A STUDY OF CHINESE CAPITAL FLOWS TO SIX COUNTRIES: **CAMBODIA**

Mitigating Governance Risks From Investment in Southeast Asia

CENTER FOR INTERNATIONAL PRIVATE ENTERPRISE

JANUARY 2020

TABLE OF CONTENTS

FORWARD & INTRODUCTION

Forward

CIPE works at the intersection of economic development, democracy and human rights, a unique position from which to address governance challenges posed by high-risk capital flows. In recent years, CIPE and its partners have witnessed an alarming trend: large amounts of capital invested by authoritarian regimes flowing through opaque channels into emerging markets. In these markets where governance is already weak and corruption is already rampant, high risk capital creates political and economic distortions which often do more harm than good in the recipient country. CIPE coined the term corrosive capital to describe state-backed financing that lacks transparency and accountability flowing from authoritarian states into new and fragile democracies.

CIPE's approach to combatting the effects of corrosive capital centers on identifying specific governance gaps in countries where democratic processes are at risk. Then, working with local partners, we design and implement projects that help close these gaps, fostering collaboration and information sharing among civil society, the private sector, and lawmakers. Because the adverse governance impacts in countries that receive this capital are well-documented and the global flows of such capital are growing

exponentially, CIPE is currently expanding both its policy research and programming on corrosive capital.

This report is unique in a number of ways: (1) it presents invaluable local perspectives on how Chinese investments are being documented, perceived, and implemented in countries around the world; (2) it identifies governance gaps which permit capital inflows to exploit or exacerbate weakness in young democracies; and (3) it provides recommendations for local stakeholders to address these gaps and make the most of Chinese investments. This publication is a demonstration of CIPE's commitment to the principles of local ownership, inclusion, learning & innovation, and accountability which are essential for emerging economies to enjoy sustainable and inclusive growth.

The report represents a group effort by CIPE and its partners. The effort grew out of a long-running dialogue on Chinese investment in Southeast Asia. CIPE partners cited a lack of data and consistency in the existing literature on the governance effects of Chinese state-backed debt and investment in emerging Asian markets. This report aims to fill that information gap and illuminate the governance distortions engendered by corrosive capital.

The first step in this effort was a set of deep-dive country-specific assessments. CIPE partnered with five think tanks and three independent researchers based in Southeast Asia to systematically study the issues. In addition, CIPE commissioned the Rhodium Group to collaborate with our partners in the development of a comprehensive dataset to track Chinese direct investments flowing into Southeast Asia.

It is CIPE's hope that this publication equips donors, implementers, policymakers, and advocates with information that makes their work more effective at managing the risks of corrosive capital. By mitigating the risks of corrosive capital, the targeted investments of CIPE's ongoing program can achieve a larger scale and aggregate impact on the resilience of markets and democracies in the face of capital flows from nondemocratic countries.

Andrew Wilson

EXECUTIVE DIRECTOR
CENTER FOR INTERNATIONAL PRIVATE ENTERPRISE

Introduction

Chinese outward investments have increased substantially in recent years, especially after 2013's introduction of its Belt and Road Initiative (BRI). BRI is the most ambitious infrastructure investment effort in recent history. The effect of BRI in Southeast Asia has been a tremendous volume of capital rushing in over a very short period of time. Chinese capital (including foreign direct investment, aid, and commercial loans) offers many benefits. It contributes to economic growth, job opportunities, and better-connected infrastructure networks in local economies. However, a growing volume of evidence indicates that many forms of capital emanating from authoritarian nations have a corrosive effect on democratic institutions and private enterprise in recipient countries.

The genesis of this publication was a CIPE forum in December 2017 at which CIPE's Southeast Asian partners expressed the urgent need to fill the information gap of the impact of corrosive capital on governance distortions. Local researchers and analysts across the region have identified an absence of evidence in the existing body of work on Chinese investment projects and the impact on the local economies and communities. Additionally, researchers and scholars sought greater clarity on specific gaps in governance through which Chinese capital can flow.

This report analyzes the patterns, trends, and characteristics of Chinese investments in Southeast Asia. Against the backdrop of the rising flood of Chinese investment across the region, the report highlights common issues and shared governance risks across countries, and identifies questions requiring further study. The sizable economic interests and political intricacies of China and BRI make this research sensitive in some countries; as result, some information has been redacted from the final report.

Countering corrosive capital requires working closely with local partners in vulnerable countries. In each case, the specific governance gaps which place democratic institutions at risk must be identified. In cooperation with local partners, CIPE can then design and implement local projects to help close those gaps and reinforce democratic institutions by fostering collaboration and information sharing among civil society, the private sector, and lawmakers.

Objectives, Scope & Methodology of the Report

This report aims to answer an important policy question: How can Southeast Asian economies benefit from the Chinese investment while mitigating the associated risks? This report will provide authoritative

and up-to-date data on Chinese regional FDI and loans in chapter 1; the following seven chapters document different forms of Chinese capital flows and identify governance gaps in six countries. Chapter 2 presents the case of Malaysia which highlights issues of opaque procurement practices associated with Chinese mega projects, as well as the need to improve corporate governance of state-owned enterprises to avoid conflict of interest. In chapter 3, Chinese investments are involved in controversial price fixing in the Indonesian extractives industry. Chapter 4 demonstrates the development of evolved oversight mechanisms to screen infrastructure projects in Myanmar. In Chapter 5, Cambodia provides an illustration of what can happen in a small to mid-sized country that becomes overly dependent on Chinese investment. In Chapter 6, the authors raise environmental concerns in Vietnam. Chapter 7 discusses regulatory capture issues in the Philippines using the online gambling industry as an example. Looking into the fast-growing Fintech industry, chapter 8 showcases risky investments and the data abuse problem in Indonesia. In all the case studies, authors examine the macro-level impact of Chinese investment, identify governance gaps, assess its initial impact. They then develop policy recommendations for key stakeholders such as businesses, governments, civil society organizations and international organizations to address these challenges and develop a streamlined, transparent, foreign investment monitoring and management process.

The scope of this report is primarily Foreign Direct Investment (FDI) from the People's Republic of China. During the research process, some authors discovered that domestic controversy centered primarily on Chinese commercial loans funding large infrastructure projects. The capital discussed in this report therefore encompasses all investments from China. Some authors focus on FDI while others place greater emphasis on other official financing such as aid and loans.

CHINESE INVESTMENTS IN CAMBODIA: MINDING THE GOVERNANCE AND ECONOMIC GAPS

CHHEANG VANNARITH (ASIAN VISION INSTITUTE [AVI])

Introduction

The flow of Chinese foreign direct investment (FDI) to Cambodia has significantly increased in the past few years, especially in the field of infrastructure development. Robust governance reforms and gradual economic diversification have enabled Cambodia to better attract investment from abroad. At the Government-Private Sector Forum held in Phnom Penh in March 2019, the government laid out new commitments and concrete reforms to reduce the cost of FDI-related production and logistics (Vannarith, 2019b).The Belt and Road Initiative (BRI) and Lancang-Mekong Cooperation (LMC) further facilitated the flow of Chinese investment.

This chapter provides an overview of Cambodia's economic development, bilateral relations between Cambodia and China, and discusses the impacts and perceptions of Chinese investments in Cambodia. These key issues will be discussed through the lens of public procurement issues and a case study in Sihanoukville.

An Overview of Cambodia's Economic Development

Cambodia has experienced high economic performance over the past two decades, with

an average annual growth rate of 7.7%. In 2018, the growth rate remained at 7.5%. High growth has been primarily driven by rapid expansion of exports as well as robust internal demand, along with a surge in FDI (World Bank, 2019). The contribution of exports to Cambodia's GDP has gradually increased from 50.6% of GDP in 2017 to 53.5% in 2018 and an estimated 54.8% in 2019. Imports have similarly increased their share from 69.9% of GDP in 2017 to 76.3% in 2018 and estimated 76.7% in 2019. The main export products are garments (66.4%) and footwear (9.7%) (National Bank of Cambodia, 2019).

