

**AUSTRALIA-CAMBODIA DEVELOPMENT
COOPERATION PROGRAM**

COUNTRY STRATEGY PAPER

From Emergency Rehabilitation To Long-Term Development

1999 - 2001

September 1999

Executive Summary

Country Situation

- Cambodia has made the transition from a command economy to a market economy while it also recovers from decades of war and internal strife. Since 1993 the country has made significant progress in stabilising the economy and restoring economic growth. However, Cambodia remains one of the world's least developed countries:
 - According to the UNDP's 1999 Human Development Index, Cambodia ranks 137th among 173 countries in terms of quality of life (income, education, housing, etc).
 - In 1968, Cambodia had the same per capita income as Thailand; today, Cambodia's per capita income of US\$300 is barely more than one-tenth that of Thailand's.
- The key development challenge that Cambodia now faces is how to maintain sustainably high levels of economic growth and to translate that growth into broad improvements in the well-being of the Cambodian people, especially in rural areas:
 - Recent economic growth has been disproportionately centred in the capital, Phnom Penh. This, in combination with inadequate access to resources, is compounding an inequitable distribution of the benefits of economic growth;
 - Lack of a stable political framework, administrative capability and skilled human resources continues to constrain Cambodia's capacity to attract private investment; and
 - Fiscal revenues are still very low, the revenue base narrow, and planned program expenditures in important development areas are not being met.
- Cambodia's economic situation worsened in 1997 and 1998 due largely to political instability following the July 1997 breakdown of the coalition Government, weak fiscal performance especially on revenue collection, a failure to check corruption and, to a lesser extent, the regional financial crisis;
- The international community is looking to the new Cambodian Government to demonstrate renewed commitment to improved economic governance and the implementation of essential reforms.

Australia's Interests and Aid Strategy

- Australia's interests in Cambodia include: promoting equitable growth, social and political stability and democracy; and contributing to regional stability and security through assisting Cambodia to participate in economic growth in the region and to become a productive member of ASEAN.
- The objective of Australia's aid program to Cambodia is:
 - to assist Cambodia achieve reductions in the incidence of poverty and make a transition towards sustainable, more broadly-based development*
- The program strategy emphasises balance between Cambodia's immediate needs for reconstruction and rehabilitation of physical and human capital, and its longer term need for sustainable economic and human resource development:

- It focuses on poverty alleviation as the single-most important long-term goal of Cambodia's Socio-economic Development Plan; and
 - It reflects a strong commitment to supporting Cambodia to re-establish institutional structures and administrative capacity so that Cambodia will eventually succeed in attracting much needed private investment.
- The focal sectors for aid to Cambodia accord with three of the five aid program priority areas which have been identified by the Australian Government - namely, **agriculture, health, education and training**. The remaining two sectors of governance and infrastructure will receive less overt attention:
 - The program will continue to support a stand-alone criminal justice project. However, in response to recent political uncertainties, governance will (apart from this one project) be treated mainly as a cross cutting issue - through community participation and institutional strengthening components of projects - with small amounts of funding continuing to be available for targeted NGO activities;
 - It is not proposed that infrastructure be a priority sector for the bilateral aid program to Cambodia given past difficulties in attracting the interest of relevant Australian expertise, although consideration will continue to be given to basic infrastructure development at provincial and district level to support project activities in the focal sectors.
 - Key areas where Australia can, and should, assist the Government of Cambodia to achieve substantial poverty reduction and sustainable development are:
 - Improving productivity and profitability in the agriculture sector;
 - Meeting basic human development needs of men and women in health and education;
 - Strengthening the institutional base;
 - Addressing demining and humanitarian relief needs; and
 - Ensuring that men and women have equal opportunity to participate in the development effort.
 - The strategy recognises that long term involvement with Cambodia through the aid program will be required if tangible and sustainable benefits are to be realised: our involvement must be responsive to changing circumstances and priorities; capacity building components will be required in practically all bilateral aid activities; and careful and innovative approaches to project implementation will be necessary given the lack of counterpart government financial and institutional capacity to support development activities.
 - Gender sensitive approaches will be applied to all aspects of activity planning and implementation. The aid program will seek to facilitate a broad notion of gender in which participation of males and females takes place not only at the village level but at all levels, including the strategic planning level.
 - Environmental assessment and management will be undertaken as a matter of course for all activities. At this stage, however, is not considered viable for Australia to engage in projects in the forestry sector given lack of commitment on the part of the Government to essential reforms which underpin sustainable use of forest resources.

TABLE OF CONTENTS

| | Page |
|---|-------------|
| Executive Summary | (i-ii) |
| 1. Background | 1 |
| 2. Development Trends, Constraints and Priorities | 3 |
| 3. Development Needs of the Recipient Government..... | 5 |
| 4. Australia’s National Interests..... | 6 |
| 5. Development Assistance | 7 |
| 6. Strategies for the Future Program Development..... | 9 |
| 7. Performance Monitoring and Review | 16 |

Tables

| | |
|---|---|
| Table 1 - Selected Economic Indicators | 2 |
| Table 2 - Selected Social Indicators..... | 4 |
| Table 3 - Australian Development Assistance to Cambodia by Sector | 7 |

1. Background

Historical Context

1.1 Cambodia is a country in transition: from a command economy to a market economy; from a single party state to democratic pluralism; and, from a state of perpetual conflict to development and stability.

1.2 It is impossible to overestimate the social and economic damage done to Cambodia during the years of conflict starting with the Pol Pot era from 1975 - 1979. The Pol Pot regime sought the rapid collectivisation of Cambodian society and property. This plan led to the dissolution of social institutions (religion, family, community, etc). Basic social and economic infrastructure (schools, hospitals, irrigation systems, roads, bridges, etc) was destroyed. Commerce and banking were disallowed and money was abolished. Over a period of four years, the social fabric of Cambodia was shattered through the mass displacement of the population. While the need for skills and literacy was recognised in rhetoric, many educated people were killed as class enemies, or escaped to other countries. It is conservatively estimated that over one million people (one in seven) died during this period.

