A Study on Foreign Direct Investment, The Case of Cambodia

By

SENG SRENG

THESIS

Submitted to
School of Public Policy and Management, KDI
in partial fulfillment of the requirements
for the degree of

MASTER OF PUBLIC POLICY

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ABSTRACT

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The establishment of a free market economy in Cambodia has created a key condition for attracting foreign direct investment. Cambodia has not only the will but also the resources to constitute an attractive venue for foreign investment. The Royal Government of Cambodia recognizes that foreign investment is essential and that it can act as a catalyst for the development of the national economy. Therefore, Cambodia will make every effort to satisfy the needs of foreign investors. The Government of Cambodia is trying to create an institutional and regulatory framework, a stable policy, and a real free market-oriented system. However, to lay the foundation for the sustained inflow of foreign direct investment, the country must maintain a competitive edge and reduce the cost of doing business. The structural reforms will determine whether the country will attract the much-needed foreign investment funds.

This paper will examine the most critical reforms for promoting foreign direct investment in Cambodia. These include: providing a tax incentive system, providing a quality work force, improving the physical infrastructure, reducing red tape and bureaucratic corruption, as well as creating a stable political environment in the country. Not only is our government determined to improve the business climate for investors, but also to create a legislative structure that is supportive of business and investment. The implementation of reform measures has been intensified in the current legislative period.

Cambodia will become a very competitive country for FDI, with a liberal business environment, low cost and hard working labor force. The Government of Cambodia will continue to attract companies from around the world to invest and to do business in Cambodia.

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LIST OF ABBREVIATIONS

FDI	Foreign Direct Investment
CDC	The Council for the Development of Cambodia
MNCs	Multinational Corporations
UNDP	United Nations Development Program
GSP	Generalize System of Reference
MEF	Ministry of Economy and Finance
BOT	Build Operate Transfer
CIB	Cambodian Investment Board
BOOT	Build, Own, Operate, Transfer
BLT	Build, Lease, Transfer
MIGA	Multilateral Investment Guarantee Agency
RCAKL	Regional Center for Arbitration in Kuala Lumpur
SIAC	Singapore International Arbitration Center
WTO	World Trade Organization
IPR	Intellectual Property Rights
UNTAC	United Nation Transitional Authority in Cambodia
ICSD	International Center for the Settlement of Investment Dispute
AFTA	Asian Free Trade Area
ADB	Asian Development Bank

INTRODUCTION

The trend of the global economy is gathering momentum and the interdependence among nations has increased considerably. Every nation of the World has a commitment to economic cooperation in order to achieve balance in the world economy expansion. In this regard, Foreign Direct Investment plays very important role in this process. Foreign Direct Investment not only provides the host-country with integration of the regional economy into the world economy but also offers the host-country technology transfers, employment opportunities, and economic development, as well. Each nation needs to take action to encourage FDI, promoting the development of the developing countries and enhancing cooperation between developed and developing nations.

In undertaking such measures, the basic goal of the Government of Cambodia in attracting FDI is to formulate appropriate policies and to provide a regulatory system to maximize the benefit of capital, technology, employment, growth of trade and peace. There are a set of factors to formulate a country's FDI policies, such as the resource endowment level of economic development, technological development, job creation and access to foreign markets, the level of information development, requirements for capital goals for economic, social, political and cultural development, the underlying economic, social and political system and the structure and level of development of administrative institutions.

Cambodia is a developing country with a market economy. Since Cambodia reestablished a constitutional monarchy in 1993, the economy has grown rapidly, except for the period between mid-1997 and late 1998, when Cambodia suffered from political instability and the spillover effects from the Asian Financial Crisis. The economy began to rebound in late 1998, with the establishment of the current coalition government, but foreign investment in most sectors has lagged, and Cambodia must depend heavily on foreign assistance to meet its investment needs. Since early 1999, the Cambodian Government has intensified its economic reform program, a program that the international financial institutions and donors participate in and monitor closely.

Cambodia's law on investment establishes an open and liberal foreign investment regime, and the Council for the Development of Cambodia (CDC), Cambodia's investment approval body, administers an attractive package of investment incentives. All sectors of the economy are open to foreign investment; there are no performance requirements and no sectors in which foreign investment is disqualified.

This research will investigate the issues and problems associated with Cambodia's current foreign direct investment regime, and more importantly the associated factors that are responsible for Cambodia's unattractiveness as an investment environment. Cambodia's performance in attracting FDI flows has been far from satisfactory. These factors include: the poor physical infrastructure, red tape, a serious lack of skilled labor, as well as political instability.

The paper is divided into five chapters. A brief review of theories of Foreign Direct Investment will be covered in Chapter 1. Chapter 2 will study the actual Foreign Direct Investment environment in Cambodia. Chapter 3 will be the government policy to attract FDI inflows, based on the free market economy of the Royal Government of Cambodia. This chapter will cover the specifics of the government policy. Chapter 4 will present some evidence that the FDI policy of the Royal Government of Cambodia has not done well in attracting investment. In Chapter 5 some recommendations will be provided on the appropriate and ideal policy of the Royal Government of Cambodia for attracting FDI in the future.

Chapter I

A THEORETICAL REVIEW

FDI: THEORETICAL BACKGROUND

Foreign Investment involves the transfer of tangible or intangible assets from one country into another country for the purpose of use in that country to generate wealth under total or partial control of the owner of the assets. It is different from portfolio investment where there is a movement of money for the purpose of buying shares in a company formed or functioning in the other country. For the portfolio investment, it is generally accepted that the investor can take upon the risks involved in the making of such an investment and is entitled to the protection of the domestic law of the host state and the diplomatic protection of the home state from which it was exported. One other factor that sets foreign direct investment apart from portfolio investment is that foreign direct investment are made largely by multinational corporations. This section will explore three popular theories of FDI. It is important to have some understanding of the economic theories behind foreign direct investment.

(i) The Classical Theory of Foreign Investment

This theory takes the position that foreign investment is beneficial to the host country. There are several factors that support this view. The foreign investor usually brings new technology into the host country. There is new employment create whereas, without foreign investment such opportunities for employment would have been lost. Infrastructure facilities will be built by the foreign investor or host state. These facilities may include health, transportation or education facilities and will be provided by the foreign investor to the benefit of the society as a whole.

(ii) The Dependency Theory

The dependency theory is opposed to the classical theory. This theory is popular among Latin American economists. It is focuses on the fact that most investments are made by Multinational Corporations (MNCs), which are headquartered in developed countries. This theory claims that the home states become the central economies of the world and the states of developing world become subservient or peripheral economies serving the interests of the central economies of the states of the multinationals. The resources that flow into the state as the result of foreign investment are seen as benefiting only the elite classes in the developing states, who readily form alliances with foreign capital. One criticism this theory has of foreign investment is that rather than promote economic development, it leaves countries underdeveloped and in a state of permanent dependence on the central economies of developed state. The theory reflects the long-held animosity of foreign investment in Latin American states.