Cambodia has shown improvement in other indicators as well. The poverty rate fell from 53% in 2004 to 13.5% in 2014 and is expected to have dropped below 10% in 2019. Health and education have made remarkable progress despite certain issues that still require government attention (Sen, 2019). Foreign direct investment has increased over the years. FDI is estimated to have reached a record high of more than USD 3 billion, or 12.6% of GDP in 2018 (World Bank, 2018). Burgeoning exports and strong FDI inflows have contributed to further accumulation of gross international reserves, which in 2018 reached USD 10.1 billion (World Bank, 2019).

With its relatively young workforce: 70% of the total population under 35 years old, Cambodia has great potential to continue its climb up the development ladder.

Cambodia's development vision is to become a higher-middle-income country by 2030 and high-income country by 2050. The 2015-2025 Industrial Development Policy adopted in 2015 has become a roadmap for expanding industrialization's scale and scope in Cambodia. The policy aims to promote the country's industrial development to maintain high, sustainable, and inclusive economic growth through economic diversification, strengthened competitiveness, and greater productivity. However, the policy has not delivered expected results due to policy and coordination failures. For example, the policy has not provided a coordinated program of concrete, time-bound targets for investment projects in the various sectors and subsectors of Cambodia's economy (Kimlong, 2019b).

The Rectangular Development Strategy (2018-2023) is the core development policy of the country, focusing on four priority areas. First, *human resource development* focuses on improving the quality of education, science, and technology; providing vocational training; improving public healthcare and nutrition; and strengthening gender equality and social protection. Second, *economic diversification* focuses on improving logistics and enhancing transport, energy, and digital connectivity; developing key and new sources of economic growth; encouraging readiness for the transition

to a digital economy and the "industrial revolution 4.0;" and promoting financial and banking sector development. Third, *private sector development* concentrates on job market development, entrepreneurship, and SME development, and public-private partnerships. Fourth, *inclusive and sustainable development* focuses on agricultural and rural development; sustainable management of natural and cultural resources; management of urbanization; and promoting sustainability and adaptation to climate change.

Regional integration is one of the key components of Cambodia's development strategy. The country has adopted a proactive regional integration scheme, which is chiefly shaped by economic pragmatism, referring to the alignment of foreign policy with economic interests (Vannarith, 2019a). Aiming to become a bridging state in ASEAN and the Mekong Region, Cambodia is advancing an inclusive, open, and rules-based multilateral system. Prime Minister Hun Sen stated in April 2019 that ASEAN has contributed to Cambodia's economic development in many ways. ASEAN has become the third largest export market for Cambodian products, after the European Union and the United States. The share of Cambodia's trade volume with other ASEAN Member States increased from a mere 4 percent in 1999 to more than 20 percent in 2018. ASEAN is also one of the top investors in Cambodia. ASEAN member states accounted for 22% FDI inflows in 2017 and 25% in 2018 (Vireak, 2019b). Within ASEAN, Thailand, Vietnam and Malaysia are the three top investors in Cambodia (MFAIC).

After implementing an opening-up policy in the early 1990s and becoming a member of ASEAN in 1999, Cambodia adopted a free-market economy and took an active role in regional integration. Cambodia's investment regime is relatively liberal and open compared with other ASEAN economies. Investment incentives are attractive to foreign investors, offering benefits such as 100 percent foreign ownership, corporate tax holidays of up to eight years, duty-free import of capital goods, and no restrictions on capital repatriation. Cambodia's current Law on Investment specifies a number of incentives, especially tax incentives, for investors (CDC).

In addition, the Cambodian government has been improving its investment facilitation services. For example, the Government decided in 2005 to establish the Cambodian Special Economic Zone Board (CSEZB) under the Council for Development of Cambodia (CDC) to promote the special economic zone (SEZ) scheme in Cambodia. Administered by the CSEZB, the Special Economic Zone Administration is to be established in authorized SEZs and is expected to provide one-stop service to zone investors from the registration of investment projects to routine

export-import approvals (CDC). However, challenges and obstacles affecting foreign investment remain, particularly bureaucracy in business registration, inconsistency in policy coordination, and weak regulatory enforcement (Kimlong, 2019b).

Between 2015 and 2018, average annual foreign direct investment in Cambodia amounted to USD 5.2 billion, Special Economic Zone (SEZ) investment accounted for USD 331 million (15.8 percent). In 2018, total FDI capital totaled USD 6.45 billion, with investment primarily directed into infrastructure (USD 2.09 billion), industry (USD 1.38 billion), tourism (USD 816 million), services (USD 782 million), hotels (USD 692 million), and agriculture (USD 444 million). China has been a key investor in Cambodian SEZs overall.

Japan and South Korea have also invested in Cambodian infrastructure, but this has declined in recent years. In 2015, the difference between Chinese, Japanese and South Korean investment was stark. Chinese business had the largest influence in Cambodia with 1,055 companies having a presence in the country, followed by South Korea at 278 companies. Japan ranked third with 250 companies and comprised USD 56.7 million out of the total USD 4.6 billion FDI for that year (Kea, 2016) (Table 1, PG. 86 and Table 2, PG. 87).

An Overview of Sino-Cambodian Relations

Cambodia is generally perceived as the closest friend of China in Southeast Asia. There were three main critical development

TABLE 1: Investment Trends 2015-2018 (Million USD)

YEARS	TOTAL INVESTMENT	NON-SEZ INVESTMENT	SEZ INVESTMENT
2015	4,643.50	4,528.90	114.60
2016	3,609.55	3,326.30	283.25
2017	6,332.00	5,847.00	485.00
2018	6,451.52	6,009.46	442.06

SOURCE: Council for the Development of Cambodia

TABLE 2: Investments by Sector 2018 (Million USD)

SECTOR	INVESTMENT
Infrastructure	2,087.29
Industries	1,375.57
Tourism	816.79
Services	782.86
Hotel	692.02
Agriculture	444.18
Garment	223.93
Building Material	58.37
Energy	58.23
Bags	50.53
Shoes	40.97

SOURCE: Council for the Development of Cambodia

points in this relationship. China offered strong diplomatic and economic support to Cambodia in the aftermath of the violence in July 1997, to counter the pressures from the U.S. and other Western countries on Cambodia. In 2010, a comprehensive strategic partnership agreement was signed to advance the bilateral relationship in all fields. In 2016, during President Xi Jinping's state visit to Cambodia, China called Cambodia an "ironclad friend." (FMPRC).

The bilateral relationship reached its peak in April 2019 when the two countries signed the Action Plan for Forging the Cambodia-China Community of Shared Future (2019-2023)

covering five key areas: political cooperation, security cooperation, economic cooperation, cultural and people-to-people cooperation, and multilateral cooperation. Under the pillar of economic cooperation, both sides agreed to continuously expand trade volume and realize the goal of USD 10 billion bilateral trade volume by 2023. Bilateral trade volume increased from USD 5.16 billion in 2016 to 6.6 billion in 2018 (Table 3, PG. 88). The main products that Cambodia exports to China are milled rice, cassava, pepper, cashew nuts, sugar, and apparel., The main products that Cambodia imported from China are mostly raw garment materials, machinery, vehicles, foodstuffs, electronics, medicines and cosmetics (Xinhua, 2019).