1.3 During the 1980s Cambodia was isolated from the international community and denied any significant level of international assistance. The 1991 Peace Accords, through which the United Nations Transitional Authority on Cambodia (UNTAC) was established, saw the warring factions finally agree to a voluntary ceasefire and heralded in a new era for Cambodia. In 1993 Cambodia had its first democratically elected government. A coalition government was formed with Prince Ranariddh (FUNCINPEC Party) assuming the position of “First” Prime Minister and Hun Sen (Cambodian People’s Party) assuming the position of “Second” Prime Minister. Australia took a leading role in the peace process and, along with all signatories to the Accords, committed itself to providing continuing support to assist Cambodia to overcome many years of turmoil.

1.4 Following the formation of the coalition Government in 1993 Cambodia, in partnership with donor countries such as Australia, multilateral organisations and international financial institutions, NGOs and other development organisations, started rehabilitation and reconstruction of its economic and socio-political structures towards a market orientation. Nevertheless, strains within the coalition Government started to show, and from May 1996 onward, the political atmosphere in Phnom Penh deteriorated. This culminated in fighting over 5-6 July 1997. The Australian Government unambiguously condemned the events of July 1997 but decided to continue the aid program for humanitarian reasons, and then only on condition that Cambodia moved expeditiously to hold democratic elections. Subsequently the military and security situation has stabilised, a national election poll was conducted in July 1998 and a new coalition Government was formed at the end of November 1998.

Economy

1.5 Cambodia is making solid progress towards a more market-based and liberalised economy as it recovers from decades of war. However, it is starting from a very low economic base, shattered social institutions and a significantly depleted cadre of professionally trained people. In 1968, Cambodia had the same per capita income as Thailand. Today Cambodia is one of the world’s least developed countries with an estimated GDP of only US\$300 per capita per year — around one-tenth that of Thailand.

1.6 Cambodia commenced reforms towards a more liberal, market-oriented economy in the late 1980s but implementation was partial and ad hoc until 1993. Following UN sponsored elections in 1993 Cambodia formulated and began implementation of a comprehensive program of macroeconomic and structural reform with support from the international donor community. The

fruits of these reforms were evident in improved macroeconomic stability and a rebound in growth over 1995 and 1996. Inflation was reigned in to single digit levels in the mid-1990s from an average of 140% in 1990 - 1992. Real economic growth averaged about 7% over 1995-96. Per capita income is estimated to have doubled from about US\$150 in 1991 to nearly US\$300 in 1997.

1.7 Despite significant increases in economic growth in the mid 1990s, economic performance deteriorated in 1997 and 1998 due largely to weak fiscal performance, failure to check corruption, political instability, disruption associated with the outbreak of fighting in July 1997 and to a lesser extent, the impact of the Asian financial crisis. As a result inflation increased; GDP growth dropped to 1% in both 1997 and 1998 (against forecast growth of 6% for 1997); and the Government of Cambodia has experienced major revenue shortfalls. The Government reduced outlays in the 1998 budget by 3.4% compared with the 1997 budget (although in \$A terms outlays decreased by around 30%), and outlays are expected to again to fall as a percentage of GDP in 1999. Revenues decreased by 9% in 1998 following a 9.6% fall in 1997. In addition to illegal activity and political interference, the revenue problem is at least partially attributable to the narrowness of the revenue base itself and inadequate revenue collection mechanisms.

1.8 Agriculture dominates the Cambodian economy contributing almost 43% of output and 85% of employment. Agriculture grew annually by only 1.5%, 2% and 1.0% in the period 1996-1998, falling behind the population growth rate of 2.5% which will, if left unaddressed, place pressure on the food security situation. The industrial and services sectors account for a growing share of GDP (21% and 36% respectively) but benefit only a small proportion of the population. Industry grew by 3% in 1997 and 4% in 1998, while services grew 1.3% in 1997 and stagnated in 1998. These results represent a significant slowdown in both sectors compared to previous years.

Table 1 - Cambodia: Selected Economic Indicators

| | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 |
|---------------------------------------|-------|--------|--------|-------|-------|-------|-------|
| Real GDP Growth | 7.0 | 4.1 | 4.0 | 7.6 | 6.5 | 2.0 | 1.0 |
| GNP Per Capita (US\$) | 180 | 220 | 240 | 280 | 300 | 300 | 300 |
| CPI Inflation | 112.5 | 41.0 | 17.9 | 3.5 | 9.0 | 9.1 | 12.6 |
| Industrial Growth (%) | 15.7 | 13.1 | 7.5 | 9.9 | 13.3 | 3.0 | 4.0 |
| Agricultural Growth (%) | 1.9 | -1.0 | 0.0 | 6.4 | 1.5 | 2.0 | 1.0 |
| Services Growth (%) | 11.2 | 7.0 | 7.5 | 7.8 | 8.8 | 1.3 | 0 |
| Imports (US\$m) | 350.7 | 422.0 | 737.1 | 711 | 771 | 799 | 802 |
| Trade Balance (US\$m) | -86.2 | -203.0 | -275.4 | -443 | -476 | -265 | -223 |
| Official Exchange Rate (Riel/US\$) | 1,253 | 2,470 | 2,543 | 2,462 | 2,624 | 2,938 | 3,750 |

Source: World Bank, Cambodia Progress in Recovery and Reform, June 1997
World Bank World Development Indicators 1997
Economic Intelligence Unit, Country Profile

1.9 The impact of the regional financial crisis is being partially mitigated by Cambodia's relatively heavy dependence on labour intensive subsistence agriculture, its small industrial base, limited integration with international financial markets, and limited use of short-term capital flows. However, these factors, which represent Cambodia's lack of integration into the global trading system and its unattractiveness as a destination for international capital, represent constraints to Cambodia's longer term development prospects. The reality is that the crisis has changed the external context for macroeconomic policy in Cambodia.

1.10 Aid donor countries are playing a crucial role in Cambodia's economic reconstruction. In addition to humanitarian work, donors are funding essentially all public investment in Cambodia as well as a very high proportion of recurrent expenditure due to the Government's lack of resources. Following the events of July 1997, Finance Minister Keat Chhon expressed concern about reduced overseas development assistance levels. He stated that the Cambodian Government, which relies on aid for more than 40% of its revenue, had lost over US\$100 million in 1997 because of aid suspensions, in particular from the United States and Germany.

