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Provincial Business Environment Scorecard (PBES)¹

Over the past decade Cambodia's economic performance has been strong, with an average annual growth rate of 7.1%.² This has helped ease poverty, reducing the poverty rate from 47% of the population in 1994 to 35% in 2004.³ The growth, however, has been narrowly based on a few sectors and geographically concentrated in urban areas. As a result, reduction in poverty has been unevenly distributed.⁴

Economic growth needs to be broad-based to ensure that its benefits are felt by all. Since business activity drives growth, having a business environment that is conducive to private sector development throughout the country (not just in the main urban areas) is needed to generate growth, increase the demand for labor and help reduce poverty. Thus, it is important for government officials at provincial and municipal levels to have a good understanding of the business environment, as most interaction between businesses and the government occur at these local levels.

To contribute to the understanding of local business environments, IFC-MPDF and The Asia Foundation are conducting an annual Provincial Business Environment Scorecard (PBES) that measures and ranks economic governance of Cambodian provinces. This Bulletin summarizes the first PBES, which ranks ten Cambodian provinces by general economic governance as well as according to ten specific sub-indices, and looks at the reform priority areas which have an immediate impact on job creation.



The 2006 Provincial Business Environment Scorecard

The PBES is a thorough diagnosis of provincial economic governance⁵ according to ten criteria: *Entry Costs, Property Rights, Transparency, Participation, Time Costs of Regulatory Compliance, Informal Charges, Crime Prevention, Tax Administration, Proactivity of Provincial Leadership, and Dispute Resolution*. The definition and scope of each of these indices are described below.

¹ Unless otherwise noted, the information provided in this Bulletin, including statistics, conclusions and recommendations, is drawn from The Provincial Business Environment Scorecard in Cambodia: A Measure of Economic Governance and Regulatory Policy (PBES). The PBES, published in October 2006, was jointly produced by the International Finance Corporation's Mekong Private Sector Development Facility (IFC-MPDF) and The Asia Foundation (with funding from the Australian Agency for International Development-AusAID).

² The average growth rate is for the 1994-2004 period. The World Bank (2006), *Cambodia: Halving poverty by 2015? Poverty Assessment*.

³ In Cambodia, the poverty line, which is a level of individual consumption of goods and services measured in terms of expenditure necessary for a decent standard of living, is \$0.45 per person per day. The World Bank (2006), *Cambodia: Halving poverty by 2015? Poverty Assessment*.

⁴ The vast majority of the poor (91%) live in rural areas. The World Bank (2006), *Cambodia: Halving poverty by 2015? Poverty Assessment*.

⁵ Economic governance refers to the policy, institutional, and legal environment within which an economy functions. Macroeconomic, microeconomic and fiscal policies, government economic agencies, regulatory policies and bodies, company law and legal institutions all form part of an economy's economic governance. <http://www.ausaid.gov.au/hottopics/apec/ecogov.cfm>



The *Business Issues Bulletin* provides those interested in business issues with a short summary and analysis of a particular topic affecting the business environment in Cambodia. Also included are opinions on topic from a number of relevant stakeholders.

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The statements and opinions presented here are only meant to provide additional reference material and do not reflect the official opinion of the Mekong Private Sector Development Facility or of IFC.

- i. **Entry Costs:** A measure of the time it takes firms to register and receive all the necessary licenses to start a business, the number of licenses required, and the official costs of obtaining all licenses/permits.
- ii. **Property Rights:** A measure of the formal rights to business premises and the security of tenure once land is properly acquired and titled.
- iii. **Transparency and Access to Information:** A measure of whether firms have access to the proper planning and legal documents necessary to run their business, whether those documents are equitably available, and whether new policies and laws are communicated to firms and predictably implemented.
- iv. **Participation:** A measure of whether firms are consulted in the creation of provincial policy and whether their interests are represented in policy discussions by business associations or other interest groups.
- v. **Time Costs of Regulatory Compliance:** A measure of how much time firms spend on bureaucratic compliance and waiting periods, as well as how often they must undergo inspections by local regulatory agencies.
- vi. **Informal Charges:** A measure of how much firms pay in informal charges, how much of an obstacle those extra fees pose for their business operations, and whether payment of those extra fees are predictable and lead to the expected results or “services.”
- vii. **Crime Prevention:** A measure of how much firms pay in explicit costs as a result of crime due to property that is lost or stolen, as well as the implicit costs of preventing crime by paying security and protection money.
- viii. **Tax:** A gauge of both the administrative and fiscal burden imposed by tax regulation in the province.

