

## 2016 Cambodia Outlook Conference A Partnership of CDRI and ANZ Royal

### Conference Brief

# ‘Getting Things Moving – Regional and National Infrastructure and Logistics for Connectivity, Growth and Development’

## 1. Transport infrastructure and logistics in Cambodia: Are the remarkable improvements sufficient to realise growth and development aspirations?

Cambodia’s transport infrastructure and logistics services have evolved remarkably following post-conflict rehabilitation and expansion and more recent efforts to build comprehensive and efficient infrastructure and logistics systems to move the economy onto the next stage of development. There has been remarkable progress in the development of both hard and soft infrastructure over the last two decades.<sup>1</sup> New transport corridors connect domestic markets to regional and international trade markets. The corridor linking Phnom Penh to Sihanoukville port is the main national trade route, while that linking Bangkok-Phnom Penh-Ho Chi Minh City is the main international corridor. Most of the infrastructure performance indicators in the World Development Indicators (e.g. access to and consumption of electricity, paved roads, mobile phone and internet users, quality of trade and transport-related infrastructure) have improved. Even more impressive is the jump in Cambodia’s ranking in the World Bank’s Logistics Performance Index<sup>2</sup> to 83 in 2014, up 46 places up from 2010.

1 RGC. 2013. Rectangular Strategy for Growth, Employment, Equity and Efficiency Phase III; MOP. 2014. National Strategic Development Plan 2014-2018.

2 <http://lpi.worldbank.org/>

**Transport networks and logistics services are inadequate to meet the demands of the next development stages.**<sup>3</sup> The Industrial Development Policy (IDP) 2015-25 highlights five key obstacles to industrial sector development, one of which is inadequate transport and logistics capacity. Various CDRI studies<sup>4</sup> have drawn a similar conclusion, that the development of Cambodia’s transport and logistics sectors is lagging behind its growth aspirations. Public investment in infrastructure remains low. Major national roads and international highways connecting Cambodia to neighbouring countries may be in good shape, but roads linking rural areas to major cities and urban transport systems are not well developed. Inland waterway transport has been neglected despite its potential to lower transport costs and expand transport capacity. Low traffic demand aside, the railway system is a weak link in Cambodia’s regional connectivity. Port efficiency has improved, but shipping costs remain high.

3 Infrastructure and Regional Integration Technical Working Group (IRITWG). 2015. *Overview of the Transport Infrastructure Sector in the Kingdom of Cambodia*. 5<sup>th</sup> Edition. Phnom Penh: RGC.

4 Cambodia Development Resource Institute. 2013. *Cambodia’s Development Dynamics: Past Performance and Emerging Priorities*. Phnom Penh: CDRI; Hing Vutha. 2013. *Leveraging Trade for Economic Growth in Cambodia*. Working Paper Series No. 81. Phnom Penh: CDRI.

**Transport network quality and connectivity are trailing behind regional averages.** The Global Competitiveness Report 2014 gave Cambodia an overall infrastructure ranking of 104, significantly lower than Vietnam (81) and Thailand (48). As a result, logistics costs in Cambodia are almost double those in neighbouring countries. A time-cost survey by the Asian Development Bank (ADB)<sup>5</sup> on transporting “normal” goods from Bangkok to Phnom Penh and from Phnom Penh to Ho Chi Minh City revealed that the average logistics cost for the Cambodian section is USD0.20/t/km from Bangkok to Phnom Penh compared with USD0.09 in the Thai section, and USD0.19/t/km from Phnom Penh to Ho Chi Minh City compared with USD0.10 in the Vietnamese section. Poor logistics performance largely stems from insufficient and poor quality infrastructure; institutional inefficiency of customs clearance processes (speed, simplicity and predictability); and a lack of integration of logistics services with neighbouring countries.<sup>6</sup> The logistics sector has developed rapidly but only a limited number of domestic firms can offer a comprehensive range of logistics services, with the sector dominated by a few buyer-appointed multinational carriers. The ADB survey also identified the issue of insufficient competition in trucking, port and air freight. Lack of logistics professionals is also a major problem for the sector.