(iii) The Middle Path

The middle path theory of foreign investment takes the position that the benefits brought in by foreign investment identified the detrimental effects of foreign investment. For the first time, serious efforts were made to identify the types of activities of Multinational Corporations that could harm the host economy. The underlying concept was that MNCs should avoid certain identified conduct seen as harmful to the economic development of poor states. The studies pointed out that MNCs defeated the tax laws of the host states by engaging in transfer pricing. According to this theory, the technology transfer touted as one of the benefits of foreign investment, did not actually take place at the levels expected. There were many restrictive clauses introduced into transfer agreements, preventing the transferees from obtaining the full benefits of the transfer. They were intended to maximize the benefits of the transferors but their effect was to hurt the host economy. The studies also indicated that the nature of the technology that was exported was not useful or hazardous. There can be harm to the environment as a result of the export of such technology. The Bhopal disaster, caused by a gas leakage in a plant set up by a multinational corporation, involved colossal damage to life and property. The indication is that the multinational corporations use technology they are not permitted to use in their own states in developing countries because it is cheaper to do so and there are not enough regulations or supervision to prevent the use of such harmful technology. The studies indicate that the need for control of such export of hazardous technology has been demonstrated by the host states.

Depending on the characteristics of the investment, according to this theory foreign investment can bring both benefits and harm to the host states. Previously, the basis of the classical theory is that foreign investment is beneficial for the host states. The classical economists may believe that these states, including Hong Kong, Singapore, Taiwan and South Korea achieved success by following free market principles and permitting full-scale inflows of non-indigenous capital and technology. But the dependency theory is diametrically opposed to the classical theory and takes the view that foreign investment will not bring about meaningful economic development. The studies indicate that the MNCs, which are headquartered in developed countries, operate through the subsidiaries in the developing countries. The proposition is that the MNCs operate in the host countries on the basis of the interests of their parent companies and shareholders in the home countries. As a result, the home states become the central economies of the world and the states of developing countries become subservient or peripheral economies serving the interests of the central economies of the home states of the MNCs. On the other hand, the middle path theory argues that the foreign investment through multinational corporations could have harmful results in certain circumstances, and the studies identify the nature of technology that was exported was often not useful or hazardous. Based on the Bhopal disaster, the harm to the environment, life and property of the host state was caused by the multinational corporation (foreign investment), which brought harmful technology.

Chapter II

FOREIGN DIRECT INVESTMENT ENVIRONMENT IN CAMBODIA

I. Background

The Cambodian economy was virtually destroyed by decades of war which effectively only ended in the past few years. Government leaders are moving toward restoring fiscal and monetary discipline and have established good working relations with international financial institutions.

Despite such positive developments, the construction efforts face tough challenges because of the persistence of internal political divisions and the related lack of confidence of foreign investors. Rural Cambodia, where the vast majority of the population lives, remains poor, and there is a scant basic infrastructure there to spur development.

Leading industries include rice milling, fishing, wood and wood products, rubber, cement, gem mining and textiles. The main agriculture products are rice, rubber, corn and vegetables. The move toward a market economy began when the constitutional monarchy was established in 1993 and the country's 1994 policy on investment establishes an open and liberal investment regime. However, due to political instability and an economic crisis in the region, foreign direct investment has slowed over the past few years and the main domestic activities on which most rural households depend are agriculture and its related sub-sectors.

More than three quarters of the workforce are engaged in agriculture. The vast majority of agricultural workers are subsistence rice farmers, many of whom supplement their income with hunting, fishing or part time jobs. The United Nations Development Program (UNDP) estimates that 39.5 percent of the population falls below the poverty line, which is defined as the minimum income required to provide 2,100 calories per day and basic items such as clothing and shelter. Economic growth in the agricultural sector has not kept pace with the rest of the economy, and thus, Cambodia is experiencing a significant migration from rural to urban areas and from labor-intensive agriculture to industrial employment.

Manufacturing output is varied but it is not very extensive and is mostly conducted on a small-scale and informal basis. The service sector is heavily concentrated in trading activities and catering-related service. However, industrial workers only accounted for 4.6 percent of the work force of 5.54 million in 1999. of these, an estimated 100,000 work in the garment industry in about 200 factories. The garment, timber, tobacco, agro-industry and tourism sectors are the fastest growing businesses in Cambodia.

In order to spur investment, the government, in January 1999, unveiled a reform program that commits to "strengthening" the institutional responsibility for promoting investments. Notably, it aimed to improve the approval procedures for investment applications, to strictly enforce the rules in effect, and banish illegal activities and corruption. Nevertheless, Cambodia continues to be heavily dependent on multilateral and bilateral aid for most of its investment needs, through projects funded by such agencies as the World Bank, The Asian Development Bank and The United Nations Development Program (UNDP).

II. Recent FDI Inflows

In 1996, domestic investment accounted for 20.7 percent of GDP (USD 647 million), of which private investment made up 68 percent of the total. Since national savings were low, at 5.1 percent of the GDP, investment was financed mainly by foreign capital inflows and foreign aid. In 1996, foreign direct investment (FDI) increased from 5.1 to 7.6 percent of GDP.

During 1997, the Council for the Development of Cambodia (CDC) approved 206 investment projects worth a total of USD 759 million, compared with the USD 1.3 billion of investments approved in 1996. Until 1997, domestic investment accounted for 21.95 percent of GDP (166,662,875 USD). Figure from CDC for registered capital of approved projects as of 1997, including domestic investment are presented in the table 1. The proportion of foreign investment in the secondary sector increased from 22 percent in 1996 to 67 percent in 1997, while proposed investment in the primary sector dropped from 66 to 17 percent.

Garment, cement production and electricity generation accounted for the bulk of foreign investment approvals in the secondary sector. The largest projects approved were: USD 196 million cement production (a joint venture between South Korea's Tong Yung Cement Corporation and a Cambodian company, power generation USD 75 million, US's Cambodia Power Company), an industrial park (USD 50 million, Hong Kong's Industrial Park), a water treatment plant (USD 21 million, Canada's Dinico International), and a wireless phone system (USD 15 million, US Portacom Wireless Communication). The majority of investment proposals were to establish garment factories ranging in value from USD 200,000 to USD 6 million.

Seventy eight percent of investment approvals in primary industry were for plantation crops and wood processing. The largest investment was a proposal from a local company, SOKIMEX, for rubber plantations (USD 37 million), followed by three investment proposals in the wood processing industry by Malaysia's Samrong Wood Industries (USD 18 million), China's Everybright Wood (used USD13 million) and Malaysia's Talam Recourses (USD 10 million). The garment industry is the fastest growing sector, with 105 garment projects worth USD 100 million approved in 1997, following the US granting the Generalized System of Preferences (GSP) to Cambodia. By the end of 1997, the number of garment factories in Cambodia more than doubled to 75, compared to 1996. Garment factories, established mainly by investors from Hong Kong, Malaysia, Taiwan, Singapore, China and South Korea, and Thailand employ 120,000 people, of which 40,000 are "direct workers".