ix. **Proactivity of Provincial Leadership:** A measure of the creativity and willingness of provincial authorities to assist and interpret in favor of local private firms – given an often unclear national regulatory framework – in implementing central policy and designing their own initiatives for private sector development.

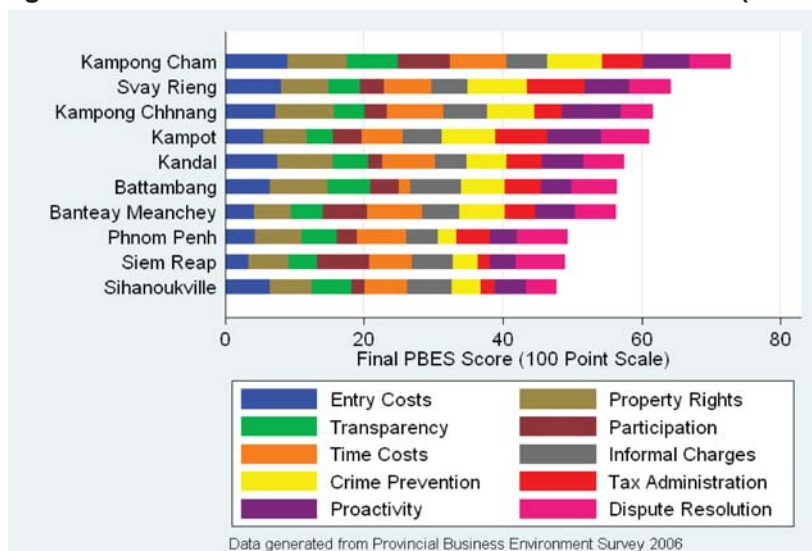
x. **Dispute Resolution:** A measure of the satisfaction firms have in the outcomes of formal and informal modes of dispute resolution in the province.

In 2006, the PBES covers Cambodia’s ten most economically active provinces, which collectively comprise 75% of the country’s GDP and 64% of its population. These include Banteay Meanchey, Battambang, Kampong Cham, Kampong Chhnang, Kampot, Kandal, Phnom Penh, Siem Reap, Sihanoukville, and Svay Rieng.

It is important to note that the PBES measures only economic governance and regulatory policy - it does not measure a province’s overall investment climate, which is defined as a combination of governance and initial endowments (e.g. infrastructure, labor force, etc). Provinces such as Phnom Penh, Sihanoukville and Kampot have better initial endowments so a ranking that included these characteristics would provide little new information for policy makers. By excluding initial endowments, the PBES therefore provides a measure of those aspects of governance which can be improved relatively easily and cheaply, within a medium-range time span.

The final results of the PBES are presented in Figure 1 below. Kampong Cham and Svay Rieng top the list, followed by Kampong Chhnang and Kampot in third and fourth place, Kandal in the fifth place, and then by Battambang and Banteay Meanchey, which rank sixth and seventh, respectively. The provinces that rank lowest are the capital city of Phnom Penh, Siem Reap, and Sihanoukville.

Figure 1: The Provincial Business Environment Scorecard (PBES)