2. Development Trends, Constraints and Priorities

2.1 Cambodia's recent history has had severe consequences for development. According to the UNDP's 1999 Human Development Index, Cambodia still ranks 137th among 173 countries in terms of quality of life (income, education, housing, etc). While the Cambodian Government made significant advances in macroeconomic management since the recommencement of official aid in 1992, the foundations for stable, secure and equitable economic development are shaky.

2.2 The economic transition process itself is raising concern because of its impact on the conditions of the poor and vulnerable. The combination of economic growth in the larger towns and stagnation in the rural areas, where the vast majority of the people live and work, means that the benefits of recent growth have not been equitably distributed and the impact of this growth on sustainable development has been limited. Despite the almost doubling in GDP per capita from US\$150 in 1991 to US\$300 in 1997, rural household incomes, and in particular, farm household incomes appear to have remained basically unchanged.

2.3 The development challenges facing Cambodia in achieving a level of sustainable economic growth required to facilitate broad based and equitable development are daunting. Education, health and infrastructure have been grossly neglected due to decades of war and privation, and the institutional foundations for sound economic development are lacking. Given Cambodia's high population growth rate of 2.8% (1990-96 average), it is estimated that economic growth in Cambodia will need to be maintained at around 6 - 7% a year and combined with a stable macroeconomic environment for around 20 years to achieve a per capita GDP of \$US 1,000.

2.4 Cambodia's development challenges call for a persistent effort in achieving a pattern of development that is people-centred and sustainable over the longer term. This will require a strong reform program that emphasises macroeconomic stability, acceleration of economic reforms and strengthening of institutional capacity and the human resource base.

2.5 While the problems facing Cambodia are not uncommon among least developed countries, due to its history, many problems are more serious and widespread in Cambodia than in many similar countries. There are also several areas of special concern in Cambodia:

Lack of security and political stability remains an overriding constraint to development. The Khmer Rouge, are no longer a threat, but banditry continues to disrupt civilian life and to pose a threat to economic development, particularly in rural areas. Large arable areas of the country are littered with land mines and unexploded ordnance, which kill or maim up to 300 people every month. The level of crime is now also becoming a major concern, particularly in Phnom Penh. The large numbers of weapons in circulation in the community and the habit of resorting to violence, are remnants from years of conflict.

Unusual demographic factors pose special development challenges: The sex ratio is skewed with

57% of the adult population being female and a high percentage of population living in female-headed households (23%); This 'surplus' of women and 'lack' of men has forced women to enter traditionally non-female work, where they are increasingly vulnerable because of persistent high illiteracy rates, prevailing invisibility in public domains of decision making, and with lack of access to and ownership of productive resources (men earn about 50% more than women in most occupations). The level of disability (of which land mine injuries are a major contributor) in the community is staggering at 1/436; there are also significant age distortions - as a result of the extremely high death rates of the Khmer Rouge period and the very rapid natural growth after this period almost half the population is under 15 years of age. This young population structure means that the proportion of people of working age will grow by 3 - 4% per year during the next decade.

Table 2 - Cambodia: Selected Social Indicators

| | Latest Available Single Year | | |
|--|-------------------------------------|------------------|------------------|
| | 1970 - 75 | 1980 - 85 | 1992 - 97 |
| Total Population mid-year (million) | 7.1 | 7.4 | 10.5 |
| Growth Rate (% annual average) | 0.5 | 2.6 | 2.2 |
| Life Expectancy at Birth | 40 | 45 | 54 |
| Infant Mortality (per 1,000 live births) | 181 | 160 | 103 |
| Maternal Mortality (per 100,000 live births) | | 500 | |
| Child Malnutrition (% under 5) | | 20 | 38 |
| Illiteracy Rate (% population age 15+) | | 71 | 35 |
| Primary enrolment rate (% school age) | 42 | | 98 |

Source: World Bank, Cambodia Progress in Economic Recovery and Reform, June 1997
World Bank, World Development Indicators, 1999 CD-ROM

The loss of a generation of educated people, coupled with almost total isolation for twenty years from modern education, technology and management methods, leaves a limited human resource base to take up the challenges of development.

Agriculture, which employs some 80% of the population, remains subsistence based. More than three-quarters of the poor are found in households in which the head has an agricultural occupation. In glaring contrast to its neighbours, the green revolution has barely touched Cambodia with productivity, yields and total production stagnating over the past three decades. Progress is constrained by a lack of public investment in essential infrastructure including: rehabilitation and extension of irrigation systems and roads for market access; and provision of extension services to support research and the introduction of new varieties and modern farming techniques. It is also being constrained by the absence of an efficient and effective private sector capacity in the formerly state-run areas of input supply (information, fertiliser, seeds) and distribution and marketing of produce.

Health status in Cambodia is very poor. The infant mortality rate of 105/1000 live births (compared to 6/1000 in Australia) and the maternal mortality rate of 900/100,000 live births are amongst the worst in Asia. Death from preventable diseases is common, especially in rural areas. HIV infection and AIDS are also a growing problem, especially among sex workers in Phnom Penh. Under current projections, anywhere from one-half to one million people could be cumulatively infected with HIV/AIDS by the year 2006. Health indicators reflect the poor state of public health provision in Cambodia. Current medical service provision at the local level is of extremely poor quality or nonexistent. At the same time, the sector is facing severe financial constraints. Cambodia currently spends only 2% of GDP on health and education, compared with an average of 5% of GDP for low income countries.

The Government of Cambodia recognises the need to increase the availability and quality of basic health services and has embarked on a program of health sector reforms to ensure more cost-effective and efficient use of its available resources. Key reforms include: redefinition of the roles and functions of each level of the health system; development of a health financing policy and a framework of pilot projects relating to this policy; development of a Health Coverage Plan which provides a defined Minimum Package of Activities at Health Centre level for communities of 10,000 or more within a radius of 10 kilometres, and at Referral Hospitals serving around 100,000 inhabitants. Substantial external assistance is required to lift the level of new capital investment and provide essential training to support the implementation of the Health Coverage Plan and Minimum Package of Activities.