Proposals in the tourism and the service sectors dropped by 23 percent to USD 123 million. Five projects worth USD 40 million were proposed for the construction of hotel complexes.

Table1 Investment Approvals by Source Country in 1997 (USD)

Country	**Registered capital**	**Percentages**
South Korea	180,000,194	24.89
Cambodia	166,662,875	21.95
United States	85,754,187	11.29
Hong Kong	72,285,405	9.52
Malaysia	65,778,925	8.66
Taiwan	44,380,306	5.84
China	36,157,049	4.47
Thailand	27,297,898	3.60
Australia	22,227,122	2.93
Singapore	15,120,278	1.99
Sweden	12,041,880	1.59
Canada	11,253,372	1.48
United Kingdom	6,389,657	0.84
Portugal	1,380,000	0.18
Indonesia	1,264,584	0.17
Macau	749,400	0.10
France	724,961	0.10

Israel	392,100	0.05
Japan	294,00	0.04
Germany	137,690	0.02
Total	**759,291,881**	**100.00%**

(Source: The Council for the Development of Cambodia)

Total foreign direct investment (FDI) flows into Cambodia for the years 1995-1999 are presented in the table below. The Ministry of the Economy and Finance (MEF) does not break down this data by country of origin or by economic sector.

Table 2 Total Annual FDI Flows into Cambodia in USD millions

1995	1996	1997	1998	1999
151	240	150	120	160

(Source: The Ministry of Economy and Finance, Cambodia)

Table3 Total Cumulative Registered Investment Capital by Sector from 1994-1999

Sector	**USD Millions**	**Number of projects**
Industry	2,235	736
- Food processing	119	48
- Garment	319	370

- Petroleum	126	19
- Wood processing	472	39
Agriculture	231	62
Service	1,765	90
- Energy	149	10
- Telecommunication	131	12
Tourism	1,972	55
Total	**6,203**	**943**

(Source: The Council for the Development of Cambodia)

III. Sectoral Investment:

Industry

In 1997, the industrial sector recorded growth of only 3 percent, compared to 13.3 percent a year earlier, reflecting the country's economic downturn. The construction sector, which accounted for 52 percent of total industry output, was the most badly affected by the economic crisis, dropping to 1.1 percent, compared to a high growth rate of 10.4 percent in the previous year. The manufacturing sector continued to expand by 7.3 percent, electricity and water by 14.9 percent and mining by 2.3 percent, which contributes 19.9 percent of GDP.

According to a study by the Ministry of Industry, Mines and Energy, from 1994 to 1996 fifty new factories were established, bringing the total numbers of factories to 120. Thirty two percent of the factories were in the apparel textile sub-sector, 16 percent were in the food, tobacco and beverage sub-sector, 16 percent were in the wood sub-sector and 12 percent were in the non-metallic minerals sub-sector. Textile and garment factories were the fastest growing, accounting for 65 percent of new jobs. Food, beverage and tobacco manufacturing was second, and the chemical industry was the third. Local production only covers about 10 percent of current domestic demand for consumer goods and clothing.

Garment production is one of the most promising industries in Cambodia. Low cost labor has enabled Cambodia to steadily increase its garment exports. Cambodia exported USD 224 million of garments in 1997, more than a fourfold increase since 1995. Between 1994 and 1997, the Council for the Development of Cambodia approved 180 garment projects undertaken mainly by companies from Hong Kong, Taiwan, China, and Malaysia. By the end of 1997, there were 75 garment factories established in Cambodia employing 120,000 people, of which

70,000 were "Direct Workers". Twenty-seven countries have granted the GSP status to Cambodia, which has contributed to the rapid expansion of this sector. The major industrial projects established in 1996-97 were: a USD 25 million joint venture between a British-American tobacco, a Thai company and a Chinese company (Zhuhai International Trade and Exhibition Ltd.) to build a USD 38 million cement factory, and a consortium of a local company and a South Korean company (Tang Yang Cement Group) to build a USD 200 million cement factory. In February, a Singapore company launched its USD 4 million electronic assembly plant, the first of its kind in Cambodia. The factory employs 30 workers who assemble televisions, home appliances, and video and audio equipment. The World Bank forecast that the industry will grow at the average rate of 9 percent a year for the next five years. This will largely be a result of increased foreign investment in Cambodia, in particular, in garment manufacturing and electronics.

Mining

Prior to 1999, The Royal Government of Cambodia signed three contracts with foreign companies, who spent more than USD 100 million on explorations. However, exploration for prospective oil and gas resources has been disappointing. In late December 1996, one of the companies, Enterprises Oil, announced that it had capped its Cambodian wells and had halted all exploration. In November 1997, an Australian company, Woodside South East Asia Pty. Ltd., signed a production sharing agreement with the Royal Government of Cambodia to carry out oil and gas exploration on two blocks in non-disputed water in the Gulf of Thailand.

Tourism

Cambodia has a comparative advantage in tourism and developing the industry makes good economic sense. It has a wide range of potential tourism assets: architectural and cultural sites of world renown (including the Angkor Wat complex). During 1997, five projects worth USD 40 million were proposed for the construction of hotel complexes. Three big hotels were launched during the year: a new 354-room international hotel, plus the Hotel Le Royal in Phnom Penh and the renovated "Grand Hotel" in the province of Siem Reap, both own by the Raffles

Group of Singapore. Tourist operators were optimistic in late 1998 that, following the restoration of political stability, the number of tourists would again begin to increase. However, the industry is unlikely to significantly pick up again before the economic turbulence in the region is over.

Commercial

The second tier of Cambodia's banking system consists of 30-registered commercial banks, including one state-owned bank and seven branches of foreign banks. The banking sector is characterized by a relative high degree of concentration (at the end of 1996, eight banks accounted for 86 percent of total deposits and seven banks accounted for 66 percent of outstanding loans). And a wide variation is the scale of activity (some of the smaller banks essentially extend credit). The level of financial intermediation is low: total loans outstanding amounted to 4 percent of GDP in 1995. Most foreign bank established branches in Cambodia in order to service their existing business customer operations in Cambodia.

Public Infrastructure

The Royal Government of Cambodia announced plans to privatize the country's infrastructure sector: railways, waterways, airports, and hydro and diesel electric plants on Build, Operate and Transfer (BOT) basis. Investors would be required to transfer the facilities to the government within 25 years to 30 years. Moreover, Cambodia granted a license to a Malaysian company, Pro-Majestic, to invest USD 15 million in stevedoring operations. In 1998, a Cambodian and Chinese company, China Central Asia Group, signed an agreement to build a USD 12 million dry ports near the international airport (Pochentong Airport).

Energy

During 1993-97, rehabilitation of the power generation and distribution system was carried out with funding from bilateral donors, the World Bank and foreign investors. At the provincial level, generation capacity remains weak, and the foreign investors are currently funding three provincial projects in the energy sub-sector.