Both sides are committed to further raising the scale and level of Chinese investment in Cambodia, with a focus on enhancing investment cooperation in agriculture, industry (mainly textile, agro-industry, and rice milling), infrastructure, construction, energy (mainly hydropower plants and coal energy), and tourism. Annual investment flows from China increased from USD 985 million in 2016 to USD 3.59 billion in 2018 (See Table 3). Over the 1994-2017 period, the total fixed investment from China was USD 12.6 billion, accounting for 20.2 percent of total investment in Cambodia. The Rhodium Group calculates that the cumulative gross value of Chinese FDI transactions throgh 2017 (including acquisitions and greenfield projects) in Cambodia is USD 7 billion. The top investment sectors are transport, utilities, infrastructure, real estate, and energy. In 2018 alone, China invested USD 2.69 billion in Cambodia. While it is not certain that China will continue to invest in the creation of dams in Cambodia, Chinese investment in hydropower plants is remarkable, accounting for USD 2.36 billion (Table 4, PG. 89). In fact, an estimated 80 percent of power produced in Cambodia comes from

TABLE 3: Trade and Investment (Million USD)

	2016	2017	2018
Bilateral Trade Volume	5,160	5,577	6,600
China’s Investment Capital	985	1,656	3,594

SOURCE: Ministry of Commerce and Council of Ministers of Cambodia

TABLE 4: Chinese Investment in Hydropower

NAME OF PROJECT (COMPLETED)	SIZE (MW)	INVESTMENT CAPITAL (MILLION USD)
Kirirom 1	12	26.00
Kirirom 3	18	47.10
Kamchay	194	280.54
Atay	120	199.97
Russey Om	338	485.76
Tatay	246	540.00
Lower Sesan 2	400	781.52
TOTAL	1,328	2,460.89

SOURCE: Ministry of Foreign Affairs and International Cooperation of Cambodia

projects undertaken by either state-owned or government-linked Chinese companies (Khmer Times, 2019a).

SIHANOUKVILLE CASE STUDY

The Sihanoukville Special Economic Zone (SSEZ) is a landmark project under the Belt and Road Initiative (BRI) and aims to create an ideal trading platform for export-oriented industries under the slogan "Investment in ASEAN, radiation to the world." (SSEZ.com) Currently, the Sihanoukville Special Economic Zone, an economic and trade cooperation zone constructed by Chinese and Cambodian companies, aims to attract 300 enterprises, which would employ about 100,000 workers. The zone currently has 161 companies, with registered capital of around USD 918 million and a labor force of 22,495, according to a statement released in January by the Council for the Development of Cambodia (Hong, 2019).

Both Cambodia and China agreed to jointly promote the implementation of major

investment projects such as the SSEZ, Phnom Penh-Sihanoukville Expressway, and Siem Reap Angkor International Airport. They will also to provide more preferential policies for the development and operation of the SSEZ while supporting the SSEZ in completing the construction of its supporting industry chain. Both parties were committed to creating a better environment for the SSEZ and to encourage pragmatic cooperation between Cambodia and China. The Cambodian side also aspired to improve the investment environment to further facilitate Chinese enterprises' business in Cambodia.

In the Sihanoukville case, it can be argued that the negative impacts on the local community and the environment outweigh the benefits arising from the influx of Chinese investment projects in the area. Chinese nationals own more than 90% of businesses in Sihanoukville. Chinese investment projects and companies have few economic links and little technology and knowledge transfer with local Cambodian enterprises. Other negative impacts stemming from the influx of Chinese investment include increasing instability in Sihanoukville due to negative public perceptions of Chinese activities, increases in living costs, and environmental degradation.

BELT AND ROAD INITIATIVE IN CAMBODIA

The BRI is complementary to Cambodia's national development strategy of strengthening the country's economic competitiveness by diversifying sources of growth and expanding Cambodia's economic horizon. Cambodia-China cooperation under BRI focuses on seven areas, namely infrastructure, agriculture, capacity building, special economic zone development, culture and tourism, finance, and eco-environmental protection (Vannarith, 2017).

There are no standard criteria of what constitutes a BRI project in Cambodia. In many cases, the designation depends on a political decision (Table 5, PG. 91, for the major projects under the BRI in Cambodia). In March 2019, state-owned construction company China Road and Bridge Corporation committed to building Cambodia's first expressway connecting the capital of Phnom Penh to coastal Sihanoukville province. The 190-km expressway will cost USD 2 billion under a Build-Operate-Transfer (BOT) agreement. This is one of the key mega infrastructure projects under the BRI.

China is also one of Cambodia's key development partners. From 2013 to 2018, China provided a grant of 6.31 billion

Yuan (about USD 1 billion). In 2019, China pledged 4 billion Yuan (about USD 600 million) in a three-year project grant. In terms of concessional loans, China provided concessional loans of about USD 1.35 billion for the period 2016 to 2018. In terms of physical infrastructure development, China has built 29 roads with a total length of 2,900 km. China has also built 7 bridges with a total length of 6,824 km. In the 2016 to 2019 period, China has provided scholarships to 849 Cambodian students (MOFAIC). China also promised to import more rice from Cambodia, with the aim to import 400,000 tons per year and to support Cambodia in the face of the threat from the European Union to revoke Everything-but-Arms (EBA) preferential trade treatment from Cambodia (Al-Jazeera, 2019).

Enabling Factors for Chinese Investments to Cambodia

Chinese investments to Cambodia have been facilitated by deep mutual political trust, stable macroeconomic conditions, market access, low labor costs, and relatively easy access to land and other natural resources. The bilateral agreement on the protection and promotion of investment that came into force in August 1999 provided a legal framework to facilitate Chinese investment in Cambodia. Currently, the two countries are in the process of negotiating a bilateral free trade agreement that aims to further promote trade and investment. In 2010, China and Cambodia signed a landmark Comprehensive Strategic Partnership Agreement to advance their bilateral ties.

TABLE 5: Major BRI projects in Cambodia

NAME OF PROJECT	AMOUNT OF INVESTMENT
Sihanoukville Special Economic Zone	USD $918 million (joint private investment by Chinese and Cambodian enterprises)
Phnom Penh-Sihanoukville Expressway	More than USD $2 billion (public-private partnership)
New Siem Reap International Airport	USD $1 billion (public-private partnership)
Lower Sesan 2 Dam	USD $781.52 million (joint investment by a Chinese SOE and Cambodian enterprise)

This was the first strategic partnership agreement that Cambodia had ever signed with an external partner.

The establishment of the ASEAN-China Free Trade Agreement in 2010, the launching of the Belt and Road Initiative (BRI) in 2013, and the creation of the Lancang-Mekong Cooperation (LMC) in 2016 all contributed to building a suitable environment for regional integration as well as the enhancement of bilateral economic ties between China and Cambodia. These multilateral frameworks facilitated the inflow of Chinese investments to Cambodia, while strengthening regional connectivity (Kha, 2019).

In April 2019, the Ministry of Economy and Finance of Cambodia signed an MOU with the Bank of China on "Cooperation under the Rectangular Strategy and the Belt and Road Initiative" with the aim of promoting the BRI projects, especially those pertaining to infrastructure development, trade facilitation, and financial collaboration. The Bank of China agreed to assist the Ministry of Economy and Finance with attracting Chinese investment, hosting or organizing investment promotion activities, and providing favorable credit policies to key projects. Moreover, since early 2019, Cambodia has started using the Chinese Yuan, colloquially known as *renminbi*, as a floating currency, making Cambodia one of the early supporters of the internationalization of renminbi.

The role of local Chinese ethnic communities is also important in drawing Chinese investors to Cambodia, in part because some local Chinese tycoons have strong political connections with local Cambodian political leaders. In a 2014 article on Chinese FDI in Cambodia, Daniel O'Neill correctly observes that, to avert risks, Chinese firms in Cambodia receive and secure political support from China (in the case of state-owned enterprises) and political connections and protection from local elites (O'Neill, 2014). Chinese investments in Cambodia are varied in terms of ownership type and asset specificity. China's state-owned enterprises have focused on hydropower plant projects facilitated through grant aid or soft loans from the Chinese government to Cambodia. These projects frequently enjoy investment approval and political protection from the Cambodian government, and some of these projects have been criticized for their lack of transparency and accountability. China's private firms, on the other hand, have concentrated their investments on the garment industry. Chinese firms investing in Cambodia's land and resource sector have strong political connections with local political elites (O'Neill, 2014).