Limited revenue due to pervasive tax exemptions and a weak tax collection capacity, coupled with fiscal discipline to avoid inflation, has depressed government salaries and the funds available for counterpart funding of operations and maintenance. This poses particular problems for development activities in terms of the Government's ability to operate and maintain the facilities provided by donor programs.

Environmental degradation and unsustainable exploitation of natural resources, particularly forests which are Cambodia's most valuable natural resources, are of serious concern. The implementation of economically and environmentally sound forestry policies could generate some US\$100 million a year in government revenue, equivalent to over one-third of budget revenue or over 3% of GDP in 1996. However, there is evidence of serious mismanagement of forestry resources: uncontrolled logging has led to rapid degradation that seriously threatens Cambodia's forests. A 1998 World Bank Forestry study estimates that, at current rates of logging, Cambodia's exploitable forests will be exhausted within three to five years. It also concludes that deforestation is contributing to floods and droughts in Cambodia, especially due to degradation in water catchment areas, and that siltation from up-stream soil erosion is negatively affecting rice growing areas.

3. Development Needs of the Recipient Government

3.1 Cambodia itself lacks the readily available resources to lay the foundations for sustainable and equitable growth within the short to medium term. This leaves it highly dependent on the outside world to provide the resources to catalyse a sustainable development process. However, private international investors are unlikely to be attracted to the most troubled country in a troubled region. Therefore, foreign assistance must play a key role in creating an enabling environment for private sector investment if hopes for economic growth are to be fulfilled.

3.2 Notwithstanding the need for foreign assistance, the onus is on the Government of Cambodia to recognise the urgent need to strengthen the domestic policy environment and take the needed steps to achieve best possible medium term growth outcomes. A first priority is to restore political stability and security throughout the country. Beyond this, substantial improvements are needed in macroeconomic and financial stability, while structural reforms need to be strengthened to remove domestic constraints to longer term growth. Three of the main policy challenges confronting the country in implementing an appropriate reform process are:

Enhancing Public Resource Mobilisation. Cambodia must broaden its revenue base. This is essential to fund priority development expenditures and to signal to the donor community that its efforts to assist Cambodia are being met by an equal effort on the part of the Cambodian

Government. Cambodia's budget revenue-to-GDP ratio (at around 9% in 1996) remains one of the lowest in the world. The income tax system is not yet fully functional and a significant amount of potential revenue has been lost to the central government. The 1998 Law on Taxation and further measures in the 1999 budget, which introduced a VAT and increased forestry royalties, represent the first steps in the right direction, but full implementation and further such reforms are necessary to adequately strengthen the revenue base: this issue requires a continued high priority;

Improving the Efficiency of Public Expenditure. Fiscal discipline has been maintained, despite shortfalls in revenue and higher than budgeted expenditure on security and defence, by compressing expenditure in health and education and other social sectors vital for human development. While continued fiscal discipline is essential, the composition of spending needs to be changed to support development priorities, shifting away from defence towards the social sectors and economic infrastructure, particularly in rural areas. Downsizing the public service remains an important objective in improving the efficiency of public expenditure but has been set back by large-scale new hiring for political purposes. The significant proportion of salaries within civilian expenditures is squeezing essential non-wage operations and maintenance expenditure and limiting the capacity of the Government to address broader issues relating to upgrading the performance of government agencies including raising salaries of public servants;

Strengthening Institutional Capacity to Implement Economic Reforms and Development Programs. An important Cambodian development priority is the need to strengthen the Government's capacity to implement its economic reform and development programs. Key priorities include strengthening the human resource base to create a core of highly trained individuals who are responsive to the needs of government; administrative reform to restrict growth of the public service and improve its efficiency and effectiveness; and legal reform to create an enabling environment for private sector investment.

3.3 Promising initial signs of the new Government's willingness to tackle key policy and governance reforms emerged at the February 1999 Donor Consultative Group meeting on Cambodia. The Government committed to a reform agenda encompassing fiscal and public administration reforms, reform of forestry sector and military demobilisation. It also pledged to strengthen the rule of law and tackle corruption. Donors and the Government put in place a quarterly monitoring process for the reform agenda under the auspices of the Consultative Group.

4. Australia's National Interests

4.1 Australia's interests in Cambodia include promoting equitable growth, social and political stability and democracy, and contributing to regional stability and security through assisting Cambodia to participate in regional growth and become a productive member of ASEAN. Pursuit of these interests falls into three broad categories: geopolitical; economic and humanitarian.

Humanitarian

4.2 For the moment, Cambodia is one of the poorest countries in the region. Because of the devastation and human loss inflicted by decades of conflict, Cambodia has a strong humanitarian claim for assistance in restoring and rebuilding its former institutions. Australia's aid program is the principal means through which we can help Cambodia to re-establish itself as a viable regional entity. For this reason, the Government firmly believes that Australian aid to Cambodia should continue as long as it can be delivered effectively to serve the humanitarian needs of the Cambodian people.

Regional Security

4.3 From the late 1960s until the beginning of this decade, Cambodia was a major source of instability in our region, drawing in both the great powers and regional countries seeking to benefit from the situation. This changed markedly after the settlement reached in the 1991 Paris Peace Agreements, which effectively ended great power involvement and substantially reduced the scope for Cambodia's neighbours to dabble in Cambodia's internal politics. Although a final internal settlement has not yet been achieved, the Cambodian problem is no longer a direct threat to regional stability. Australia's principal strategic interest thus relates to Cambodia's role as a member of ASEAN and as a key building block in the potentially rich greater Mekong region.

Economic

4.4 Because of its relative poverty and the difficulties of rebuilding the institutions of society and the economy, Cambodia is unlikely to present significant trade and investment possibilities for Australia, even in the medium to long term. Australia's investment in Cambodia currently stands at about 0.04% of Australia's direct equity investment overseas, with Telstra by far the largest investor. It is anticipated that the difficulties of operating in an environment affected by corruption, security threats and an uncertain legal framework will continue to deter Australian investors. However, despite these current difficulties, it is also recognised that Cambodia occupies a key position in the Mekong Basin sub-region, an area of current attention for possible major infrastructure development, which may offer significant opportunities for Australian commercial interests if the political and security environment continues to improve.