**Cambodia is committed to developing a multimodal transport network and a vibrant logistics system.** Cognisant of the importance of transport and logistics in driving the next stage of development, government has identified the sector as one of the four key pillars of Rectangular Strategy III. Government is committed to continuing investment in transport infrastructure and improving trade facilitation aimed at developing a vibrant logistics system and a multimodal transport network to ensure connectivity within the country, within the region and with the rest of the world. In addition, government continues

5 ADB. 2012. *Trade and Trade Facilitation in the Greater Mekong Subregion*. Manila: ADBI.

6 Julian Latimer Clark and Sok Vannara. 2013. *Getting Things Moving! Improving Cambodia’s Logistics to Benefit Fully from Regional Growth*. Issue Sheet, Trade Development. Washington, DC: World Bank.

to give high priority to expansion of low-cost energy production and distribution networks aimed at ensuring available, reliable, accessible and affordable energy to meet development needs. Priorities in the National Strategic Development Plan 2014-18 include the design and implementation of a Master Plan for Transport Infrastructure Development. The Plan will connect all parts of the country with neighbouring countries through developing multimodal and cross-border transport links and efficient logistics services. The expected outcomes from continued infrastructure investments are (1) lower transport costs, (2) improved reliability and efficiency, (3) strengthened competitiveness, and (4) increased investment and trade.

**Trade enabling infrastructure is critical for connecting Cambodia to emerging regional production networks.** At the core of IDP 2015-25 is industrial infrastructure development, whereas the Cambodia Trade Integration Strategy 2014-18 focuses more on trade logistics improvement. Trade logistics improvement is critical for Cambodia to participate fully in the production networks that are developing in Southeast Asia. Key measures include creating national logistics plans and linking them to existing ASEAN frameworks, accelerating implementation of the Cross-Border Transport Agreement and improving transport regulations. The latest overview of the transport sector<sup>7</sup> draws similar conclusions, that the rapid growth of garment factories and other industries inside and outside Cambodia’s special economic zones indicates the need for infrastructure investment to ensure timely and cost-efficient shipping.<sup>8</sup> Customs administration reform has strengthened clearance processes and reduced offences, including illegitimate trade and informal payments. The soon-to-be implemented National Single Window (NSW) will provide standardised information and documents that need only be submitted

7 IRITWG (2015). *Overview of the Transport Infrastructure Sector in the Kingdom of Cambodia* (5th Edition). Phnom Penh, Infrastructure and Regional Integration Technical Working Group; RGC (2013)

8 IRITWG. 2015.

once at a single entry point to fulfil all import, export and transit-related regulatory requirements. The NSW will then connect with the planned ASEAN Single Window to support integration and connectivity across ASEAN member states.

## 2. What do we need to do, why and how?

Cambodia needs to develop its transport and logistics sector to ensure regional and global connectivity to trading platforms and market gateways. Quality infrastructure is vital for economic growth and competitiveness. On average, a 1 percent increase in the stock of infrastructure directly contributes a 0.08 percent increase in GDP.<sup>9</sup> The quality and extensiveness of local transport and logistics systems reduce the effect of distance between regions, integrating and connecting the national market at low cost with markets in other countries.

Quality transport and logistics also play a role in attracting investment and promoting industrialisation and exports. Improvements in infrastructure also have a positive impact on social development such as education, public health and community capacity. For the transport and logistics sector to serve the country's growth aspirations, physical and institutional infrastructure, cooperation frameworks and logistics skills need to be further developed. This can be achieved through:

- **Intensive and consistent investment in transport infrastructure.** Massive investment is needed for infrastructure to keep pace with economic growth. An earlier ERIA report suggested that between 2013 and 2022 this would require investments of USD12 bn to USD16 bn.<sup>10</sup> Investment should support the development of multimodal and cross-border transport links, and efficient and competitive logistics services. Efforts should focus on developing the railway sector, developing airport and seaport infrastructure, assessing

the potential for inland water transport, breaking monopoly control over transport services and intensifying implementation of cross-border agreements and protocols. More specifically, Cambodia needs to improve and maintain provincial and rural road networks to ensure better linkages and access to industrial areas. Also required is the upgrading of national highways such as National Roads 1, 4, 5 and 6 and the building of an expressway to link Ho Chi Minh City, Phnom Penh and Sihanoukville port.<sup>11</sup> The railway system, the weakest link in the country's regional connectivity, needs to be repaired and extended to connect Cambodia with Thailand and Vietnam. While Vietnam and Thailand rely on inland waterways for low-cost transport of major crops, Cambodia has largely neglected its inland water transport sector. In tandem with expanding the new port in Phnom Penh, there are clear logistics costs and efficiency gains to be realised by building river ports along the Mekong River where ships can load and unload cargo. Essential transport services should be linked to special economic zones and other industrial hubs.<sup>12</sup>