Local Perceptions Towards Chinese Investment

Chinese investments have had substantial impact on Cambodia, from political to socio-cultural, environmental, and socio-economic impacts. In the case of Chinese investments in Sihanoukville, the negative impacts on local community development and environment seem to outweigh the benefits arising from the influx of Chinese investment projects to the area. An increasing crime rate, booming gambling and sex industries, environmental degradation, inflation and rising cost of living, and social and cultural tensions between the Chinese and local community are some of the issues and concerns facing the local people (Sovinda, 2019).

There is a divergence of views among different actors and stakeholders in Cambodia regarding Chinese investment. The ruling elite are comfortable and quite confident that Chinese investment has helped to develop the national economy and strengthen regime legitimacy. This same elite, however, is also concerned about political and strategic implications from overreliance on China. Local business communities have different views. For example, it is primarily large corporations that have more opportunities and advantages to link up with Chinese companies, especially under joint venture frameworks. Local small and medium size enterprises (SMEs) have much less to gain, and some are even marginalized due to their losses from competition with Chinese companies.

STATE ACTORS

China has played a critical role in developing the Cambodian economy, especially through the development of infrastructure, investment and job creation, and trade relations. China is most responsive to Cambodia's development needs in the context of infrastructural megaprojects. In the words of Cambodia's Secretary of State of the Ministry of Economy and Finance (Meng), "Without China, there would be no Cambodia today — one must learn to accept that. Why should we go to China for assistance? We don't want to favor China, but if they give us what we need, shouldn't we take it?" The Under-Secretary of State of the Ministry of Economy and Finance further wrote, "The prospect of shifting and relocating some of China's industries and production base to countries along the Belt and Road can only be promising for small economies like Cambodia" (Vanndy, 2019).

The Cambodian government has made efforts to attract more Chinese investment, especially through the reduction of production and logistics costs. Speaking at the Dinner Party of the Cambodia-China Business Forum on Cambodia in December

2016, Prime Minister Hun Sen said that the government would continue to improve the investment and business climate by improving logistics, providing stable and low-cost electricity, offering skills development for the work force, and reducing irregular fees (CNV).

Under mounting diplomatic and economic pressure from the US and the EU, Cambodia has sought assistance from China to mitigate the risks and hedge against the pressures from the West. Wang Huning, a Member of the Politburo Standing Committee of the CPC and Secretary of the Party's Secretariat, told Prime Minister Hun Sen in April 2019 that China would help Cambodia with all problems, including those arising from the withdrawal of EBA status by the EU (Niem Chheng, 2019b). The statement demonstrates China's firm commitment to assist Cambodia in all circumstances. An editorial in Khmer Times warned that, "the threat to revoke the EBA, which costs Cambodia up to USD 650 million dollars a year, would force Cambodia to fall completely into China's camp, and this might be an irreversible trend" (Khmer Times, 2019b).

With regard to the concern over the possible debt trap caused by the BRI projects, Cambodia is confident that it has managed its external debt prudently. According to the Debt Sustainability Analysis by the IMF, Cambodia is at low risk of external debt distress (IMF, 2017). Prime Minister Hun Sen stated at the second Belt and Road Forum in April 2019 that, "BRI will [not] make some countries fall into a debt trap. Cambodia will negotiate and prepare projects in the interests of the nation and its people and not increase the financial burden and public debt. As a sovereign country, we have the right to make whatever choices we want and receive the loans necessary. We will implement these projects for national development based on self-reliance" (Niem Chheng, 2019a).

LOCAL PRIVATE SECTOR (SMALL BUSINESSES)

Chinese investment projects have few economic links with local enterprises and a low level of technology and knowledge transfer among local enterprises and workers. Some local small-businesses have even been marginalized and adversely affected because they could not compete with Chinese companies. Chinese firms have little interaction with local firms and do not contribute much to the capacity and skill development of the local workforce (Kubny, 2010). As a result, the spillover effect of Chinese investments on local SMEs has been limited.

Numerous news reports on Chinese investments in Sihanoukville illustrate that

small local businesses do not benefit from the influx of Chinese investments in the province. Local analyst Heng Pheakdey (2018) argues that, "Even though Chinese investment is bringing wealth to Cambodia, this wealth is mainly kept within Cambodia's Chinese community. Chinese residents and visitors in Cambodia buy from Chinese businesses, eat in Chinese restaurants and stay in Chinese hotels. The trickle-down effect to local businesses is minimal." A news report (Ng, 2018)quoted a local businessman as saying:

> *Hundreds of family-owned businesses have put up shutters in the past year. Many were evicted because the landlords preferred to lease properties to Chinese businessmen, who can afford to pay up to five times more. To make matters worse, local businesses have lost their traditional customer base: Western tourists who used to flock there for the sun, sand, and sea.*

LOCAL COMMUNITY AND CIVIL SOCIETY

The local community and civil society have different views on the impacts of Chinese investments on their livelihood. Some welcome the presence of Chinese investments because they bring job opportunities and higher incomes. Some are concerned over the fact that their livelihood has been affected due to the climbing cost of living, rising crime rate, and environmental degradation. Chinese investments in Cambodia lack strict social or environmental safeguards. With regard to Sihanoukville, local analyst Sim Vireak (2019) argues that "Unchecked development by Chinese investors has come at a cost, freezing out locals and changing the city's character." Scholar Kimkong Heng (2019) argues that, "The capital inflow and rising visitor numbers have been both beneficial and disruptive for Cambodia's economic development and social cohesion."

Rising crime is another concern for local people. In January 2018, local governor Yun Min warned that Chinese investments were bringing organized crime and instability to Sihanoukville. Governor Yun Min warned that the Chinese influx had "created opportunities for Chinese mafia to come and commit various crimes and kidnap Chinese investors, causing insecurity in the province." China's then-ambassador to Cambodia, Xiong Bo, also acknowledged the rising crime rate among Chinese living in Cambodia, including drug and sex trafficking as well as internet and telephone scams (Benjamin, 2019).

Social and cultural tensions between locals and Chinese immigrants have also been rising due to the lack of respect shown by some Chinese toward Khmer culture and values. Misspelling of Khmer language in commercial signboards, a booming sex

industry in the case of Sihanoukville, and other related identity conflicts are some of the sources of tension between the two communities, especially during the drastic increase in the number of Chinese immigrants over the past few years. In the case of Sihanoukville, it is estimated that Chinese make up about 20 percent of the resident population. Chinese nationals own more than 90% of businesses in Sihanoukville (Heng, 2019). This has fueled rising hostility among locals toward the influx of Chinese residents (Ellis-Petersen, 2019). Anti-China sentiment has been on the rise, fueled by some irresponsible politicians and individuals (Capital Cambodia, 2019). Analyst Heng Pheakhdey argues, "If the situation continues to deteriorate and more social chaos is caused by the Chinese community in Cambodia, I think… it's possible that it will create a negative sentiment towards Chinese nationals in Cambodia," he said. "It's a real risk for Cambodia" (Millar, 2018).

Challenges and Issues

REGULATORY QUALITY AND INSTITUTIONAL CAPACITY

In 2016, China invested USD 3.6 billion in Cambodia. This figure nearly doubled in 2017, with Chinese investment totaling USD 6.3 billion. The remarkable magnitude and velocity of Chinese investment in Cambodia has outpaced the speed and capacity of Cambodian government bodies to regulate, monitor, and manage these investments. Cambodia lacks a regulatory regime capable of effectively managing investment projects, particularly in light of the high rates of corruption and the lack of transparency in Cambodia. Moreover, due to the lack of policy and coordination mechanisms to promote technology and knowledge transfer to the local labor force, Chinese investment has brought with it an influx of Chinese migrant workers to Cambodia.

Some Chinese investors have contributed to projects that have led to criminal activity, social and cultural tensions, environmental issues, and other unintended negative impacts on local communities. Due to the lack of regulation and weak law enforcement, Cambodia is vulnerable to these "irresponsible" investors (Khmer Times, 2019a). Cambodia's judicial system lacks the institutional capacity to address those crimes and otherwise faces political constraints limiting its effectiveness (Cox, 2012).