Telecommunications

The Royal Millicom, a joint venture between the local Royal Group, Swedish Millicom and the Ministry of Telecommunications, signed a USD 30 million joint venture agreement with the Cambodian government to establish a second gateway for international telecommunications. The gateway will be established to provide Cambodia with a satellite link for telephone, fax data and video conferencing services. Cambodia signed an agreement with South Korea's company, Tang Yang Group, and a local company to build a USD 70 million third telecommunications gateway. The joint venture will lay an underwater cable connecting Cambodia to a major international cable system, linking Cambodia to 70 countries. Moreover, Cambodia began work on a USD 17 million fibre optic telecommunication line, funded by Germany, liking Cambodia to Thailand.

Chapter III

THE GOVERNMENT POLICY TO ATTRACT FDI

I. Incentive Policy

As the Cambodia investment law is aimed at bringing in more foreign capital into the country, it offers investment incentives and guarantees to foreign investors. An enterprise permitted by the Cambodia Development Council (CDC) shall enjoy a tax holiday of up to eight years, and the law on investment and subsequent decrees create the following incentives:

- A corporate tax rate of 9 percent, compared to the standard corporate profit tax rate of 20 percent for business enterprises not receiving CDC investment incentives; natural resources companies, including timber and oil companies and companies mining gold and precious stones, are subject to a 30 percent corporate profit tax rate
- An exemption from a corporate profit tax for up to eight years depending on the type and location of profit

- A five-year loss carry-forward
- Tax-free distribution of dividends, profits and proceeds of investment
- Tax-free repatriation of profits
- 100 percent exemption from import duties on construction materials, machinery and equipment, spare parts, raw materials and semi-finished products, and packaging materials for most projects for the construction period and the first year of operation. The period of exemption from customs duties for the above items can be extended for export-oriented projects with a minimum of 80 percent of production set aside for export and projects located in a special development zone, although these have not yet been specified.

Investment incentives are available for manufacturing prospects in the following sectors: when investment capital exceeds US$500,000-rubber and miscellaneous plastic, leather and other products, electrical and electronic equipment and manufacturing, and processing of food and related products.

A minimum investment of US$1,000,000 applies when seeking incentives in the following three sectors: apparel and other textiles, furniture and fixtures, chemicals and allied products, textile mills paper and allied products, fabricated metal products and production of machinery and industrial equipment.

The investment law also provides an irrevocable state guarantee that an enterprise permitted by Cambodian Investment Board (CIB) shall not be nationalized. It also provides for repatriation of profits (after deduction of all taxes and prescribed funds) as well as the legitimate balance of salary and lawful income of foreign personnel (after payment of living expenses and taxes).

II. Legal Framework

In 1993, the Kingdom of Cambodia changed its centrally planned economic system that has been in place for more than one and a half decades to a market oriented system. In doing so, the private sector has been given the opportunity to be involved extensively in almost all economic activities, especially in the area of trade and investment. Regulations were created for a series of existing legislation, and new laws enacted. Moreover, the existing laws that are no longer appropriate for the new system were amended to be compatible with the changing economic environment.

In order to foster the investment activities in the market economy system, it is necessary to have in place the required policies, law and regulations, which generally regulate private sector operation. Moreover, the dispute settlement procedures must be an important key element in order to support interactions among the government, entrepreneurs and private citizens in the market place.

Addressing the needs of foreign investors, the Cambodian government has enacted a variety of laws and regulations as follows:

- The early adoption of the following legislation:
  - ■ From CDC, the privatization of state-owned assets legislation, and the law on BOT (Build, Operate, Transfer), BOOT (Build, Own, Operate, Transfer), and BLT (Build, Lease, Transfer).
  - ■ From various ministries: a customs code, a taxation law, an insurance law, a casino and gambling law and guidelines and rules

for public procurement and tendering, a law on contracts, a bankruptcy law, a labor law and a law on the organization of the judiciary.

The ratification of international conventions to persuade foreign and domestic businesspeople that, in the event of disputes, the Cambodia Government will provide the means by which they can be resolved quickly and fairly, namely by:

- Ratifying the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitrage Awards ("the New York Convention").
- The Multi-lateral Investment Guarantee Agency (MIGA) offers both investment guarantees and loans in Cambodia. Cambodia is today a member of the Multilateral Investment Guarantee Agency (MIGA).
- Appointing a body, on a transitional basis at least, either the Regional Center for Arbitration in Kuala Lumpur (RCAKL) or the Singapore International Arbitration Center (SIAC), for the purpose of the Model Law in international commercial disputes where parties are unable to

agree on the choice of arbitrators.

The development of an enabling legal environment by:

- Reestablishing and strengthening certain key legal institutional capacities and procedures required for developing the economic and financial legal framework necessary for private sector development in the country.
- Encouraging the transfer of experience and expertise by qualified foreign lawyers and professionals.
- Strengthening the government's institutional capacities and official procedures by:
    - ◆ Publishing a compendium of Cambodian laws
    - ◆ Regularly publishing Cambodia's official journal in Cambodian, French and English languages and disseminating it effectively.
- Establishing an automated system for systematic reporting, collection and publication of the decisions of Cambodia's higher courts.
- And developing a system for jurisprudence and doctrinal writings.

Protection of Intellectual Property Right

Cambodia has ratified a bilateral trade agreement with the United States that establishes the standards for intellectual property rights, which Cambodia has agreed to meet. Cambodia drafted laws to protect trademarks, patents and copyrights.

Cambodia is not a WTO member and its intellectual property rights (IPR) regime falls far short of WTO standards. The 1996 U.S.-Cambodia Trade agreement contained a board range of IPR protection, but given Cambodia's very limited experience with IPR, the agreement granted phase-in periods for the Cambodian government to fully implement these provisions, including the enactment of new legislation. The copyright, trademark and patent laws have been prepared with assistance from WIPO. The status of specific IPR areas is outlined below:

- Copyrights: responsibility for copyright is split between the Ministry of Culture (phonograms, CDs and other recordings) and the Ministry of Information (printed materials). The Ministry of Culture prepared a draft copyright law in 1998 and submitted it to WIPO and the Ministry of Commerce in October 1998 for comments. The Ministry has not sought comments on the law from the U.S. or private sector nor submitted it to the National Assembly. With no copyright law or regulations in place, there accordingly has been no enforcement of copyright provisions of the trade agreement.

- Trademarks: This is the most advanced part of the Cambodian IPR regime. The Ministry of Commerce has created an effective trademarks registration system, registering more than 10,000 trademarks (over 2,9000 for U.S. companies)

III. Institutional Framework

The Council for the Development of Cambodia (CDC)

This is Cambodia's one-stop foreign investment approval body. Through its operational arm, the Cambodian Investment Board (CIB), it is responsible for processing applications for investment projects and required to give a decision within 28 days of submission. It is the highest-level authority on investment and is chaired by the Prime Minister and composed of Senior Ministers from related ministries. It administers a package of investment incentives.