5. Development Assistance

Australia's Aid: snapshot and recent developments

5.1 In April 1992, Australia announced details of a program for resumption of bilateral aid. In real terms (1997/98 \$) Australia has provided \$A160 million in bilateral aid since then, and prior to that some \$94 million through NGOs and multilateral organisations since 1979. The annual program to Cambodia averages around \$A23 - \$A24 million of bilaterally agreed activities with an additional amount of around A\$9 million from other AusAID programs including emergency relief and food aid. This places Australia at number three among bilateral aid donors, after Japan and France.

5.2 Consistent with the objective of Australia's aid program *to advance Australia's national interests by assisting developing countries to reduce poverty and achieve sustainable development*, Australia's bilateral aid strategy for Cambodia aims to assist Cambodia make a transition towards sustainable, broad-based development. The program focuses on poverty alleviation as the single-most important long-term goal of Cambodia's Socioeconomic Development Plan. It also recognises that realisation of this goal will depend on Cambodia's own success in mobilising non-aid resources for domestic investment programs.

Table 3: Australian Development Assistance to Cambodia by Sector

| Sector | 1995/96 | 1996/97 | 1997/98 | 1998/99 (est) | 1998/99 % |
|--|----------------|----------------|----------------|--------------------------|----------------------|
| Agriculture | 4.38 | 5.30 | 7.06 | 8.47 | 26 |
| Education | 4.63 | 4.12 | 3.32 | 4.65 | 14 |
| Food Aid / Refugees / Emergency | 7.53 | 5.65 | 5.56 | 4.04 | 12 |
| Good Governance & Human Rights | 1.35 | 1.60 | 5.00 | 3.51 | 11 |
| Health | 3.44 | 4.67 | 4.46 | 5.09 | 15 |
| Infrastructure | 3.36 | 5.45 | 2.47 | 0.63 | 2 |
| Mine Clearance & Related Assistance | 4.85 | 4.27 | 4.11 | 4.12 | 13 |
| Other / Multisector | 3.36 | 2.94 | 2.90 | 2.37 | 7 |
| Total | 32.89 | 34.00 | 34.87 | 32.88 | 100 |

5.3 Program activities are being undertaken in the four sectors of agriculture, health, education and training, and good governance, although the latter (apart from a stand-alone project focusing on the criminal justice system) is addressed mainly as a cross-sectoral activity. Australia also provides demining assistance and emergency humanitarian assistance. Within these sectors, activities focus on:

- Strengthening human capital. Human resource development is the main theme of the Australian program. All program activities include training components and there are targeted interventions in health and education, basic skills training and English language training;
- Strengthening the institutional base. Australia is assisting through projects which support the reform of public administration in the context of our projects. Australia is also supporting targeted interventions including electoral assistance and small activities focused on human rights training; and
- Breaking the poverty cycle. - through programs to increase productivity in the rural sector, and improve access to basic health and education services. Activities implemented through Australian and local NGOs at the village level are an important part of this strategy as government services are largely concentrated around urban centres.

5.4 The bilateral program, including both firm approved commitments and strong expectations, is firmly committed until the end of 1999 - 2000. Based on current finding levels, there is scope to introduce one to two new activities into the program in 2000/2001;

5.5 Following the fighting which broke out in Cambodia in July 1997, the Australian Government very clearly condemned the use of force to bring about political change but decided to continue the aid program for humanitarian reasons. But this decision has always been dependent on the performance of the Cambodian Government in living up to the commitments it has made in regard to human rights, good governance and respect for the principles of the Paris Peace Accords. Initial indications are generally positive. But a final judgement is not yet possible at this early stage after the formation of the new coalition government.

Other Donor Programs

5.6 Donors have responded generously to the many needs of Cambodia. Between 1992 and 1997 donors will have invested around US\$2 billion in emergency programs, budget support and development programs. However, the events of July 1997, and general donor dissatisfaction with the Government's performance, particularly in implementing measures to strengthen budgetary transparency, passage of key legislation, human rights violations, and poor prospects for a more open and participatory government and society, and very slow disbursement of loans from IFIs, led to substantial cuts to major donor programs (US and Germany) and cessation of activity pipeline development by other donors.

5.7 This impasse contributed to a number of worrying trends over the intervening period between July 1997 and the World Bank Consultative Group meeting in February 1999. Few if any projects were designed which primarily work with Government to build capacity and strengthen institutions, civil society or the rule of law. Donors put on hold efforts to actively address key policy issues, pending the conduct of the July 1998 elections and evidence of clear commitment on the part of the new Cambodian Government to renewing its reform agenda, and the situation for project counterpart funds deteriorated rather than improved. The value of maintaining ongoing development assistance to Cambodia was increasingly being questioned, by donors particularly

given increased competition for scarce aid funds by other countries in the region as a result of the Asian Financial Crisis.

5.8 More recent developments have, however, moved Cambodia back from the brink of donor fatigue. Cambodia, led by Prime Minister Hun Sen reaffirmed commitments to a substantial reform agenda at the Consultative Group meeting. In response, donors pledged an amount which will meet in full the aid funding requirements for 1999 as set out in Cambodia's rolling public investment program. But donors were also united in wanting to see a more formal and frequent consultative and monitoring mechanism in place than has existed to date. Donor efforts following the Consultative Group meeting will be applied to active monitoring of progress and failure on the part of the Cambodian Government to demonstrate its ongoing commitment to implementing new policies will almost certainly result in donor exodus.

