capacity Through a Trade Sectorwide Approach' Presented at the Meeting with Stakeholders on SWAp Trade Sectorwide Approach, Ministry of Commerce, June 22, 2006, Phnom Penh, Cambodia. Enhanced IF and Cambodia TRADE-IFII

As indicated above, it should be emphasized that both the TRADE-IFII project and the Enhanced IF share the same vision and spirit: The basic idea of these activities is to strengthen and help institutionalize poverty reduction-oriented trade policy making over the long term; but at the same time integrate pro-poor trade policy in the NSDP in a fundamental and sustainable way. As it is demonstrated in the in the Chart 2 above, the main mechanism for this is, in strong collaboration with donors and stakeholders, the support to the mainstreaming of such pro-poor trade policies in the National Strategic Development Plan (NSDP) by using DTIS and HDIA as the 'substances' of the pro-poor trade policy making. This flow chart also conveys the HE Sr. Minister's vision. It should also be noted that sustainability of this mechanism requires international support both financial and substantive. For instance in the area of ICT

More specifically:

Firstly in many fora, documents, and discussions at country, regional, and global levels it is agreed that there is a need for both phases of the IF should focus on poverty eradication and human development, trade should not be seen as means to an end not an end itself, and there is a two-way relationship between enhanced trade and human development (please see Annex 2 for a synopsis of the conceptual linkages between the two).

Secondly, the Enhanced IF emphasizes the importance of capacity building for enhanced trade for poverty eradication starting within the Government, but expanding it to the private sector, civil society, and academia. The second component of the Cambodia Project aims at doing exactly that. The Project goes beyond the human resource capacity enhancement and strongly emphasizes the importance of the enhanced ICT, which will be a permanent infrastructural mechanism that would raise Cambodia's profile in the international fora.

Thirdly, as both poverty and trade and trade related measures are extremely dynamic, the DTIS must be regularly updated with the support of a comprehensive and participatory human

development impact assessment and naturally through ICT. It further emphasizes better coordination among donors as well as inviting them to increase their financial and in kind contributions. This is explicitly mentioned and strongly emphasized under the 'critical issues' of the report of the Task Force. The overall approach like the TRADE-IFII Project refers actually the Paris Declaration for enhanced aid effectiveness. The first component of the TRADE-IFII Project aims to make updating of the DTIS and TRTA Action Matrix institutionalized. The Project also aims at enhancing coordination, harmonization, alignment and management for results, through, *inter alia*, DTIS updating mechanism.

Last but not least discussions in different fora have been taking place in the area of emphasizing sectoral development; so far DTISs have been mostly emphasizing 'trade liberalization' or more concretely import liberalization and how to get 'there,' but now the discussion is moving towards how to enhance supply capacity of the country for enhanced export capacity. Under certain circumstances (like well managed and sequenced trade policies) and with the support of 'trade-related development policies,' which requires the involvement of other Ministries and groups and a strong collaboration among donors and other stakeholders. As will be more explicit below, sectoral work that is being undertaken within the Cambodia Project is geared specifically to enhancing exports but at the same time ensuring the poor people's increased quality employment and access to productive resources (through strategically increased intermediate goods imports).

CONCLUSION

Cambodia continues to face many challenges as a result of the integration that globalization and increased international integration brings. Development of international trade for the benefit of human development requires coordinated and strategic partnerships with the donor community, private sector, civil society organizations, academia, and think tanks with a solid and proven methodology like the IF and Enhanced IF. Cambodia is way ahead of the game in terms of having fulfilled the recommendations of the Enhanced IF. In addition it has a very vibrant and willing trade community. Success in international trade development strongly depends, among other things, also a coordinated and wide range of interested (both national and international) parties as well as visionary leadership such as the MOC of Cambodia and mechanisms, such as the Enhanced IF. All of these strongly exist in Cambodia.

Cambodia has already made important gains from the opportunities that have been presented. But she needs to keep focused on what is the key benefit of this trade and investment: Cambodia needs to ensure trade is for human development. The measures should be understood and implemented with an '**out of the box**' mentality which helped today's developed countries develop with a set of 'trade and trade related development policies' (including industrial, macro, and social), unique to each of them.

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ANNEX 1

A Snapshot of the IF

Integrated Framework (IF) for Trade Related Technical Assistance (TRTA) is an initiative by six IF agencies. The IF aims at mainstreaming trade policies in poverty reduction strategies in LDCs. The initiative is implemented in two phases in the IF countries. The first phase involves putting in place institutional bodies in the government (most of the time Ministries of Commerce) such as the IF Core Group and the IF Secretariat (an interministerial and relatively high level committee). A bilateral donor is identified as the Lead Donor Facilitator in this phase.

The main product of the first phase is a Diagnostic Trade Integration Study (DTIS). A team called 'the DTIS team' of international and national consultants is put together to do analytical work in the areas of trade and trade policy, poverty reduction, existing institutional set up, and required actions. The DTIS team is lead by an international expert. Following its Executive Summary and Introduction, the DTIS has three critical sections. These are the Part B on Cross-Sectoral Issues, Part C on Sectoral Issues, and TRTA Action Matrix. The contents of Parts B and C are quite obvious by their names. The third section (TRTA Action Matrix) lays out possible areas of donor support, which are identified by the DTIS team in close collaboration with the government bodies mentioned above. The first phase involves all of the six IF agencies in their different capacities, and the substantive work is always led by the World Bank (in close collaboration with the government). The exception is made when the Bank doesn't have the institutional capacity in a given IF country. In those (limited number of) cases, UNDP takes over the substantive work as well as coordination responsibilities. UNDP's main role in the first phase is donor coordination, channeling (managing) the funds allocated for the first phase, and some substantive input (along with other IF agencies) to the production of the DTIS.

