Cambodia’s Middle Income Journey: Challenges and Opportunities

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(The views expressed here are solely those of the author)

Cambodia graduates to LMIC and begins its middle income journey - close on the heels of other CLMV countries

- Per capita income now above $1000, compared to just above $200 in the mid-1990s.
- One of the few post-conflict countries around the world to achieve that feat.
- Sustained GDP growth of more than 7% a year for more than 20 years now – about to join the ‘globally coveted county club’.
- Extreme poverty is now down to negligible levels and income inequality and polarization are declining.
- People live longer, healthier, and more educated lives.
- Aspires to become an UMIC by 2030 (per capita income above $4300) and a HIC by the middle of this century (per capita income above $12,000).
- Pure arithmetics make these aspirations look hard to accomplish.
- Yet, they serve as broad goalposts/benchmarks to guide the country’s middle income journey.
- **How does that journey look like from today’s vantage point?**

Multiple dimensions of the middle income journey may make it a bumpier journey – a 'trappy' travel!

- **Sector-specific:**
  - Slowing agriculture and a stalled agricultural transformation.
  - Lack of industrial diversification – both within, and away from, garments.
  - A large, yet flagging tourism sector.
  - A slowing, yet bubbly and frothy real estate sector.
  - A growing and more interconnected financial sector.
- **Economy-wide:**
  - Aid-dependency to resource-sufficiency.
  - Rural to an urbanizing country – urban infrastructure/facilities.
  - Informal to a more institutionalized economy.
  - Quantity as well as quality-focused education and training.
- **AEC:**
  - The imperatives to travel with the other ASEAN members, learning to travel together!

- **Overall, the challenges during Cambodia's middle income journey are many but so are the opportunities!**

For fostering competitiveness, the key challenge is one of promoting a mix of imitation, improvisation, and innovation

- Revive agriculture and transfer the excess labor in the countryside for industrialization.
- Keep up the country's openness to trade, investment, and people – remain connected to compete – FDI-exports-people nexus.
- Upgrade infrastructure – maintenance as important as new constructions; IT/telecoms as important as roads, ports, airports, and power plants; and so is soft infrastructure .
- Improve the business environment/investment climate for FDI – indeed aggressively court FDI!
- Forge greater links with global supply chains and regional production networks – focus on trade in tasks than in products.
- Do not neglect services, especially tourism and hospitality.
- **In all these efforts at fostering competitiveness, imitation, improvisation, and innovation will be key, although to varying degrees at different stages and across sectors and activities.**

A ‘learning society’- germane for all - imitation, improvisation, and innovation – during the middle income journey

- Learning – both abstract learning and learning by doing – critical for skill (hard and soft) acquisition to imitate, improvise, and innovate.
- Despite recent achievements, Cambodia continues to be a labor surplus but skill deficit country.
- Options available – import skills and/or develop skills domestically.
- Public sector can finance skill development but within limits set by the fiscal space and other constraints.
- Private sector – both domestic and foreign owned – has two options.
  - A passive approach - lower its investment and production to limits set by the skill gap – prolonging/derailing the middle income journey.
  - A proactive approach – invest in skill development (including through PPPs) - enabling a successful middle income journey
- **The private sector, as much as the public sector, will thus determine the course of the country’s middle income journey – an opportunity for a truly public-private partnership!**

Providing an environment conducive for a competitive private sector – should be an overarching goal of public policy

- Private investment responds to the two 'Rs' - risks and returns.
- Yet not all combinations of the two 'Rs' may elicit sufficient private investment.
  - Non-appropriable returns.
  - Heavily time-discounted returns.
  - Unquantifiable risks.
- Private sector needs public policy support in those circumstances.
- Key public policies and interventions needed.
  - transparent and fair legal and institutional arrangements.
  - interventions to lower the time-horizon for realizing the returns by the private sector.
  - Underwriting certain private sector risks.

- **The key objective of public policy - promote an internationally competitive, not a protected, private sector.**

Public policies to be avoided or sparingly used: not-so-good ideas in development

- ’Open ended’ protection/incentives for specific sectors, industries, and firms.
- Bans on imports and exports.
- Price and interest rate controls.
- Energy subsidy, except for a well targeted poor and vulnerable.
- Premature exchange rate appreciation to promote industrial diversification to higher productivity sectors.
- Preoccupation with industrialization at the neglect of services
- Inadequate or ‘light-touch regulation of the banking/financial systems to promote financial development.
- Cutting public infrastructure investment and social spending to balance the budget.
- Job creation through civil service expansion, underpaying civil servants and teachers.
- Ignoring environmental implications of growth as an ‘unaffordable luxury’.
- **This negative list of what not to do is as important as the positive list of what to do!**

Now on to a few facts and figures about the middle income trap, who has avoided it, and who is in it…

Economies that became lower middle income after 1950 and graduated to upper middle income (Felipe 2012)

Economy	Region	Year Economy Turned LM (YLM)	Year Economy Turned UM (YUM)	Years as LM	Average GDP per Capita Growth Rate (%) (YLM to YUM)
China, People's Rep. of	Asia	1992	2009	17	7.5
Malaysia	Asia	1969	1996	27	5.1
Korea, Rep. of	Asia	1969	1988	19	7.2
Taipei,China	Asia	1967	1986	19	7.0
Thailand	Asia	1976	2004	28	4.7
Bulgaria	Europe	1953	2006	53	2.5
Turkey	Europe	1955*	2005	50	2.6
Costa Rica	Latin America	1952*	2006	54	2.4
Oman	Middle East	1968	2001**	33	2.7

*This refers to the second time Turkey and Costa Rica attained lower middle-income status. Turkey became lower middle-income in 1953 but slipped back to low income in 1954; Costa Rica became lower middle-income in 1947 but slipped back to low-income in 1950.