- Under the 1994 law, all sectors of the economy are open to foreign investments; there are no performance requirements and no sectors in which the foreign investor is denied national treatment.
- The CDC is specifically targeting pioneer and high-tech industries, those that create jobs for Cambodians, export-oriented industries, tourism, agro-industries and processing, light electronics assembly, transportation and infrastructure, and the energy sectors for foreign investment. In addition, it supports industries enhancing provincial and rural development, as well as environmental protection.
- Investors who wish to take advantage of investment incentives must submit an application to the Cambodian Investment Board (CIB), the division of the CDC charged with reviewing investment applications. Investors who do not wish to apply for investment incentives may establish their investment simply by registering corporate documents

with the Ministry of Commerce of Cambodia. Once the investor's application is completed and an application fee is paid, the CDC is required by executive order to issue a decision on an investor's application within 28 days of submission. Once the CDC approves the project in principle, the investor must pay a second application fee and deposit a performance guarantee of between 1.5 and 2% of the total investment capital at the National Bank of Cambodia and register the corporate entity at the Ministry of Commerce of Cambodia. Once these steps have been taken, the investor will receive a formal investment license from the CDC requiring the investment to proceed within six months. Once the project is 30 percent completed, the investor is eligible for a refund of the performance guarantee.

Privatization

Privatization is one important component of the economic reform of Cambodia, which started in 1994. The trends towards selling majority shareholdings in state-owned enterprises have given privatization a big boost.

With respect to the privatization of state-owned assets, the overriding objective is to ensure the successful drive towards the transfer of state-run enterprises to the private sector in order to stimulate growth and efficiency with the minimum dislocation to workers. In its Declaration on Privatization on December 1994, the government identified various aspects of its policies and implementation mechanism. For example, it extended the scope of privatization to all state-owned industrial and commercial enterprises (autonomous enterprises and administrative services) and it defined methods of privatization and the rules of institutions concerned. An Interministerial Committee in charge of privatization supervises all operational aspects of privatization (e.g. evaluation of assets, staff reduction plans, condition of contracts, preparation of tender documents, and selection of preferred tenders).

State Institution

The ultimate object of these initiatives is to lay the foundations for good governance and the Rule of Law. They concern the fair and equitable application of the policies and law of Cambodia, and for this, the functions of government ministries and agencies must be clarified and strengthened, the policies of government and administration must be transparent and accountable, as well as neutral, and the government must work as partners of the private sector.

The objective of this component is essentially to organize governmental work efficiently, this contributing to the strengthening of the effectiveness of the administration. It principally involves the strengthening of the state-run superstructure to manage and coordinate governmental action, to clarify ministerial attributions and to restructure the services necessary for administrative effectiveness and propriety.

IV. Dispute Settlement

Cambodia's legal system, modeled on French law, was dismantled by the

Khmer Rouge. The legal system of the successor state of Cambodia was superseded by statute put in place by the United Nation Transitional Authority in Cambodia (UNTAC). These remain in place.

The government has acknowledged the desirability of binding international arbitration of investment disputes in Article 20 of the Cambodian Investment Law. The Article provides that an investment dispute shall first be settled through consultation between the parties, and then, should agreement fail to be reached, through conciliation before the CDC, through proceedings in the Cambodian courts, or by reference to international rules as mutually agreed by the parties (International Arbitration). The government of Cambodia intends to become a member of the International Center for the Settlement of Investment Dispute (ICSD), and Cambodia ratified the New York Convention on the recognition and enforcement of foreign arbitration awards on January 5, 1960.

V. Membership in ASEAN and AFTA

Cambodia is more likely to benefit politically from ASEAN membership, which is expected to reinforce its political stability and help to establish a mechanism for peaceful settlement of political conflicts and border disputes with neighboring countries. It is also hoped this will instill confidence in potential investors, attracting FDI which is crucial to future economic development and reducing Cambodia's dependence on foreign aid.

Cambodia is a member of ASEAN and AFTA and hopes to benefit from economic integration. ASEAN and AFTA membership requires the Government of Cambodia to reduce tariff and non-tariff barriers to trade, broaden the tax base to lessen its dependency on customs revenues and play an active role in regional and international affair. The Government of Cambodia needs to establish a modern taxation system in line with those of ASEAN countries, and harmonize the customs valuation system. Customs duties accounted for 70 percent of all tax revenue and 42 percent of current revenue in 1997. Therefore, tariff reduction will have an adverse impact on budget revenue unless the tax base is broadened. Over the medium to long term an active role in ASEAN/AFTA could transform Cambodia into an attractive investment destination.

Aside from political and common benefits as previously described, Cambodia expects to gain the following economic benefits from regional integration:

- ASEAN will enhance investor confidence in Cambodia; the fact that ASEAN allows Cambodia to be a member represents a collective vote on the country's political and economic situation. In the past, some foreign investors took a "wait and see" attitude as a result of the internal political and security situation uncertainty. By admitting Cambodia as a regional partner, ASEAN is de jure placing its seal of approval on the country as a whole in terms of the political, security and economic environment. This is an important and positive sign that may greatly influence the attitude of foreign investors.
- The combined population of the ASEAN-10 is nearly 500 million people, and the grouping, which is rich in natural resources, raw materials and land, represents a large market full of economic potential and an attractive destination for investment. Cambodia is geographically situated in the middle of the ASEAN and Mekong-6 (Cambodia, Laos, Burma, Thailand, Vietnam and the Yunan province

of China) regions, and together, the two regions have a combined market size exceeding 600 million people. Cambodia can capitalize on its geographic advantage along with growing economies of scale to attract foreign direct investment (FDI).

VI. Infrastructure

The Cambodia infrastructure is not well developed, and has become a priority for the government, particularly in urban areas. The state of the country's physical infrastructure acts as a binding constraint in developing the country.

In July 1997, the government of Cambodia announced plans to privatize the country's infrastructure sector: railways, waterways, airports, and hydro and diesel electric plants on a Build-Operate-Transfer (BOT) basis. Investors would be required to transfer the facilities to the government within 25 to 30 years. During 1994-1997, the government completed its program to repair the most dilapidated sections of the primary road network linking Phnom Penh city to the major provincial capitals. One thousand kilometers of the existing 4,000 km of national roads have already been renovated. With the assistance of the ADB and Multilateral and Bilateral donors, the road infrastructure has improved considerably. Some rehabilitation of the rural road infrastructure, to improve transportation of agriculture products, promote rural development and foster tourism, has been supported by the World Bank and the European Union. The Government of Cambodia hopes to rebuild Route Nos. 1, 5, 6 and 7 within the next three years, to contribute to the concept of the Trans Asian Highway.