6. Strategies for the Future Aid Program

Incorporating Lessons Learnt

6.0 Experience to date suggests that the following factors should be taken into account in the planning and implementation of Australia's future aid program:

- Given the low base from which Cambodia is starting, there will remain immense needs in all sectors for Cambodia for some time. Australian interventions in all sectors must be considered on the basis of where the maximum developmental impact can be achieved as part of a long-term involvement which will change over time. It is therefore considered appropriate that the Australian program continue to have activities within the three priority sectors of **agriculture, health, and education and training**.
- In the context of a weak bureaucracy and limited financial resources stand alone governance programs tend to be less effective than programs which incorporate governance as a cross-cutting issue - targeting improvements in transparency and accountability in development planning and resource allocation as part of our broader project efforts in the focal sectors of agriculture, health and education and training.
- Consideration should also continue to be given to basic infrastructure development at provincial and district levels. However, past experience indicates that Australia may not be in the best position to implement major physical infrastructure projects in Cambodia, such as main roads and bridges;
 - The size of such projects (eg bridges) combined with the high level of political and security risk to successful project implementation, and the relatively poor prospects for flow-on commercial business, makes it difficult to attract the interest of relevant Australian expertise in the infrastructure sector.
- From Australia's perspective, the program to Cambodia is relatively generous. However, the program is relatively small when considered against the enormous demand for assistance required in all sectors in Cambodia. It is therefore important that Australia respond in a clear and focussed way within the priority sectors identified above, to ensure the maximum possible impact and a high Australian profile is achieved through our aid interventions in Cambodia. These considerations dictate that the program should:

- Not be spread across a large number of disparate and ad hoc activities in too many locations;
 - Address long-term constraints to economic growth which can often be achieved in concert with addressing immediate humanitarian concerns (eg rural development, human resource development). This strategy has the potential to achieve maximum impact on areas of most need in Cambodia with relatively small interventions;
 - Seek opportunities to work cooperatively with other multilateral and bilateral donors in larger activities in sectors of mutual interest - without necessarily tying ourselves in to their designs and project implementation constraints; and
 - Ensure that Australian funded activities are mutually reinforcing. For example in the agriculture sector, Australia has been funding a very successful agricultural research program with IRRI for a number of years. Coordination between this project, the Cambodia Australia Agricultural Extension Project which commenced in 1996, previous advisory assistance to the Ministry and a planned new production-oriented project is enhancing the impact of Australia's very significant program of assistance to the agriculture sector in Cambodia.
- Security of Australian aid workers is of great concern to the Australian Government and is kept under close scrutiny. Many consultants have reservations about working in Cambodia, particularly in rural areas. Until this improves, this will be an issue for program planning/design and a major risk to project implementation. All projects should have in place appropriate security plans.
 - The enormous deficiencies in the human resource base and the limited capacity of the Government to support its development efforts require among other things that:
 - all activities include a capacity building component
 - Australia rethink traditional approaches which assume dedicated counterpart inputs and government support. Given the number of donor interventions and limited domestic Cambodian capacity and resources, undue pressure for dedicated counterpart inputs could well create unsustainable burdens on Cambodia human, physical and financial resources.
 - It is important to recognise the limitations of Cambodia's national government bureaucracy in relation to rural service delivery. The bureaucracy has a role to play in supporting appropriate policy and institutional reforms to accelerate and deepen the pace of rural development. But it is too weak to actually control activities in a sector and/or fully develop services. Community level initiatives and the private sector will therefore have an important role to play. The program must therefore:
 - Continue to support the work of Australian Non-Government Organisations which have successfully worked at the grassroots level in rural areas of Cambodia for many years, including through their inclusion in project training activities which aim to strengthen the provision of public services in the health and education sectors. Given the role of the non-government sector in providing a bridge between the current low capacity within, including in project training activities; and
 - Attempt to broaden its focus to include support for a small-scale, locally oriented private sector which is gradually emerging in rural areas with a particular focus on the agriculture sector where AusAID has the advantage of being able to capitalise on its very long-term involvement in rice research and the agricultural extension system;

- Given the stage of development in Cambodia and the weakness of Government, there are significant risks inherent in all activities. In these circumstances, it is proposed to minimise risk by identifying known solutions to well understood problems and seeking to deliver the solutions to the rural populations most able to absorb such support. This means accepting that projects need not always focus on the poorest people in the poorest regions of the country in the short-to-medium term.
- The economic, social and political transition process in Cambodia is compounding the complexities of equitable community level participation in development planning, implementation, institution-building and the equitable sharing of resources. The views and roles of women must be fully considered in the planning and implementation of projects both as potential contributors and beneficiaries in order to ensure meaningful and viable project implementation.
- Key strategies to facilitate the incorporation of gender objectives include:
 - Gender sensitisation/training of staff, including provision for ongoing discussion of gender concerns rather than gender sensitisation being perceived as a one-off training exercise;
 - Sufficient financial resources to be made available to ensure consultation with, and active participation of, women in gender-related project activities;
 - Ensuring that technical recommendations in sectors such as agriculture, where women play a very significant role, are appropriate to the circumstances of low-income subsistence-oriented households including those headed by women; and
 - Analysing the factors which lead to successful gender-balanced participation in activities (eg provision of childcare, food stipends, location of activities) so that appropriate participative models can be adopted in future programs and activities.

Supporting Cambodia’s Own Agenda and Priorities and Working Collaboratively with Other Donors/International Organisations

6.1 The Government of Cambodia is gradually operationalising a public investment management system to help to ensure that resource allocation is in harmony with the Government policies and planning priorities. Australia strongly supports this process. In consequence Australian aid projects should now be increasingly designed in parallel with sectoral ministry initiatives and action plans under the public investment programs.

6.2 It is also considered essential that Australia and other donor/international agencies work in close collaboration to ensure that programs are complementary, and that they reinforce sound government policies and institutional structures. A coordinated approach optimises the use of scarce resources and helps to ensure that programs can be absorbed and maintained by the Cambodian Government in the longer term.

Approach

7.1 The challenge that the country now faces is how to sustain economic growth and translate it into broad-based improvements in the well-being of the Cambodian people, particularly in rural areas.

7.2 Building on Australia’s existing program of assistance to Cambodia, the following strategies will be adopted in order to assist the Government of Cambodia to ***achieve reductions in***

the incidence of poverty and make a transition towards sustainable, more broadly-based development:

i) Improve productivity and profitability in the agriculture sector. In 1996, the World Bank estimated that 39% of Cambodia's total population was living below the poverty line with the highest number being in the rural sector.