**This refers to the second time Oman attained upper middle-income status. It became upper middle-income in 1997 but fell back to lower middle-income in 1998.

Economies that were in upper middle income after 1950 and graduated to high income (Felipe 2012)

Economies	Region	Year Country Turned UM (YUM)	Year Country Turned H (YH)	Years as UM	Average GDP per Capita Growth Rate (%) (YUM to YH)
Hong Kong, China	Asia	1976	1983	7	5.9
Japan	Asia	1968	1977	9	4.7
Korea, Rep. of	Asia	1988	1995	7	6.5
Singapore	Asia	1978	1988	10	5.1
Taipei,China	Asia	1986	1993	7	6.9
Austria	Europe	1964	1976	12	4.1
Belgium	Europe	1961	1973	12	4.4
Denmark	Europe	1953	1968	15	3.3
Finland	Europe	1964	1979	15	3.6
France	Europe	1960	1971	11	4.4
Germany	Europe	1960	1973	13	3.4
Greece	Europe	1972	2000	28	1.8
Ireland	Europe	1975	1990	15	3.2
Italy	Europe	1963	1978	15	3.4
Netherlands	Europe	1955	1970	15	3.3
Norway	Europe	1961	1975	14	3.5
Portugal	Europe	1978	1996	18	2.8
Spain	Europe	1973	1990	17	2.7
Sweden	Europe	1954	1968	14	3.6
Argentina	Latin America	1970	2010	40	1.2
Chile	Latin America	1992	2005	13	3.7
Israel	Middle East	1969	1986	17	2.6
Mauritius	Sub-Saharan Africa	1991	2003	12	4.0

Economies in the lower middle income trap in 2010 (Felipe 2012)

Economy	Region	2010 GDP per Capita (1990 PPP $)	Years as LM until 2010	Average Growth (%) 2000–2010	Years to Reach $7,250*
Philippines	Asia	3,054	34	2.5	35
Sri Lanka	Asia	5,459	28	4.3	7
Albania	Europe	4,392	37	4.8	11
Romania	Europe	4,507	49	4.1	12
Bolivia	Latin America and Caribbean	3,065	45	1.8	49
Brazil	Latin America and Caribbean	6,737	53	2.0	4
Colombia	Latin America and Caribbean	6,542	61	2.6	5
Dominican Republic	Latin America and Caribbean	4,802	38	2.8	15
Ecuador	Latin America and Caribbean	4,010	58	2.2	27
El Salvador	Latin America and Caribbean	2,818	47	0.4	251
Guatemala	Latin America and Caribbean	4,381	60	1.1	47
Jamaica	Latin America and Caribbean	3,484	56	-0.3	-
Panama	Latin America and Caribbean	7,146	56	2.4	1
Paraguay	Latin America and Caribbean	3,510	38	1.5	48
Peru	Latin America and Caribbean	5,733	61	4.2	6
Algeria	Middle East and North Africa	3,552	42	2.2	34
Egypt	Middle East and North Africa	3,936	31	3.0	21
Iran	Middle East and North Africa	6,789	52	3.4	2
Jordan	Middle East and North Africa	5,752	55	3.5	7
Lebanon	Middle East and North Africa	5,061	58	4.1	10
Libya	Middle East and North Africa	2,924	43	2.4	39
Morocco	Middle East and North Africa	3,672	34	3.3	21
Tunisia	Middle East and North Africa	6,389	39	3.5	4
Yemen, Rep. of	Middle East and North Africa	2,852	35	0.9	109
Botswana	Sub-Saharan Africa	4,858	28	1.7	24
Congo, Rep. of	Sub-Saharan Africa	2,391	33	1.8	63
Gabon	Sub-Saharan Africa	3,858	56	0.0	-
Namibia	Sub-Saharan Africa	4,655	61	2.4	19
South Africa	Sub-Saharan Africa	4,725	61	2.0	23
Swaziland	Sub-Saharan Africa	3,270	41	2.2	37

* Number of years to reach $7250 = ln(7250/gdp2010) / ln(1 + avegr), where avegr is the average growth rate of income per capita during 2000–2010.

GDP = gross domestic product, LM = lower middle-income, PPP = purchasing power parity.

Economies in the upper middle income trap in 2010 (Felipe 2012)

Country	Region	2010 GDP per Capita (1990 PPP $)	Years as LM	Years as UM until 2010	Average Growth (%) 2000–2010	Years to Reach $11,750
Malaysia	Asia	10,567	27	15	2.6	5
Uruguay	Latin America	10,934	112	15	3.3	3
Venezuela	Latin America	9,662	23	60	1.4	15
Saudi Arabia	Middle East	8,396	20	32	0.9	37
Syria	Middle East	8,717	46	15	1.7	18

* Number of years to reach $11750 = ln(11750/gdp2010) / ln(1 + avegr), where avegr is the average growth rate of income per capita during 2000-2010.

GDP = gross domestic product, LM = lower middle-income, PPP = purchasing power parity, UM = upper middle-income.

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