Weak law enforcement and corruption are the main root causes of these adverse impacts. In January 2018, Preah Sihanouk provincial governor Yun Min expressed frustration over the growing crime and public disorder in Sihanoukville. These problems are frequently associated with the influx of Chinese funds and migrants. In a letter to the

Interior Ministry, Min also bemoaned rising property rent, the inability of local businesses to compete with Chinese companies, and the oversaturation of Chinese laborers in the construction sector (Nachemson, 2019). The collapse of a Chinese-owned apartment block under construction in June 2019 was a case in point illustrating the weakness of the local government in monitoring the quality and standard of construction (BBC, 2019).

LAND OWNERSHIP ISSUES

Some Chinese companies are allegedly involved in land disputes and forced eviction. According to local NGO Coalition of Cambodian Farmer Community (CCFC), some 20,000 families have suffered as a result of land disputes related to Chinese investment since 2003 (Reaksmey, 2018). According to Cambodia's Investment Law, ownership of land for the purpose of carrying out investment activities shall be vested only in natural persons holding Cambodian citizenship or in legal entities in which more than 51% of the equity capital is directly owned by natural persons or legal entities holding Cambodian citizenship.

Due to some loopholes in implementation and law enforcement, land disputes have not been effectively resolved. A study by the Mekong Region Land Governance argues that, "long running disputes over land abound, but access to justice through the Cambodian court system or other dispute resolution mechanisms is limited" (Scurrah, 2015). Since the government began selling off land in 2001 to private investors for development, about 800,000 people have been displaced, according to the International Federation for Human Rights in 2016 (Ng, 2019).

LABOR ISSUES

Some Chinese investment projects have stirred local discontent due to infringements of labor rights, and degradation of local livelihoods and environmental quality (Vannarith, 2017). Moreover, the huge inflow of Chinese workers to Cambodia has also caused social tensions. Concerning the employment of Chinese workers, Cambodia's Investment Law stipulates that investors can hire foreign employees on the condition that workers with the necessary qualification and expertise are not available among the Cambodian populace. In addition, the investors have an obligation to provide adequate and consistent training to Cambodian employees and promote Cambodian staff to senior positions over time.

In accordance with Cambodia's Labour Law of 1997, foreign workers must apply for work permits and employment cards issued by the Ministry of Labour. These work permits are valid for one year but may be extended. The maximum percentage of foreigners who

can be employed in any given enterprise shall be determined by a Prakas (*Declaration*) of the Ministry of Labour. However, the implementation of the investment law and labor law faces limitations, mainly due to corruption and insufficient transparency. Specifically, unclear employment contracts, poor oversight of minimum wage adherence, and the absence of a labor court are common challenges to implementation of Cambodia's labor regulations (Nop, 2017).

TECHNOLOGY TRANSFER

Technology and knowledge transfer by Chinese companies is low (Lam Thanh Ha, 2019). Chinese firms have little interaction with local firms and contribute little to capacity and skill development for the local workforce (Kubny, 2010). Moreover, although some studies suggested that Cambodia has economically benefitted from the inflow of Chinese investments and development assistance, "economic gains from China are taking place at the expense of social dislocation and environmental destruction" and the deterioration of good governance (Pheakdey, 2016).

As an illustration of these negative impacts, some local people in Sihanoukville are not happy with China's presence in their communities. Increases in both cost of living and crime rates, weak links between Chinese investment and local small businesses, and degradation of local livelihoods have all been linked to the Chinese presence (Ng, 2019). Other issues include a public perception that the growing influence of Chinese entrepreneurs and politicians in Cambodia may result in the marginalization of local Cambodians and that Cambodia might fall into a debt trap especially under the infrastructure megaprojects under the Belt and Road Initiative (BRI) (Touch, 2018). Responding to these concerns, analyst Keo Piseth suggests that "mechanisms for transparency and accountability for BRI projects, especially in infrastructure, should be established to prevent elite capture and corruption in these gigantic, loan-based infrastructure projects." (Piseth, 2019)

Implications for Cambodia's Foreign Policy

Some Western media outlets and political analysts tend to portray Cambodia as a vassal state of China. In fact, Cambodia is implementing a diversification and hedging strategy instead of bandwagoning with any major power. Strengthening an open, inclusive, and rules-based multilateral system is the key objective of Cambodia's foreign policy (Vannarith, 2016). Cambodia's recent embrace of Chinese investment can be attributed to strategic and economic interests; (Kimkong Heng, 2019) a desire

to counter pressures from the U.S. and its allies on human rights and democracy issues (Var, 2015); and an attempt to counterbalance against existential threats posed by Cambodia's neighbors, Thailand and Vietnam (Thearith, 2017). Cambodian analyst Cheunboran Chanborey argues that "Cambodia's geography of being sandwiched by its two powerful historically antagonistic neighbors—Thailand and Vietnam—has been a persistent compelling factor shaping the country's strategic direction. To address this geopolitical predicament, Cambodian leaders have frequently adopted alignment politics with external great power(s)." (Chanborey, 2018)

The rumor that China is eyeing a naval base in Cambodia's Koh Kong province is stirring public debate both inside and outside the country. Domestically, concerns over national security are high because there is precedent of China building port facilities for dual civil-military use. Some foreign powers are also concerned that Koh Kong will serve as a forward operating base for the PLA Navy in the Gulf of Thailand and the South China Sea. The U.S. 2019 Indo-Pacific Strategy states, "we remain concerned about reports that China is seeking to establish bases or a military presence on its coast, a development that would challenge regional security and signal a clear shift in Cambodia's foreign policy orientation" (DOD, 2019).

The Cambodian government has repeatedly denied that it intends to align with any major power, and stresses that it will never permit any foreign military bases on its soil, citing a foreign policy stance of permanent neutrality and non-alignment (Sakhuja, 2019). There is no legal basis, security need, or strategic intention to host foreign military bases in Cambodia (Vannarith, 2018). Prime Minister Hun Sen recently stated, "the Constitution of Cambodia bans the presence of foreign troops or military bases in its territory… whether naval forces, infantry forces or air forces." (Straits Times, 2018)

Cambodia is determined to stay relevant in the international system by leveraging its international role. Taking sides with any major power could push Cambodia into a geopolitical trap. Some Cambodian leaders are aware of the risks stemming from over-reliance on any single major power. According to this perspective, Cambodia must be cautious and has to adopt a strategy to mitigate geopolitical risks posed by over-reliance on China (Khmer Times, 2019a).

Cambodia's ability to implement a hedging strategy to dilute and mitigate these risks is crucial for long-term peace and stability in the country. Competition between China and the West will continue to influence Cambodia's foreign policy and will chart the nation's course as it navigates through turbulent times ahead (Khmer Times, 2019a). Cambodia has

neither interest nor intention to become a vassal or client state of any major power. Cambodia has benefitted from reforms and opening up, and therefore continues to support an open, inclusive, and rules-based multilateral system (Khmer Times, 2019b).

The ruling elite is very much aware of the risk arising from Cambodian overdependence on China, but Cambodia has limited capacity and strategic space to maneuver (Chanborey, 2018). Hedging and diversification are recognized as important strategies, but implementation remains an issue. It will take a few more years for Cambodia to develop a concrete action plan, build institutional and leadership capacity, and strengthen institutional coordination and synergies between ministries (Vannarith, 2019c). Mey Kalyan, senior adviser to the Supreme National Economic Council said, "Cambodia welcomes Chinese investment but is concerned about the growing dependence on China. We should not allow just one country to dominate investment" (Heijmas, 2019).