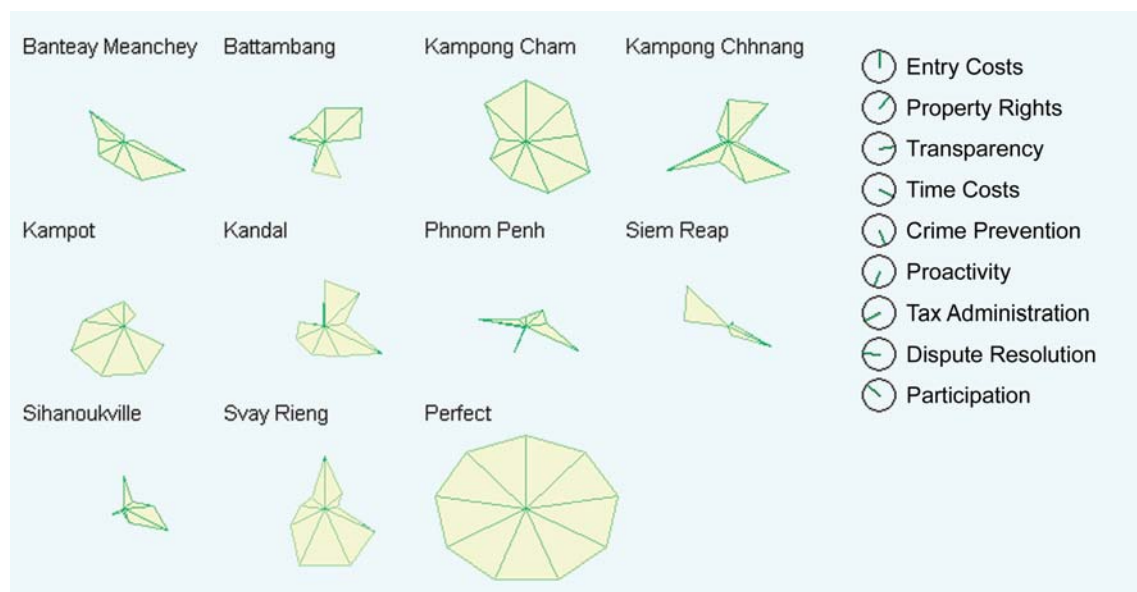


The star chart in Figure 2, below, demonstrates each province's relative strengths and weaknesses, as compared to the perfect score. No single province excels in all areas. Even top-ranked Kampong Cham scores poorly on the sub-indices related to informal charges, proactivity, and dispute resolution. Provinces such as Battambang and Kampong Chhnang have highly skewed governance scores, with excellent marks in some areas and a need for significant improvement in others. The lowest scoring provinces demonstrate a need for improvement on every dimension.

inces, such as Siem Reap, Sihanoukville and Phnom Penh. This news is encouraging, because although the richer provinces have some natural advantages (better infrastructure, better access to markets, etc.) the report's findings indicate that poorer provinces can still compete with them on governance. We hope that the provincial scorecard will start a competitive race among provinces to improve their business environments and create growth and jobs that enable faster poverty reduction.

**Ms. Nisha Agrawal, Country Manager,
The World Bank, Cambodia**

Figure 2: Star Chart of Provincial Scores on Each Sub-Index



The Provincial Business Environment Scorecard's objective is in line with Cambodia's Small and Medium Enterprise Development Framework. By analyzing the status of small and medium-sized businesses, especially as it relates to different aspects of economic governance in ten provinces, the PBES provides the public and private sector in each province with an effective tool for improving the business environment and fostering economic growth.

I support the co-operation between IFC-MPDF, The Asia Foundation, and AusAID. We will work closely together, especially with stakeholders in all provinces, to turn the PBES findings into an action plan to improve the business environment for SMEs at the local and national levels.

H.E. Suy Sem, Minister of Industry, Mines, and Energy

The PBES is a timely report because provinces now already have the authority to approve investment projects under \$2 million. The government is also drafting the new Decentralization and Deconcentration Law, and this will give provinces even more decision-making authority in the future.

One of the most interesting findings of the PBES is that some of the poorer provinces, like Svay Rieng and Kampong Cham, have a better business environment than some of the richer prov-

The PBES measures economic governance in ten Cambodian provinces. It reflects private sector perceptions of how well provincial governments are performing in creating business friendly environments. We hope it will serve as a useful tool for authorities in determining how best to concentrate their efforts when improving local regulations and implementation of central law. Our statistical analysis reveals that successful reforms in these 10 areas (especially informal charges and property rights) should lead to the growth of businesses and the creation of more jobs.