- **Creation of a National Transport and Logistics Master Plan and Task Force.** International experience suggests that countries with national logistics plans have significantly better logistics performance. Yet Cambodia does not have a comprehensive transport and logistics policy nor a central body to plan, implement and monitor the sector's performance. Indonesia, Malaysia, Thailand and, to some extent, Vietnam have put in place logistics development policies, while Cambodia pursues segmented policies with strong emphasis on infrastructure development. Thailand's logistics development strategy, for example, has three broad objectives: increase supply chain competitiveness, enhance trade facilitation and develop logistics capacity. The Thai National Logistics Council was established and chaired by the prime minister, with as its secretariat the National Economic

9 UNESCAP. 2014. *Regional Connectivity for Shared Prosperity*. Bangkok: United Nations.

10 <https://www.cambodiadaily.com/archives/call-for-more-investment-in-infrastructure-33737/>.

11 IRITWG. 2015.

12 Ibid.

and Social Development Board which comprises agencies from ministries related to economic activities and business associations. After the release of the Investment Climate Assessment 2014 Report<sup>13</sup> it was proposed that Cambodia create a trade logistics blueprint as policy direction and a national logistics taskforce as the coordinating body. Similarly, the Infrastructure and Regional Integration Technical Working Group (IRITWG) recommended the establishment of a coordinating mechanism to plan and develop a multimodal transport and logistics system that will seamlessly link between local industrial hubs and the region.<sup>14</sup>

- **Encouragement of more logistics service providers and innovation.** Despite rapid development, few domestic service firms can offer a comprehensive range of logistics services. As a result, there is a lack of healthy competition in trucking, sea and air freight services.<sup>15</sup> Lack of logistics professionals is another major problem for the sector. These limitations jeopardise the country's efforts to develop an integrated transport and logistics system. Singapore, which ranks top in infrastructure and logistics by several international assessments (e.g. Logistic Performance Index and Global Competitiveness Index), has over 7000 logistics companies with over 180,000 employees<sup>16</sup> and many qualified logistics professionals. In addition, logistics research and development centres promote innovation and creativity. Cambodia should consider creating institutions that specialise in transport and logistics.
- **Reform and modernisation of import, export and transit operations.** Complex customs formalities including paperwork, clearance, regulations and fees remain

a key impediment to exports.<sup>17</sup> More attention must be paid to supportive soft infrastructure and logistics efficiencies. Improvements can be achieved through the elimination of all forms of informal fees, reform and modernisation of customs, wider information sharing and integration in regional road transport markets.

### 3. How can infrastructure and logistics development be financed? Some options to consider

There are various ways to finance infrastructure projects. National budgets, domestic and foreign loans and official development assistance are the traditional sources. However, these types of finance have dwindled over the past few decades; and public capital investment in infrastructure on average has declined in OECD countries.<sup>18</sup> Financing trends are more diverse with more focus on public-private partnerships (PPPs) and private investment and ownership.<sup>19</sup> Cambodia might consider the following potential sources of infrastructure financing:

- **Public-private partnerships.** PPPs allow governments to expand the provision of services by using market tools, rather than publicly provided and managed facilities<sup>20</sup>. Restricted budgets, ineffective public spending control and inefficient infrastructure management have led governments to consider the need to shift investment efforts to the private sector<sup>21</sup>. As in South Korea during the 1990s, for

13 ADB; World Bank. 2015. *Cambodia's Investment Climate Assessment 2014: Creating Opportunities for Firms in Cambodia*. Phnom Penh: World Bank.

14 IRITWG. 2015.

15 ADB 2012.

16 2013. "Logistics Sector in Singapore." Accessed 5 Feb 2016. <http://singapore.nlembassy.org/doing-business/priority-sectors/logistics/logistic-sector-in-singapore.html>.

17 ADB. 2012. *Trade and Trade Facilitation in the Greater Mekong Subregion*. Manila: ADB; World Bank (2015)

18 R.D. Croce and S. Gatti. 2014. "Financing Infrastructure - International Trends." *Financial Market Trends* 1:123-138.

19 D.H. Brooks and F. Zhai. 2008. "Infrastructure Financing: Impacts on Macroeconomic Balances." In *Infrastructure and Trade in Asia*, edited by D.H. Brooks and J. Menon. London: Edward Elgar.