Conclusion

China is the top foreign investor in Cambodia, enabled and facilitated by deep political trust and ties between the two governments, the relatively open and liberal investment regime in Cambodia, and bilateral and multilateral agreements and mechanisms. The BRI is the main catalyst of growth as well as the facilitator of Chinese investment in Cambodia. While there are economic opportunities and interests deriving from the influx of Chinese investments, there are also concerns and questions over the quality and real impacts of the investments. For instance, there is an upsurge of anti-China sentiment across Cambodia as result of mismanagement of Chinese investments in a number of instances. The case of Sihanoukville exemplifies the risks associated with Chinese investments such as increases in living costs, higher crime rates, and environmental degradation.

The perception gaps among the ruling elite, small-scale local entrepreneurs, and grassroots communities are also a matter of concern. The legitimacy of the government is affected if the local people cannot fairly benefit from the growing economic presence of China in their localities. Trilateral dialogue among the state, private sector, and civil society is therefore required to explore acceptable solutions to the problems and issues caused by Chinese investments. Overall, Cambodia-China relations will be affected if the majority of the local Cambodians continue to hold negative perceptions of China.

The case of Sihanoukville illustrates the weakness of the local authorities and their inability to prevent or manage crime, ensure the quality of construction, or support local businesses. The decision of the central

government to ban online gambling was welcomed by the general public, but it also caused short-term economic shock as thousands of workers were laid off after the resulting business closures and a sudden slowdown in the construction sector. The real estate bubble in Sihanoukville also started to deflate. The lesson learned is that overreliance on Chinese capital is risky. The local economy is not resilient enough to mitigate shocks.

Due to the excessive speed and magnitude of Chinese investments in Cambodia over the past two years, local authorities have found it difficult to manage these investments. Strengthening the capacity of public institutions and law enforcement agencies, conducting a comprehensive analysis of Chinese investment projects, implementing better management of foreign workers, and ensuring fair and just distribution of benefits and opportunities arising from FDI are some of the possible measures by which Cambodia could improve its governance of Chinese BRI investment projects (Piseth, 2019).

References

Aljazeera. (2019, April 30). China "to help" Cambodia if the EU implements trade sanctions, https://www.aljazeera.com/news/2019/04/china-cambodia-eu-implements-trade-sanctions-190430001935041.html

BBC. (2019, June 23). Cambodia: Sihanoukville Building Collapse Death Toll Rises. https://www.bbc.com/news/world-asia-48729072

Benjamin. (2019, May 17). Foreign investors do not only bring economic growth to Cambodia *Capital Cambodia*, https://capitalcambodia.com/foreign-investments-do-not-only-bring-economic-growth-to-cambodia/

Mean, Sok Sok. (2019, June 6). Bin Chin, Remarks by Deputy Prime Minister and Minister of Council of Ministers. *Thmey Thmey*. https://thmeythmey.com/?page=detail&id=79005

Hong, Cai & Yingqing, Li. (2019, March 13). Zone is pillar of cooperation. *China Daily*. http://global.chinadaily.com.cn/a/201903/13/WS5c8860f9a3106c65c34ee53c.html

Cambodia New Vision. (2016, January 12). http://cnv.org.kh/dinner-party-cambodia-china-business-forum/

Capital Cambodia. (2019, May 31). If not China then who?, https://capitalcambodia.com/if-not-china-then-who/

Ng, Desmond & Zachariah, Elizabeth. (2019, March 5). China's chequebook diplomacy in Cambodia a double-edged sword creating resentment. *Channel News Asia*.

https://www.channelnewsasia.com/news/cnainsider/china-chequebook-diplomacy-cambodia-investments-resentment-debt-11311662

Cheunboran Chanborey. (2018). Cambodia-China relations: What do Cambodia's past strategic directions tell us? Deth Sok Udom, Sun Suon, and Serkan Bulut (eds) Cambodia's foreign relations in regional and global contexts. Phnom Penh: KAS, p.243.

Chheang, Vannarith. (2019) Cambodia's approach to regional integration. Phnom Penh: Asian Vision Institute (AVI). AVI Policy Brief, Issue: 2019, No.2.

Chheang, Vananarith. (2017) Cambodia embraces China's Belt and Road Initiative. ISEAS Perspective No. 48. Singapore: ISEAS-Yusof Ishak Institute, https://www.iseas.edu.sg/images/pdf/ISEAS_Perspective_2017_48.pdf

Chheang, Vannarith. (2018, November 26). Cambodia has no reasons to host foreign military bases. *Khmer Times*. https://www.khmertimeskh.com/552864/cambodia-has-no-reason-to-host-foreign-military-bases/

Chheang, Vannarith. (2016, April 25). Cambodia is hedging, not bandwagoning. *Khmer Times*. https://www.khmertimeskh.com/23186/cambodia-is-hedging-not-bandwagoning/

Chheang Vannarith (2019) Cambodia's new era of reforms. AVI Commentary, Issue: 2019, No. 4. Phnom Penh: Asian Vision Institute (AVI).

Chheang Vannarith, "Cambodia's worldview 2019", Khmer Times, 5 June 2019, https://www.khmertimeskh.com/50610950/cambodias-worldview-2019/

Chheang Vannarith (2019) "Can Cambodian foreign policy find its feet?" East Asia Forum, 18 January 2019, https://www.eastasiaforum.org/2019/01/18/can-cambodian-foreign-policy-find-its-feet/

Chheang Vannarith (2017) The Political Economy of Chinese Investment in Cambodia. Trends in Southeast Asia, 2017, No. 16. Singapore: ISEAS-Yusof Ishak Institute. https://www.iseas.edu.sg/images/pdf/TRS16_17.pdf

Chheng Kimlong (2019) Can regulatory governance of business start-ups in Cambodia be improved? AVI Perspective, Issue 2019, No. 2. Phnom Penh: Asian Vision Institute (AVI).

Chheng Kimlong (2019) Rethinking Cambodia's Industrial Development Policy: A big-push approach and long-term strategy. AVI Perspective No.6. Phnom Penh: Asian Vision Institute.

China Daily. (2018, January 12). Chinese investors, tourists contribute to Cambodia's socio-economic development: Business leaders. http://www.chinadaily.com.cn/a/201801/12/WS5a584fa8a3102c394518edc0.html

Council for Development of Cambodia. Policies Toward FDI. http://www.cambodiainvestment.gov.kh/investment-scheme/policies-toward-fdi.html

Cox, Marcus & Ok, Serei Sopheak. (2012). Cambodia Case Study, Evaluation of Australian Law and Justice Assistance. https://www.oecd.org/countries/cambodia/cambodia.pdf

Department of Defense. (2019, June 1). Indo-Pacific Strategy Report. https://media.defense.gov/2019/May/31/2002139210/-1/-1/1/DOD_INDO_PACIFIC_STRATEGY_REPORT_JUNE_2019.PDF

Edel, Charles. (2018, August 17). Cambodia's troubling tilt towards China. *Foreign Affairs*. https://www.foreignaffairs.com/articles/china/2018-08-17/cambodias-troubling-tilt-toward-china

Ellis-Petersen, Hannah. (2018, July 31). No Cambodia left: Now Chinese money is changing Sihanoukville. *The Guardian*. https://www.theguardian.com/cities/2018/jul/31/no-cambodia-left-chinese-money-changing-sihanoukville

Heijmas, Philip. (2018, September 11). Chinese money is driving one of Asia's fastest property booms. *Bloomberg*. https://www.bloomberg.com/news/features/2018-09-10/chinese-money-is-driving-a-property-boom-in-cambodia

Hem, Vanndy. (2019). Closing remarks at the 3rd Policy Dialogue on "Belt and Road Initiative in Cambodia: Economic Diversification and Debt Management". Phnom Penh: Asian Vision Institute (AVI). AVI Policy Brief, Issue 2019, No. 3, p. 1.