After the completion of the DTIS and its National Validation, the second phase starts. The second phase involves mainly the implementation of the recommendations coming from the DTIS and especially its TRTA Action Matrix. These recommendations are converted into projects by interested donors and implemented. The advocacy, coordination, and harmonization role is given to the IF Facilitator. UNDP's main responsibility in this second phase is to contribute to this effort. The implementation of the Action Matrix-recommended projects takes place in several ways. One main way is where donors and agencies with sufficient funding bring their own projects and implement them according to their rules, regulations and procedures. Another one is to tap into the IF Trust Fund sources, which are between US\$ 500 thousand and 1 million. In the latter case, while the project is designed, approved, and implemented according to UNDP rules and procedures, other interested agencies and donors are invited, in fact, strongly encouraged to contribute financially or otherwise. In most cases, specific UNDP CO also contributes from its own budget and resources. Other than donor coordination and (both substantive and financial) management of the Trust Fund resources, UNDP is also tasked to be active in capacity building activities, especially in its niche area of identifying and operationalizing the relationship between trade and poverty reduction.

ANNEX 2

International Trade and Human Development I: When does trade help?

Determining the dynamics of the relationship between international trade and human development is not an easy task. As the UNDP sponsored book on *Making Global Trade Work for People* suggests, theories of international trade have not been able to explain the relationship to a satisfactory extent.

While a full understanding of the dynamics require further research, it is a stylized fact that there are at least two aspects to the relationship between trade and human development:

- (1) Trade policies do affect human development outcomes and components;
- (2) Enhanced human development is instrumental in achieving sustainable and high trade performance.

These two aspects are in fact difficult to separate, but for analytical reasons this piece focuses on the first one. There are diverse views as to how and under which economic policy circumstances trade policy works to enhance human development. The conventional wisdom suggests that the impact of liberalized trade on economic growth and (then) human development is *automatic* and *guaranteed*. Static welfare gains (by improving allocative efficiency, increasing capacity utilization, expanding product variety and so on) and dynamic welfare gains (through greater economies of scale, improving growth potential and so on) from *more* trade (both exports and imports) will almost certainly be achieved through a greater degree of trade liberalization.

This view has been challenged by recent research from the members of both neoclassical and non-neoclassical groups of economists. Rodrik and Rodriguez (2000) from the former group argue, for instance, that the argument that greater degree of liberalized trade automatically yields higher rates of economic growth is empirically invalid. They demonstrate that the only systematic relationship between countries' average tariff and non-tariff restrictions and their growth performance is that countries dismantle trade restrictions, as they get richer. Other factors such as the macroeconomic policies, institutional set-up, regulatory framework, and good governance are critical in determining the growth performance in developing countries.

More recently, looking at the trade and investment (FDI) policies of a group of Latin American countries in relation to their growth performance over the last three decades, John Weeks has argued that the relationship between trade and GDP growth depends on the dynamics of the transmission mechanisms and complementarity (or lack thereof) between export and non-export sectors in the domestic economy. GDP growth can only be enhanced if the export sector can generate positive growth dynamism in the non-export sector (Weeks 2003). In its empirical investigation the paper shows that this complementarity has been greater in countries where the transmission mechanism was facilitated by expansionary macroeconomic policies (monetary and fiscal policies as well as exchange rate regime) and where there are solid industrial policy measures in place. A contractionary macroeconomic policy framework -- using restrictive monetary and fiscal policies for instance-- will be likely to negatively influence "export dynamism", measured by the elasticity of real exports and non-export GDP, by compressing (especially domestic) demand. This reduces the stimulating effect of exports on non-export production and thus on GDP growth (Weeks 2003). The linkage operates through the crowding in and income effects of government expenditures. Moreover, according to Taylor (2001) using real exchange rate appreciation to spur export growth may cause declining terms of trade for agriculture, reducing rural rents and hurting both landowners and agricultural workers, ultimately weakening food security.

Effective social policy and a fair and equitable governance structure, prioritizing spending on education and health as well as investment in basic infrastructure, which heavily depend on

expansionary macroeconomic policy, are also important for positive and sustainable human development outcomes as well as increased trade performance (the latter will be taken up next time). Expansionary macroeconomic policies require substantial financing. In most developing countries and in almost all LDCs, however, upto 40% of government revenues originate from customs duties, and the relationship between tariff revenues and tariff rates is still positive (Rao 1999). Tariff restrictions and other types of trade liberalization policies are, therefore, more than likely to put an additional financial burden on the government budget, limiting their ability to conduct meaningful social and economic policies, which would otherwise benefit trade, further growth, and human development.

This is not to say that trade is bad for human development. Liberalized trade *can* produce positive results through the efficiency gains talked about above if the policy is skillfully managed (including the export and import compositions) and sequenced, and put in the context of overall development policy specific to each country case. The importance of conscientious policy making and treating international trade policy as part of a consistent development strategy, rather than as a 'magic stick' for human development cannot be overstated and seems to have been growing obvious to many lately. Trade policy advice to developing country governments should therefore be carefully formulated in the context of overall development strategy, which requires close linkages with other components of economic and social policy making.

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