Major projects currently underway include a USD 250 million loan agreement with the ADB for the upgrade of Route Number 1, linking Phnom Penh city to Ho Chi Minh city, a Japanese-funded project to improve the road from Phnom Penh city to the provinces and build a bridge across the Mekong River and a USD 13 million World Bank pledge to overhaul 104 km of roads in three major towns. In 1997, the Government of Cambodia began work on the reconstruction of 14 roads in Phnom Penh. On 23 April 1998, the Government of Cambodia and a Chinese company, China Central Asia Group, signed an agreement to build a USD 12 million dry ports near Pochentong Airport. In mid-1998, Cambodia opened its second dry port, a USD 20 million joint venture between CWT Distribution Ltd. of Singapore and the Sihanouk Ville Port Authority. The Cambodia-CWT dry port, an inland container depot in Sihanouk Ville, provides customs clearance services and warehousing facilities.

Cambodia's railway system consists of two single-line meter gauge tracks, one reaching 385 km from Phnom Penh city to Poipet and the other 263 km from Phnom Penh City to Sihanouk Ville. The railway is in dilapidated condition and the track and rails need to be replaced.

Cambodia's ferry transport has been boosted by an USD 18 million reconstruction project funded by Denmark, with two new ferries, the overhaul of three existing ones and upgrading of ferry landing and other facilities.

Energy

During 1993-1997, rehabilitation of the power generation and distribution system was carried out with funding from bilateral donors, the World Bank, the ADB and foreign investors. Power generation in Phnom Penh city was increased to 112 MW in early 1998, a 40 percent increase in two years. It is expected to increase to 172 MW in the year 2000. The current power supply in the capital is more than sufficient to meet demand. At the provincial level, generation capacity remains weak and foreign investors are currently funding three provincial projects in the energy sub-sector. Local companies along with bilateral and multilateral donors are also working with the Government of Cambodia to upgrade power generation and the distribution infrastructure in several provinces.

Water

Under the first five-year Social and Economic Development Plan for 1996-2000, the Government of Cambodia proposed to invest about USD 160 million in water supply. In September 1997, the Phnom Penh Municipality signed a USD 40 million BOT contract with a Canadian company, Dinico International, to build a water purification plant. The construction is expected to be finished by the end of

2000. In December 1997, Japan provisionally agreed to fund the third phase of the "Clean Water to All" master plan for Phnom Penh, to increase the capacity of its water treatment plant to more than 150,000 cubic meters per day.

Telecommunication

Cambodia's telecommunication industry is growing into a modern, nationwide system. In 1997, the total number of telephone lines increase by 78 percent to 47,000, compared to 1996. The supply of phone lines is more than sufficient to meet demand. In February 1997, the Government of Cambodia approved a USD 140 million master plan to expand the existing exchange system in an attempt to improve Cambodia's clogged and chaotic mobile phone networks and overhaul the telecommunications system. The master plan would address the problem of transmission, connections, charges, information systems and human resource development.

VII. Labor Market and Regulation

Labor Market

Cambodia has a workforce of 4.85 million people, accounting for 45.3 percent of the population. While Cambodian women contribute 55.7 percent of the labor force, the world's highest percentage of women in the workforce, they predominate in the lowest paying jobs. About 16 percent of Cambodia's nearly four million children between the age of five and seventeen (around 600,000 children) are in the workforce. An estimated 120,000 new workers join the formal job market each year, with about 27,000 of them migrating to Phnom Penh city from rural areas in search of jobs. Wage employment accounts for just 10 percent of the workforce and unemployment continues to worsen.

Because the education system was destroyed during the years 1975 to 1979, average levels of education remain low. However, many Cambodians are enrolled in computer, language, and other courses as adults. Investors reported that Cambodian workers are easily trained; they take personal responsibility for their work and work long hours willingly.

Labor Regulation

A new labor law, enacted in January 1997, is responsive to the requirements for receiving MFN trading status and the Generalized System of Preferences (GSP) and is aimed at complying with “Internationally Recognized Workers' Rights”. The new law provides for the protection of workers' rights, formation of trade unions, collective bargaining, a minimum wage and special working conditions for children and females workers. The law sets procedures for labor inspections at the work place. Employers are also required to provide training to their employees.

Both written and oral employment contracts are valid under Cambodian law, which also provides for the hiring of staff and termination procedures. Collective bargaining contracts are permitted. Industrial disputes, which cannot be resolved amicably, must brought before the local labor inspector for conciliation and arbitration before proceeding to court. The government ministries may also play a role before the judicial process begins.

All foreigners working in Cambodia must register with the Ministry of Social Welfare, Labor and Veterans Affairs, pay an annual tax of USD 100, present a medical check up report and have a valid business visa before being issued a work permit and employment passbook. The passbook is to be used to record employment dates, employers, and salary rates of laborers.

VIII. Investment Guidelines

The Cambodian Investment Board (CIB), operating within the Council for the Development of Cambodia (CDC), is the government agency responsible for granting investment incentives and approving investment projects. An investor may establish a company through the Ministry of Commerce, but investors must submit their applications through the CIB to take advantage of the more favorable provisions of the investment law.

The investment process is easier than that of some regional countries. An application is filed with the CIB, along with a USD 100 application fee, a feasibility study, and the latest report of the investing company. The law provides that the CIB has 28 days from submission to decide whether to approve the investment. Although the law states that the CDC is a “one-stop” organization, foreign investors must often meet with officials from relevant ministries and provincial authorities governing the sector of their project. This helps ensure that those parties will support the project at the CDC and recommend that a license with maximum incentives be granted.

If the government will have an interest in the project, or it involves the lease or purchase of government assets, the government usually precedes the investment process at the CIB/CDC. Prime Ministerial approval may be required for large investment projects.

IX. Political Stability

Political factors have played and will continue to play a pivotal role in Cambodia’s economic and social performance. Political stability is a key pre-requisite for development as these shape investors' expectations and set the overall enabling environment for private sector led growth.

Political stability has improved following the formation of a new government in late 1998, and has brought an upturn in commercial activity. Cambodia has emerged as an open, democratic society. Since the October 1991 Paris Peace Accords, Cambodia has organized two national elections, which were considered vital for the democratization of this country. The 1993 election, organized under United Nations supervision, was an important turning point for Cambodia. The 1998 election, however, was entirely organized by the Cambodians themselves, and despite some controversies, both elections were considered to be free, fair and credible. At the same time, as a result of the 1998 election, Cambodia today has a very active opposition party within the National Assembly and two Senates. The opposition party has a critical role to play to in ensuring the process of democracy as well as promoting a system of check and balances. In addition, the role of the media is indispensable for the development of democracy and a free market economy. Cambodia has one of the freest presses today in the region. It also has a vibrant civil society, which has been active in nation building and the development of Cambodia.

For the first time in the past thirty years in this country, peace, stability and security have been consolidated and further strengthened. The end of the Khmer Rouge brought an end to Cambodia's era of war and conflict. This was a remarkable achievement for this country. There was a sense of real peace, happiness and looking to the future for the people of Cambodia. In this respect, Cambodia has entered a new era of peace and political stability, where more effort, energy and time will be concentrated on nation building and economic development. This is the way for Cambodia to gain the confidence and trust of foreign investors who may consider investing in the country. It is strongly believed that Cambodia will continue to enjoy greater peace and stability in the coming years. The total demise of the Khmer Rouge and the commitments of the two major political parties to work together for the development of Cambodia are the two key elements for a lasting peace and stability in this country.