Given that over 90% of Cambodia's rural population is engaged in agriculture, it is considered that a process of development which has its main starting point in agriculture would be in line with the need to promote economic growth with the broadest possible base. It is also crucial to achieving the goals of food supply stability and poverty alleviation:

- The dominant role of agriculture as a source of both food security and income for the people means that even moderate improvements in productivity will have a noticeable effect on human welfare and on incomes;
- The potential for increased production both in absolute terms and in yield per land unit and per working hour must be regarded as very good as the current bases are very low; and
- The potential for increased profitability in agriculture by means of improved distribution channels and the establishment of more efficient markets, is also considerable.

Agriculture is currently the largest single sector within the Cambodian bilateral aid program (representing an estimated 26% of development assistance in 1998/99). This support includes two major projects in critical areas of agriculture development, namely rice based farming systems research and agricultural extension. These projects provide the skills and resources to identify the technology required to improve agricultural productivity and make it accessible to farmers in a farming systems approach which recognises their socio-economic circumstances. But additional support to achieve productivity gains is essential if returns on our investments in research and extension are to be realised.

It is therefore planned that a major new agriculture sector project will be developed and introduced into the program in 1999/2000. The intention of this support would be to use the research technology and extension infrastructure to deliver assistance which will bring real productivity gains to farming households. This support should take Cambodian farmers beyond their current level of marginal subsistence and thus assist in breaking the poverty cycle.

A number of options have been considered and, following a period of consultation, agreement was reached between the two governments on a preferred project option which aims to improve the quality of agricultural produce so as to make this produce more competitive in the commercial market. Building on "lessons learnt", the project will be designed with the following considerations in mind:

- The project should be relatively simple and focussed;
- Project target districts will be selected on the basis of an assessment that they will allow a direct and positive impact on agricultural productivity in Cambodia;
- Highest priority will be accorded to rice seed production and rice milling supported as necessary by agriculture infrastructure development and capacity building.

Australia's long-standing support for rice research in Cambodia is scheduled to end in 2001 and

the Cambodia Agriculture Extension Project will effectively come to an end in the first quarter of 2000. Consistent with the expectation that Australian intervention in all sectors will be part of a long-term involvement further support for research and extension activities in Cambodia is anticipated. Mid term reviews will be conducted in relation to both activities and will provide initial views on possible future support directions.

Overall, it is anticipated that Agriculture will increase to approximately 35% of the Australian bilateral program to Cambodia by 2000/2001. As health and education will remain priority sectors for the program, the resources required for the increased focus on agriculture will need to come from an overall increase in the program budget or from reductions in expenditure in areas such as multisector and good governance and human rights.

ii) Maintain a strong focus on basic human resource development. There are compelling reasons to give development of human capital very high priority in Australia's aid strategy for Cambodia. Low educational levels and inadequate standards of health care constitute critical constraints on both economic and social development. The prevalence of poverty among uneducated heads of households is 47% as compared to 30% for those who have completed secondary education. Mortality figures reflect the poor state of public health provision in Cambodia. Only 50% of the population has access to public health facilities. Experience suggests that economic growth alone can take an inordinately long time to improve social and human indicators and that it is possible to short-circuit the process by selective and targeted human development and anti-poverty interventions in health and education. Human resource development should therefore continue to be a key theme for the Australian aid program to Cambodia:

- All program activities will include training components.
- There will be targeted interventions in health (particularly primary health care delivery outside the major population centres). These interventions will include a major ongoing project to support the Cambodian Government to implement its national primary health care policy and support for a range of NGO activities also focusing on primary health care. Australia has also agreed to provide funding to UNICEF and WHO for immunisation programs in Cambodia commencing in 1999. Support to the health sector is expected to increase to approximately 20% of Australia's bilateral aid program to Cambodia by 2000/2001.
- Australian support for vocational education, adult literacy and skills training will continue. Activities implemented through Australian and local NGOs, including those which focus on skills training for women and/or other disadvantaged groups, are an important part of this strategy. These activities will compensate those without physical assets by providing them with human capital to enhance their productivity and food security.
- In the formal sector, Australia is assisting with the establishment of a credible high school examination system and providing English language training to Ministry officials. Around 50 students are currently studying in Australia on full scholarships in fields such as agriculture, engineering, health, economics and administration and education.
- Increased levels of support for the education sector in Cambodia are unlikely to be possible within the period of the current strategy. However, the education sector would receive high priority if additional resources become available. Technical and vocational education is currently considered to be the area where future Australian education assistance could achieve the greatest impact given known capacity constraints within the Ministry of Education.

- It would be timely in a post-election environment in Cambodia, and in line with Australia's Education and Training Policy; which requires the development of training strategies within the context of the overall Country Program Strategy, to conduct a review of training. This review could provide an overview of the role of training as a mechanism within the bilateral program, investigate the desirability of introducing a short-course training component, assess the current Australian Development Scholarships program and associated English Language Training and consider further options for these programs. The review will also examine strategies to increase gender equity in training programs.

iii) Strengthen the institutional base. There is a very close relationship between the growth of prosperity and stability and good governance. It is therefore appropriate that Australia's aid strategy for Cambodia should focus on rebuilding Cambodia's institutional structures and administrative capacity as quickly as possible.

There is a severe shortage of administrative and technical skills in Cambodia. In addition, the transformation towards democratic government and a liberalised, market-based economy requires a fundamental transformation of institutional structures that is far from complete. At present, the Government's ability to take responsibility for its development programs is limited due to a very low revenue base and weaknesses in procedures for planning and controlling expenditure. Progress in the reform of public administration is essential if developmental effort is to yield any substantial and lasting impact.

Australia can assist through specific institutional strengthening projects. However, in a generally ineffective, poorly motivated and ill-equipped Cambodian public sector, there is a need to carefully consider the practicalities of providing such support. An integrated programming approach which supports the reform of public administration in the context of projects designed to improve service delivery would be appropriate.