**Professor Edmund Malesky, Technical
Advisor for the PBES project**

The PBES assesses economic governance using a set of specific criteria. But, some criteria used by the PBES do not reflect the real picture of economic governance of provincial administrations as they are under the authority of central government and not provincial administration. For example, tax collection is not under provincial or municipal authority, but rather under the authority of the central government.

**Mr. Suon Rindy, Deputy Chief of Cabinet,
Phnom Penh municipality**

For Kampong Cham, I agree with the findings that highlight the province's seven strengths and three weaknesses. As all indicators are important in determining the business environment, we plan to address each of them. But we will also work closely with the private sector to prioritize reforms that can impact the three weaknesses.

We welcome any technical assistance provided by the donor community. We are ready to work with both donors and the private sector to improve the business environment in our province.

**Mr. Yin Bun Tith, Secretary General,
Kampong Cham province**

I welcome the PBES results and recommendations. I support further dissemination of the results to the business community and government officials.

To improve the business environment in Kampot, I will develop and discuss reform plans with the provincial authority. The reform plans will cover two main areas: first, in reducing the number of procedures and the time involved in obtaining operating licenses, and second, in disseminating business-related laws and procedures to the private sector so that they develop more predictable business plans.

**Mr. Chhun Hin, Director of Department of Industry Mines and Energy,
Kampot province**

In my opinion, the tax burden in Kampong Cham seems to be reasonable. However, the PBES finds that about 84% of firms in the province consider bribes to tax officials a major obstacle. This does not seem to provide an accurate picture of the tax situation.

The more important issue in Kampong Cham is that while some businesses are formal, many are informal. This prevents the development of a level playing field for formally registered firms. I think that the PBES should take this into account.

**Mr. Banh Leng, Chief of SME Association,
Kampong Cham province**

The Impact of the Provincial Business Environment on Businesses

Statistical analysis in the PBES shows that improving the business environment will result in firm expansion and job creation; if mid-ranked provinces were to improve their economic governance to the level of the best-ranked province, their firms would be more likely to expand. For example, if Battambang were to improve from its present PBES score of 56.46 to the level of Kampong Cham, which has a PBES score of 72.9, firms within Battambang's borders say they would be 17% more likely to invest in expansion.

The PBES data also indicates that better economic governance would lead to more employment. As a case in point, if Banteay Meanchey were to improve its present economic governance score to the level of Kampong Chhnang's, it could expect firms to hire nearly 13% more employees.

In Kampot province, there are two areas that the authorities should improve: transparency and informal charges. With regard to transparency, businesses in Kampot are not informed about laws, procedures and their implementation. Also, businesspeople in Kampot have to pay unofficial fees to police and tax officials. Both of these issues prove cumbersome for businesses.

If the authorities improve transparency and reduce informal fees, then businesses in Kampot will be better off. I believe that as a result, businesses (particularly SMEs) would expand their activities and hire more workers who are currently poor.

**Mr. Ton Sakhorn, Vice Chief of SME
Association, Kampot province**

While improving the business environment is not an easy task, IFC's experience in other countries shows that it can be accomplished. For example in 2001 reforms significantly reduced costs and times for receiving business licenses and permits in Qezon City in the Philippines. In the city of La Paz in Bolivia, after just one year of simplifying business registration with IFC technical assistance, the time to get an operating license is 13 times faster.⁶

Conclusion

There are three main conclusions to draw from the 2006 Cambodia PBES:

First, provincial economic governance, as measured by the PBES, differs drastically across the different regions of Cambodia.

Secondly, there is room for improvement in all provinces, no matter how high their scores. No province has a perfect score. For provinces that perform well, there are fewer priorities areas in which they can concentrate their reform efforts. Provinces that scored lower need to improve in all areas of regulatory policy and economic governance.

Finally, any improvements in governance are likely to have a strong impact on provincial business expansion and employment. Nevertheless, a few areas will yield enormous returns. The analysis in the PBES demonstrates that improvements in *Entry Costs, Property Rights, Transparency, Participation, Informal Charges, and Crime Prevention* will be the most effective in creating firm growth and more jobs.

⁶ *Simplification of Business Regulations at the Sub-National Level: A reform Implementation Toolkit for Project Teams IFC (2006) pages 104 and 115.*