Pheakdey, Heng. (2018, August 29). Are China's gifts a blessing or a curse for Cambodia. *East Asia Forum*. https://www.eastasiaforum.org/2018/08/29/are-chinas-gifts-a-blessing-or-a-curse-for-cambodia/

Pheakdey, Heng. (2016). Chinese Investment and Aid in Cambodia's Energy Sector: Impacts and Policy Implications. Unpublished Doctoral Dissertation. *Amsterdam: Vrije Universiteit*, pp.iv-v. https://research.vu.nl/ws/portalfiles/portal/42167644/complete+dissertation.pdf

Puy, Kea. (2016, August 23). Japanese Investment in Cambodia rises, but weak infrastructure a problem. The Japan Times. https://www.japantimes.co.jp/news/2016/08/23/business/japanese-investment-in-cambodia-rises-but-weak-infrastructure-a-problem/#.XfALv-hKg2w.

Reaksmey, Hul. (2018, October 31). Activists Claim Chinese Investment Fueling Land Disputes in Cambodia. https://www.voacambodia.com/a/activists-claim-chinese-investment-fueling-land-disputes-in-cambodia/4637185.html

Hun Sen Remark at the 75th Session of the UN-ESCAP "Empowering People and Ensuring Inclusiveness and Equality". (2019, March 27). *Bangkok*. http://cnv.org.kh/empowering-people-ensuring-inclusiveness-equality/

Kea, Puy. (2016, August 23) Japanese investment in Cambodia rises, but weak infrastructure a problem. *Japan Times*. https://www.japantimes.co.jp/news/2016/08/23/business/japanese-investment-in-cambodia-rises-but-weak-infrastructure-a-problem/#.XfALv-hKg2w

Keo, Piseth. (2019). The Belt and Road Initiative: Risks and opportunities for Cambodian Sustainable Development. Phnom Penh: Asian Vision Institute (AVI).AVI Policy Brief, Issue: 2019, No. 6. P.1.

Cambodia embraces East and West. (2019, June 4). Editorial. *Khmer Times*. https://www.khmertimeskh.com/50610630/cambodia-embraces-east-and-west/

Can Cambodia balance China with the West. (2019, May 9). *Khmer Times.* https://www.khmertimeskh.com/50601997/can-cambodia-balance-china-with-the-west/

Heng, Kimkong. (2019, February 8). Is Cambodia's foreign policy heading in the right direction? *The Diplomat*. https://thediplomat.com/2019/02/is-cambodias-foreign-policy-heading-in-the-right-direction/

Kubny, Julia & Hinrich Voss. (2010). The impact of Chinese outward investment: Evidence from Cambodia and Vietnam. *German Development Institute*. Discussion Paper 16/2010.

Piseth, Keo. (2019). The Belt and Road Initiative: Risks and opportunities for Cambodian Sustainable Development. Phnom Penh: Asian Vision Institute (AVI). AVI Policy Brief, Issue: 2019, No. 6. P.4.

Ha, Lam Thanh. (2019). Chinese FDI in Vietnam: Trends, Status and Challenges. ISEAS Perspective, Issue 2019, No. 34. Singapore: *ISEAS-Yusof Ishak Institute*. https://www.iseas.edu.sg/images/pdf/ISEAS_Perspective_2019_34.pdf

Thearith, Leng. (2017). Small state diplomacy: Cambodia's foreign policy towards Vietnam. *The Pacific Review*, Vol. 30, pp. 328-347.

Millar, Paul. (2018, November 13). Anti-Chinese sentiments in Cambodia. *Southeast Asia Globe*. https://southeastasiaglobe.com/anti-chinese-sentiment-in-cambodia/

Ministry of Foreign Affairs and International Cooperation of Cambodia. Retrieved from: https://www.mfaic.gov.kh/site/detail/29835

Ministry of Foreign Affairs of China. Retrieved from: https://www.fmprc.gov.cn/mfa_eng/topics_665678/XJPDJPZMJLGJXGSFWBCXZYDGAJXDJZGJLDRDBCHW/t1407054.shtml

National Bank of Cambodia. (2019, June 20) Economic and Monetary Statistics, June 2019, https://www.nbc.org.kh/download_files/publication/eco_mon_sta_eng/Review%20308%20June%202019-Eng.pdf

Desmond, Ng & Phang, Charles. (2018, October 20). China brings Casino boom to Cambodian town-but doom to local businesses?. *Channel News Asia*. https://www.channelnewsasia.com/news/cnainsider/china-belt-road-casino-boom-sihanoukville-cambodia-phnom-penh-10846730

Chheng, Niem, (2019, April 29). Hun Sen: Cambodia will not fall into Belt and Road debt trap. *Phnom Penh Post*. https://www.phnompenhpost.com/national-politics/hun-sen-cambodia-will-not-fall-belt-and-road-debt-trap

Chheng, Niem. (2019, April 30). Questions asked over 'post-EBA' China help. *Phnom Penh Post.* https://www.phnompenhpost.com/national-politics/questions-asked-over-post-eba-china-help

O'Neill, Daniel. (2014). Playing risk: Chinese foreign direct investment in Cambodia. Contemporary Southeast Asia 36, no. 2: 173–205.

Meng, Cheng Chou. *Radio Free Asia.* Retrieved from: https://www.rfa.org/english/news/special/chinacambodia/loans.html

Sakhuja, Vijay. (2019, June 13). There is more to Koh Kong. *Khmer Times.* https://www.khmertimeskh.com/50613745/there-is-more-to-koh-kong/

Vireak, Sim. (2019, April 20). Sihanoukville: A Cambodian City Losting its 'Cambodian-ness'. *The Diplomat.* https://thediplomat.com/2019/04/sihanoukville-a-cambodian-city-losing-its-cambodian-ness/

Vireak, Sim. (2019, November 8) The Dynamism of Chinese Investment in Cambodia. *Asia Times.* https://www.asiatimes.com/2019/11/opinion/dynamism-of-chinese-investment-in-cambodia/

Sok Kha. (2019). Cambodia: Transforming China-led and other regional initiatives into a source of development. Phnom Penh: Asian Vision Institute. AVI Commentary Issue 2019, No. 6.

Nachemson, Andrew. (2019, May 1). South China Morning Post. Chinese investment in Cambodia is bringing Phnom Penh closer to Beijing – and further from the EU. https://www.scmp.com/news/asia/southeast-asia/article/3008451/chinese-investment-cambodia-bringing-phnom-penh-closer

Sihanoukville Special Economic Zone. http://www.ssez.com/en/company.asp?Ione=3

Sovinda, Po & Heng, Kimkong. (2019, May 4). Assessing the impact of Chinese investments in Cambodia: The case of Preah Sihanouk Province. Issues and Insights, Working Paper Vol. 19, WP 4, May 2019. *Honolulu: Pacific Forum*.

Straits Times. (2018, November 19). Cambodian PM says no China naval base being built. Retrieved from: https://www.straitstimes.com/asia/se-asia/cambodian-pm-says-no-china-naval-base-being-built

Tomoya, Onishi. (2019, March 23). Cambodia breaks ground on $2bn China-funded expressway. *Nikkei Asian Review*. https://asia.nikkei.com/Spotlight/Belt-and-Road/Cambodia-breaks-ground-on-2bn-China-funded-expressway

Touch, Daren (2018, February 2) What does Chinese investment mean for Cambodia? *The Diplomat*. https://thediplomat.com/2018/02/what-does-chinese-investment-mean-for-cambodia/

Veasna Var, "Cambodia: Between China and the US", *The Diplomat*. https://thediplomat.com/2015/05/cambodia-between-china-and-the-united-states/

World Bank. (2018). Foreign Direct Investment, Net Inflows (% of GDP) World Bank, https://data.worldbank.org/indicator/BX.KLT.DINV.WD.GD.ZS

World Bank. (2019, May). Cambodia Economic Update. http://documents.worldbank.org/curated/en/843251556908260855/pdf/Cambodia-Economic-Update-Recent-Economic-Developments-and-Outlook.pdf

Xinhua News. (2019, June 21). Cambodia-China trade volume jumps to 5.8 bln USD last year: Minister. http://www.xinhuanet.com/english/2018-06/21/c_137270877.htm

CONCLUSION

Investments from China into Southeast Asia have contributed to economic growth and the development of the private sector in the host countries. For example, in Malaysia the solar panel and glass industries have seen leaps in growth due to Chinese investments. Yet there are also cases in Southeast Asia in which the local private sector received marginal benefit from Chinese investments. For instance, in Cambodia, the report showed that Chinese firms have little interaction with local firms and do not contribute much to the capacity and skill development of the local workforce. As a result, the spillover effect of Chinese investments on local SMEs has been limited.