X. Conversion and Transfer Policy

There are no restrictions on the conversion of capital. The investment law guarantees investors the right to purchase foreign currencies through the banking system and to remit foreign currencies as payments for imports, repayments on loans, payments of royalties and management fee, profit remittances and repatriation of capital. The Government of Cambodia conducts a weekly auction of US dollars in which all licensed traders and companies in Cambodia are eligible to participate. The foreign exchange law does allow the National Bank of Cambodia (the Central Bank) to implement exchange controls in the event of a crisis, but the law does not define what would constitute a crisis.

CHAPTER IV

OBSTACLES TO FDI IN CAMBODIA

I. Weakness of Institutional and Legal Structure

The investment environment in Cambodia is a challenging one, although there has been overall improvement in recent years. The key ingredient for success in the Cambodian market is the development of a network of effective personal contacts within the bureaucracy and among suppliers, distributors and agents. Traditionally, the investment is done through family and friendship connections.

Cambodia's difficult past and its recent rapid transition from communism to capitalism has resulted in a highly unregulated investment environment, including some of the region's most liberal retailing and advertising policies.

One of the most visible problems of investment in Cambodia is the lack of effective physical and institutional infrastructure. Basic public utilities are improving, the increasing demand for electricity and power supply are gradually being met, and telephone services are improving. In early 1998, major work began to upgrade several major roads and some provincial highways with the assistance of international aid. However, particularly outside the capital, the quality of roads remains extremely poor.

The lack of a strong legal culture is a problem. The Royal Government of Cambodia has passed some legislation to replace the outmoded law of the communist period, such as the investment law, the commercial registration law, the labor law and various amendments to the tax law. By early 1998, however, the government remained only partway through the implementation of a number of the laws that are to make up the country’s commercial code. There are still many gaps, including in such areas as property, companies and associations, contracts and dispute settlement, bankruptcy, mortgages, insurance and mining. The law will be developed over time, but it takes longer to develop a legal culture for their effective application. There is no tradition of an independent judiciary to arbitrate on commercial disputes.

However, Cambodia's court system is weak. Judges, who have been trained either for a short period in Cambodia or under another system of law, have little access to published Cambodian law. Judges are inexperienced and the courts are understaffed. The local and foreign investment communities have reported problems with inconsistent judicial rulings as well as outright corruption. Cambodian judges are paid minimal salaries, which are not adequate to sustain a livelihood. Corruption is a far greater problem in Cambodian courts than government interference in judicial decisions.

There is currently no law requiring a Cambodian court to enforce either a foreign judgment or arbitration award. The Cambodian Government has acknowledged the desirability of binding international arbitration and hopes to include implementing provisions for the New York Convention on the Recognition and Enforcement of Foreign Arbitration Awards, which Cambodia signed in 1960, in the Commercial Arbitration Code. Meanwhile, the government has prepared interim legislation to bring the New York Convention into force, but has not yet submitted it to the National Assembly. Regardless of the legal basis for implementing arbitration awards, foreign or domestic, the ability of the Cambodian Courts to enforce even their own decrees remains limited.

II. Bureaucracy and Corruption

An important aspect of investment in Cambodia is dealing with the bureaucracy. The Royal Government of Cambodia itself admits that corruption is a problem. After the fighting in July 1997, the CPP (Cambodian People's Party) effectively took control of the structures of government once more, restoring to some extent the bureaucratic system (and many of the personnel) from the former communist regime. Low salary levels and unreliable payment of wages often leads to poorly motivated officials who are frequently absent from their positions. Delays and inconsistent decisions can become frustrating.

There are no performance requirements applied to foreign investors in Cambodia. A generous set of investment incentives is administered by the Council for the Development of Cambodia (CDC), which is meant to be one-stop-service for potential investors. In fact, investors reported that the process often requires significant red tape and the involvement of several government agencies.

Some of the consequences of the lack of rule of law and the state of the bureaucracy are that:

- Most bureaucratic decisions involve a process of negotiation at the enterprise level, rather than the application of law.
- Tender outcomes are often questionable.
- Dealing with corruption is a fact of business life; and
- Contracts are frequently not honored.

III. Unskilled Labor Market

A feature of the Cambodian labor force is its low level of education and, generally, its low productivity. Only 20 percent of the population is educated beyond the primary school level. Illiteracy affects 35 percent of the adult population (50 percent among women). At present, 31 percent of those aged 7 years and over attend school and receive some sort of vocational training. Business people find it is easy to recruit unskilled factory workers and laborers, but much harder to recruit skilled office workers. Most business employ a high proportion of expatriates for administrative, management and other specialized positions.

Unskilled labor requirements in both the public and private sector are extremely low. The businesses people are concerned with have risen above the level of unskilled workers. Most of the workers in Cambodia have been huge lack of proper skill and talent, including English language, technical and specialized skills.

IV. Security and Political Apparatus

Security Apparatus

Cambodia's security situation places constraints on investment activities, particularly in the rural areas. Security problems are most likely to arise from either bandits or undisciplined elements of the security forces. It is often difficult to determine the perpetrators, and indeed to distinguish banditry from politically related activity. The Khmer Rouge threat has essentially disappeared, with the defection of almost all forces during 1998. Security in the major urban centers like Phnom Penh and other cities is reasonable, but the main problem is armed robbery. Particular care needs to be taken at night. There have been some instances of foreign investors and rich Cambodian nationals being kidnapped for ransom in the countryside. In the countryside, the Khmer Rouge have largely disappeared, but traveling in the countryside remains problematic due to robbery at the hands of either bandits or elements of the local security forces.

Political Violation

The violent political events of July 1997 had a significant negative effect on foreign investment in Cambodia. The most significant event in Cambodia during 1997 was the fighting which broke out on 5-6 July between factions of the security forces loyal to the two major political parties in the governing coalition, FUNCINPEC and the Cambodian People's Party (CPP). With political tension between the two major parties making up Cambodia's fragile ruling coalition government, the tensions focused on a struggle for control of the armed forces and the recruitment of defectors from Khmer Rouge in the North and West of the country. FDI dropped substantially with the political instability of 1997, and has not fully recovered. The Council for the Development of Cambodia, the government's investment agency, reports that new investment commitments dropped significantly to only USD 482 million in 1999, compared to over USD 800 million per year in 1996.

In summary, the government of Cambodia has adopted a free market, pro-investment economic policy. The state's role in the economy is minimal and the government offers significant incentives to attract foreign investment. However, significant gaps in the legal system, the weakness of institutional framework such as the Council for the Development of Cambodia as well as related line Ministries, and the problems of unskilled labor, physical infrastructure, non-transparency and corruption continue to deter investment. One notable exception has been the garment industry, which has attracted over 160 new factories since 1994 and now accounts for over 90 percent of Cambodia's exports. This industry was drawn to Cambodia by the availability of a textile quota for the US market, and Cambodia has not yet repeated this degree of success in any other sector.