20 ADBI, and ADB. 2012. *Infrastructure for Asian Connectivity*. Cheltenham: Edward Elgar Publishing Limited.

21 R.D. Croce and S. Gatti. 2014. "Financing Infrastructure - International Trends." *Financial Market Trends* 1:123-138.

example, the government introduced private sector participation in infrastructure investment through supportive policies. The PPP market in South Korea has since grown and developed into a highly profitable financial market.<sup>22</sup> The Cambodian government is already using this model in a number of infrastructure projects. Given that government and development partners cannot generate the huge investment capital required for infrastructure development, PPPs are a viable source of financing. The key to their success, however, is a conducive policy environment and transparent public procurement and partnership procedures.

- **Regional and sub-regional mechanisms.** Cambodia is a party to the Master Plan on ASEAN Connectivity (MPAC) which aims to enhance the region's physical infrastructure, institutions and people-to-people relations. The MPAC has identified projects and determined possible funding sources to support them, and created the ASEAN Infrastructure Fund. Despite difficulties in mobilising funding, the MPAC remains relevant and can support Cambodia's infrastructure plans to connect with neighbouring countries. At the subregional level, Cambodia has benefited significantly from the Greater Mekong Subregion (GMS) transport development program. For example, the improvement of National Roads 1 and 5 and the completion of Tsubasa Bridge, which now form part of the Southern Economic Corridor linking Bangkok, Phnom Penh and Ho Chi Minh City. The GMS will continue to be a main source of financing for Cambodia's infrastructure upgrading.
- **The Asian Infrastructure Investment Bank.** The AIIB, initiated by China but now with broad international partnership, including Cambodia as a founding member, is a major new regional response to the huge need for infrastructure development and financing in the region, with a capital

base of USD100 bn. For Cambodia, it will be important to establish how the AIIB can support national and regional (GMS, ASEAN and beyond) infrastructure development and connectivity as both a new source of funding and provider of much needed expertise. This is especially important in improving and expanding connectivity between China and ASEAN member states.

#### 4. What are some key success factors for Cambodia's infrastructure and logistics development?

Learning from international success stories in infrastructure development, some major factors for Cambodia to consider in its future infrastructure development might be:

- **Strong vision and commitment.** Efficient infrastructure development requires that governments formulate a concrete vision for the infrastructure system which serves the best interests of comprehensive socioeconomic development planning. As well as a long-term master plan, a strong leading institution to coordinate infrastructure planning and development is necessary, and a culture of coordination and cooperation between relevant ministries and agencies in close engagement and cooperation with the private sector.
- **Transparency and quality control.** Decision-making processes for infrastructure investment usually face considerable political pressures. Transparency and professional expertise in regulatory decision-making are necessary to mitigate these pressures. This is particularly important in tendering and selection processes for major infrastructure projects as there is much international evidence that a lack of genuinely competitive procurement procedures is a major factor in the failure of PPPs.<sup>23</sup>

<sup>22</sup> Kim Jay-Hyung and Choi Seokjoon. 2011. *Public-Private Partnership Infrastructure Projects: Case Studies from the Republic of Korea*. Manila: ADB.

<sup>23</sup> V. Cuttaree. 2008. *Successes and Failures of PPP Projects*. Washington, DC: World Bank; J. Woetzel, O. Tonby, P. Burt and G. Lee. 2014. *Southeast Asia at the Crossroads: Three Paths to Prosperity*. McKinsey Global Institute; RGC. 2013.

- **Private sector participation in infrastructure development.** The key to successful infrastructure development in many countries is the ability to attract private investment in major infrastructure projects. This requires not only an effective and supportive institutional environment but strong regulatory frameworks and public procurement regimes with high standards of transparency and accountability.

## 5. Some policy questions to consider

In meeting the needs and challenges for transport and logistics development, Cambodia might consider some broad policy questions:

- What types of infrastructure, transport and logistics systems would best serve Cambodia and its next stage of development to promote growth and connectivity, improve regional and global competitiveness, and support national socioeconomic goals?
- How can cross-ministerial and agency coordination and cooperation under Cambodia's Industrial Development Policy (IDP), and other major policy mechanisms, be improved and fast-tracked to achieve broad IDP and specific infrastructure and logistics goals?
- Which model of national institutional frameworks would best serve Cambodia's infrastructure, transport and logistics development needs? Would a National Transport and Logistics Taskforce, comprising government, private sector and expertise, be a useful and feasible mechanism for improving policy coherence and coordination in achieving national goals?
- How can Cambodia best utilise the opportunity presented by the establishment of the Asian Infrastructure and Investment Bank (AIIB) while continuing to benefit from partnership with existing multilateral and bilateral development agencies and financial institutions?

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