Local firms in host countries seek to benefit more from investments from China. Several authors pointed out that small businesses are concerned about being unfairly outcompeted by Chinese firms, which are supported by state-led industrial policies and cheap credit from the state.

Foreign direct investments from China sometimes goes into high risk and lightly regulated industries, such as mining, online gambling, and payday lending. In the cases of the Philippines and Indonesia, the authors documented that these investments bypass, ignore, or undermine regulations in the host countries. Problems include importing illegal workers, evading taxes, and exploring military networks which are deeply vested in the economy. Southeast Asia's young democracies have suffered from weak rule of law and lax enforcement. Chinese

investments at times exploit and exacerbate these governance gaps.

Chinese-funded megaprojects raise more concerns than traditional FDI due to a lack of transparency and the opacity of the deal-making processes. The deals are made among the ruling elites of China and the host countries without proper scrutiny or oversight. It is widely recognized that the influx of Chinese capital and contractors help to alleviate the massive infrastructure gap in the region. To better utilize these capital inflows, the governments in Southeast Asia need to strengthen their capacity to mitigate the risks identified in this report, such as weak public procurement regulatory regimes, a lack of information on and robust oversight of BRI projects, weak governance of SOEs, and corruption.

Table 1 (PG. 198-199) lists recommendations to help mitigate risks stemming from large Chinese investment inflows:

TABLE 1: Recommendations to Help Mitigate Risk Stemming from Large Chinese Investment Inflows

PROBLEMS	SOLUTIONS
Lack of transparency in public procurement	• Increase transparency of the public sector and public procurement process • Have clear legal regulations on public procurement • Follow public procurement international best practices, such as competitive and public bidding • Replace low-bid procurement practices with Life-Cycle Cost Analysis (LCCA) to promote quality infrastructure project • Empower civil society and interested stakeholders to advocate for greater transparency on public procurement process
Corruption	• Strengthen anti-corruption work through institutional changes • Lawmakers should exercise oversight of loans that the government undertakes • Implement Freedom of Information act • Publicize government loan terms • Disclose ownership of companies which participate in mega infrastructure projects (especially if these companies are owned by government officials, their families, or close associates). • Provide for third party quality control/independent audit mechanism of the mega infrastructure projects • Implement PPP laws to facilitate investments and monitor PPP projects in hopes to increase transparency and accountability

CONTINUES ON NEXT PAGE

CONTINUED FROM PREVIOUS PAGE

PROBLEMS	SOLUTIONS
Weak governance of state-owned enterprises	• Demand greater scrutiny of SOEs by lawmakers • Require disclosure of SOEs' annual reports and detailed financial statements as well as disclosure of remuneration of company directors, any financial liabilities potentially borne by the taxpayer and justification of the entities' activities against public policy objectives • Implement mechanisms for SOEs to reduce conflicts of interest among directors
Illegal worker/ migration	• Implement better management systems for foreign workers • Improve the system of working permits and business licenses for foreign investors
Social tension, environmental degradation, land grabbing and force eviction	• Apply multilateral development bank (MDB) standards (such as financial feasibility, environment assessment, social and governance impact analysis) for Belt and Road Initiative loan projects • Promote Corporate Social Responsibility and corporate governance among Chinese firms
Little contribution to local private sector	• Provide a level playing field for local and foreign contractors by requiring foreign firms to abide by the OECD guidelines on export credit assistance • Ensure any local content requirements focusing on promoting technology and knowledge transfer between foreign and local firms

The countries of Southeast Asia should strengthen their regulatory environment to reduce the likelihood of corruption, increase transparency, enhance oversight mechanisms, and improve their public procurement framework. In addition, civil society organizations can play a more significant role as a bridge between foreign investors and local communities to spearhead inclusive dialogue among governments, local civil society, and foreign investors before megaprojects begin so as to ensure that local voices are heard. Civil society and a free press can also help monitor foreign business behavior and promote OECD guidelines for multinational enterprises in agriculture supply chains, the extractive sector, mineral supply chains, and textile and garment supply chains to advocate for more responsible business practices.

Governments can also use regional platforms such as ASEAN to gain stronger negotiation power when advocating for more responsible investments from China.

For China

Chinese civil society is eager to work with foreign counterparts to encourage Chinese firms to engage in more corporate social responsibility and be more responsive to local communities' concerns. Chinese companies could seek Chinese civil society's assistance to try to act more responsibly and inclusively.

The Chinese government could work with Chinese companies abroad to ensure that they are abiding by guidelines released by Chinese business associations. The mining and construction industry associations from China have published guidelines that are on par with international standards. More broadly promoting and sharing these guidelines would help improve business behavior overseas.

Regarding investments with an international development purpose, China should try to employ the standards of AIIB in all its BRI projects to ensure that this new global power is also advancing development goals by acting more responsibly. Greater transparency in business engagements and MOUs between governments would help improve China's image in the region and counter a reputation of colluding with ruling elites.

Lastly, the report highlights research questions requiring further scholarly attention, including:

- Whether Chinese private firms are driven purely by the profit motive or instead act based on the policy guidelines from the state
- Whether SOEs and private firms from China respond differently to local pressure and incentives
- The extent to which China uses its economic leverage to influence host countries' domestic politics or foreign policy

ACKNOWLEDGEMENTS

The report was authored by think tanks and researchers from Southeast Asia and was prepared by the Center for International Private Enterprise, an international affiliate of the U.S. Chamber of Commerce and a core institute of the National Endowment for Democracy (NED).

These chapters were written by Laurence Todd, Azam Wan Hashim, Septa Dinata, Muhamad Ikhsan, Mary Silaban, and A. Khoirul Umam, Chheang Vannarith, Khine Win, Ajisatria Suleiman, Pingkan Audrine Kosijungan, Galuh Octania, Alvin Camba, Thilo Hanemann, and Stanley Seiden with additional content contributed by Cameron Moubray under the editorship of Catherine Tai and John Morrell.

Catherine Tai coordinated overall production, assisted by Claire Garney, Ryan Patrick Evangelista, and Cameron Moubray. Andrew Wilson, Abdu Alkebsi, Kim Bettcher, and John Morrell provided strategic vision and expert feedback to the authors. Stanley Seiden, Anne Henochowicz, Cameron Moubray, Erika Lewis, Gregory McAndrews, John Fei, and Richard Tucker provided copyediting support. The publication also benefited from comments provided by expert reviewers Christina Fink, Brian Eyler, Courtney Weatherby, Mihir Prakash, Thomas Kellogg, and Chang Chiu.

ABOUT CIPE

The Center for International Private Enterprise (CIPE) is a non-profit international affiliate of the United States Chamber of Commerce and a core institute of the National Endowment for Democracy. Founded in 1983, CIPE's mission is to strengthen democracy around the globe through private enterprise and market-oriented reform, fulfilling our vision of a world where democracy delivers the freedom and opportunity for all to prosper. CIPE does this by partnering with local business associations, chambers of commerce, universities, think tanks, and advocacy groups to advance democratic and economic reforms worldwide.

CIPE is headquartered in Washington, D.C. and currently has regional offices and representatives in more than a dozen countries, as well as a vast network of partners past and present. A wide range of donors directly support CIPE's work, and CIPE regularly collaborates with other international development and democracy organizations to carry out joint projects.

CENTER FOR INTERNATIONAL PRIVATE ENTERPRISE
1211 Connecticut Avenue, NW Suite 700 Washington, D.C. 20036
(202) 721-9200

WWW.CIPE.ORG | @CIPEDC | @CIPEglobal