The World Bank, UNDP, IMF and the ADB are the key players in relation to macroeconomic reform, civil service reform, and improved fiscal governance (including in relation to management of forest resources). As a relatively small player in absolute terms compared to the Banks and the UN, Australia cannot expect to play a major project role in these areas. But there would be scope to contribute to the wider efforts of these organisations. The extent to which Australia becomes involved in the area will be a matter for judgement depending on the disposition and commitment of the new (post November 1998) Cambodian government.

iv) Continue to target improved governance. Broad-based development with real humanitarian improvements is best achieved in an environment of strong economic growth and social development. But the impact of programs focusing on these issues can only be truly significant when they are in support of appropriate partner government policies and governance. The program will continue to recognise the very close relationship between the growth of prosperity and stability in Cambodia through continued support for an ongoing project targeting improved human rights standards within the criminal justice system, through capacity building for government officials in the context of ongoing projects in agriculture, health, education and training, through participative development in the implementation of project activities at the community level, and through targeted support for NGO activities in the area of human rights.

v) Continue to address demining and humanitarian relief needs. As discussed in Section 3, the problem of landmines and unexploded ordnance is a major humanitarian problem in Cambodia that requires special attention. To combat this problem and assist Cambodia in its reconstruction,

Australia should continue to provide significant assistance to the Cambodia Mine Action Centre, Cambodia's national humanitarian demining organisation. Australia should also continue to support NGO activities in mine clearance and awareness and rehabilitation for victims of landmines. This assistance also has a strong poverty focus as injury or death caused by landmines will plunge families even further into poverty because of a lower earning capacity. It is important to economic development in Cambodia in terms of opening up land for resettlement of internally displaced persons and landless poor and for agriculture. It will also complement the Australian Government's new policy of supporting the international ban on land mines.

The development assistance strategy for Cambodia must recognise the need to continue to provide support for refugee resettlement and rehabilitation activities, and emergency humanitarian relief as required.

v) Apply gender sensitive approaches to planning and implementation. According to a recent World Bank report based on the Cambodian Socio-Economic Survey, it does not appear to be the case in Cambodia that female-headed households are more vulnerable to poverty than those headed by males. The incidence of poverty averages only 35% in female-headed households compared with 40% in male-headed households. There are, however marked gender differences in social outcomes. Some of these favour boys, while others favour girls. For example, girls have much lower enrolment rates than boys in secondary school despite the fact that the estimated rate of return to secondary schooling is significantly higher for females than for males (20% versus 6%). On the other hand, infant mortality rate for boys is nearly 40% greater than for girls. These illustrations highlight the need for gender concerns to be taken into account at all stages of the project cycle. The Australian aid program to Cambodia recognises that this will involve a long-term process of awareness raising and application of gender sensitive approaches to all aspects of planning and implementation.

Australian efforts to help Cambodia provide services to its people across a range of programs in the key areas of education, health, rural development and governance will have direct benefits for women. The broad strategic approach to the incorporation of gender issues into aid activities with Cambodia is discussed under the lessons learnt section of this paper, at paragraph 5.9. Additional operational approaches will include: assessing gender requirements and social impact analysis at early stages of project preparation and implementation; allocating a portion of project resources to provide tangible and quantifiable benefits to women; inclusion of a program "window" for Australian NGOs to conduct a range of community development activities focusing heavily on the needs of women and including literacy, skills training, income generation activity, family food production, health, household nutrition and sanitation components; and institutional strengthening projects to encourage the participation of women at the strategic planning level.

vi) Undertake environmental assessment and management for all activities. The relationship between social and environmental sustainability is a particularly crucial issue in Cambodia. Presently, much of the country's resources are destroyed through short-term exploitation. For example, large timber concessions have been awarded, with unsustainably high harvesting intensity and royalties that account for about one-fifth of their economic value; and only a part of revenues from logging activities have been transferred to the national budget.

There has been considerable effort on the part of multilateral agencies to work with the Cambodian Government to improve policies and management in the forestry sector but for some time these efforts failed to bear fruit. Only with the formation of the new Government has evidence of decisive action on this critical issue emerged. Australia will continue to press the Cambodian Government to improve policy and management in the forestry sector as part of its

ongoing dialogue on development assistance across a range of fora including annual Consultative Group Meetings and High Level Consultations. However, until such time as there is clear evidence of sustained commitment on the part of the Cambodian Government to sustainable forestry practices, it is not seen as a viable option for Australia to engage in project activities in the forestry sector. This matter will need to be kept under review.

More generally, environmental assessment and management will be undertaken as a matter of course for all aid activities.

8. Performance Monitoring and Review

8.1 The implementation of the overall strategy will be monitored as follows:

- The extent to which the program will have achieved a greater focus on rural development;
- Adherence to a strategy of reducing the number of disparate and ad hoc activities in the bilateral program through the introduction of new project activities which reinforce existing activities in priority sectors;
- Support for the work of Australian non-government organisations to be provided on the basis of those organisations and activities that have successfully worked at the grassroots level in rural areas of Cambodia for many years;
- Maintenance of a full project pipeline in accordance with agreed priorities outlined in this strategy;
- Participation in international fora; maintenance of close consultation with Australian government and non-government agencies with an interest in Cambodia; ongoing consultation with the Government of Cambodia, including through the HLC process, and donor coordination meetings; and
- Ensuring that Australian assistance remains relevant through ongoing review of the program.

Table 3: Australian Development Assistance to Cambodia by Sector

| Sector | 1995/96 | 1996/97 | 1997/98 | 1998/99 (est) |
|-------------------------------------|-------------------|-------------------|-------------------|----------------------|
| Agriculture | 4,381,494 | 5,298,616 | 7,060,314 | 8,465,000 |
| Education | 4,630,122 | 4,124,550 | 3,316,612 | 4,655,000 |
| Food Aid / Refugees / Emergency | 7,530,343 | 5,654,775 | 5,560,702 | 4,035,000 |
| Good Governance & Human Rights | 1,346,045 | 1,596,073 | 4,995,469 | 3,515,000 |
| Health | 3,436,309 | 4,668,066 | 4,463,368 | 5,090,000 |
| Infrastructure | 3,360,434 | 5,452,472 | 2,465,687 | 630,000 |
| Mine Clearance & Related Assistance | 4,850,000 | 4,265,242 | 4,107,750 | 4,120,000 |
| Other / Multisector | 3,359,103 | 2,938,481 | 2,899,903 | 2,370,000 |
| Total | 32,893,850 | 33,998,275 | 34,869,805 | 32,880,000 |

**Australian Development Assistance to Cambodia by Sector
1998/99 (est)**