CHAPTER V

RECOMMENDATIONS FOR FURTHER PROMOTING THE FDI POLICY IN CAMBODIA

To further promote FDI, the measures taken by the government so far should continue to be steadily implemented, and the recommendations below suggest ways to continue facilitating it.

(i) Respond quickly to Complaints and Requests

For individual complaints regarding foreign investment, The Royal Government of Cambodia should require of the Cambodian Development Council (Cambodia Investment Board) to reach solutions. Where requests related to various areas of investment are concerned, the Cambodian Development Council should make efforts to deal with the problem fairly and quickly and other related line Ministries should be supportive. All decisions made by Cambodian Development Council, which is one-stop-service for potential investors should be transparent and exhibit accountability. There is no doubt that there will be more investment and economic dialogues and consultations between the private sector and the government. This kind of dialogue will promote better understanding between the private sector and the government. It is aimed at exploring in conjunction with the business community measures and solutions to facilitate and promote investment in Cambodia.

(ii) Eliminating Bureaucracy and Corruption

Another challenge for Cambodia is the lack of good governance in almost all institutions. Cambodia needs to promote good governance in all institutions and at all levels--be they public or private. For example, this country needs to at least contain corruption, if not move towards ending it. Cambodia also needs to reduce the non-transparent and arbitrary decisions dealing with economic issues. One important consideration is to promote access to reliable, consistent, up-to-date economic information. In this context, Cambodia may need to set up its own information infrastructure and promote a culture of information in this country. Ultimately, access to reliable information could help reduce risk for investors who are considering business in Cambodia.

Cambodia needs to promote greater institutional coordination and cooperation, Specifically, inter-ministerial economic cooperation to ensure that policies are implemented and followed through upon is critically important for policy coordination and implementation if Cambodia is to offer a real one-stop-service for investment.

(iii) Physical Infrastructure

While FDI policy frameworks and a range of business facilitation measures can lure foreign investors to a particular location, the investors also seek a combination of cost reduction and "created" assets that can help maintain a competitive edge. "Created assets" include the communication infrastructure, marketing networks and innovative capacity. These are critical for enabling foreign firms to maintain their competitiveness in a rapidly changing world. The rising importance of created assets indicates an important shift among the determinants of FDI.

The importance of primary infrastructure for foreign investors is based on the operational needs of prospective investments. It is well acknowledged that facilities are a crucial determinant of operational efficiency and profitability.

Cambodia is dominated by poor physical infrastructure. One frequently mentioned consideration for local accessibility to regional and national markets is the country's transportation linkages. The country lacks of good network of tarred and all weather roads. The country's seaport and transportation have suffered from the inevitable process of deterioration. The deterioration not only affects the country's physical plant but also its skilled labor force working at the seaport. This deterioration negatively impacts on foreign investment.

As more resources are invested in the infrastructure development of this country, it is highly likely that the cost of doing business in Cambodia will decrease. Especially, the cost of electricity, telecommunications and transportation will decrease over time. In order to provide foreign investors with readily available facilities, infrastructure development is essential for all round development; emphasis has been given on construction and maintenance of roads and bridges for smooth and secure transportation. With the international donor community, Cambodia should rehabilitate the infrastructure of the country because the poor infrastructure of Cambodia is a binding constraint on foreign and domestic investment.

(iv) Skilled Labor

A motivation for FDI is to lower costs through the utilization of low-cost factors of production in the host country. A host country's relative cost of its wage rate and unit-labor costs influences FDI inflows. While most analysts believe that the cost of labor reduces profitability, therefore may discourage foreign investors (Woogward and Rolfe, 1993), it is widely acknowledged that it is not the cost of labor that attracts foreign investors but the level of skills (Scheider and Frey, 1995). As more companies are shifting their sophisticated production lines to emerging markets, the cost and availability of skilled labor is becoming more important than the cost of labor in general.

For foreign investors looking at the possibility of having a future presence in Cambodia, there are several aspects of its labor force that may be considered: quality, availability, capacity, attitude and skill. While the cost of labor is low, the quality is poor. Cambodia doesn't have an efficient supply of skilled labor. In determining the availability of the labor force, that is the extent to which there are workers available for employment if new firms enter the country, we looked at the report of Economic Forum, 1997.

Due to lack of resources the region has been unable to develop comprehensive and detailed data sets on most aspects of the country's demographic, social, and economic dynamics. The country exhibits a demographic profile of a traditional less-developed society that is not favorable to investment.

The labor force in Cambodia is approximately six million. The cheap labor cost is not enough for Cambodia to attract FDI. According to the report from investors, Cambodia is lacking seriously in human resource development Most of the workers lack sufficient skill and proper talent. In order to provide efficient workers, the Government of Cambodia has to rehabilitate labor resource development for supplying the labor market. With the financial assistance from the international community, Cambodia can create human resource development centers, providing the workers with skills and talents necessary for working, such as English language, computer basics, accounting, as well as other technical knowledge.

(v) A Nation of Peace, Stability and Security

Political and security violations are a sensitive issue for FDI policy in Cambodia. Cambodia's political and security situation places constraints on investment activities as mentioned above, and FDI dropped substantially with the political instability of 1997 and has not yet fully recovered. In light of this context, peace, stability and security must be guaranteed and consolidated by the Royal Government of Cambodia. The country has to enter a new era of peace and stability, where more efforts, energy and time will be concentrated on nation building and economic development. This is the way forward for Cambodia to gain the confidence and trust of foreign investors who may consider investing in the country.

CONCLUSION

The failure of Cambodia to attract FDI is due to a number of obstacles, mainly, the public and physical infrastructure, the lack of skilled labor and an unstable political environment. FDI policy frameworks are only one determinant of the location of foreign investment. The country must also pay attention to other factors. Improvement in the quality of human resources through education and vocational training is thought to be one of the key elements in explaining the success of other countries in attracting foreign investment. Taiwan and Korea placed strong emphasis on education in the 1950s and 1960s, as had Hong Kong. These countries entered the 1970s with better-educated work forces. The country's success in implementing key structural reforms will determine the inflow of foreign investment. The experiences of other developing countries indicate that structural reform makes the single largest contribution to attracting foreign investment.

Cambodia needs the participation of the private sector to rebuild its economy following more than two decades of internal conflict, isolation and political instability. The engine of economic growth will largely depend on external resources, namely foreign direct investment (FDI). To attract FDI, the Cambodian Government has to provide the environment and climate conducive to doing business in Cambodia.

During the last decade, the Cambodian Government's attitude towards inward FDI changed from restriction and control to encouragement and regulation. Cambodia has achieved some progress in its FDI policy within a relatively short period. However, comparing its current FDI policies to internationally acknowledged investment rules, Cambodia still has a long way to go to further liberalize its FDI regime in order to attract foreign investor and benefit from FDI in the long run. The Royal Government of Cambodia should therefore work to further develop the necessary climate for promoting foreign direct investment

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