

## Recent trade policy developments and possible implications for Cambodia's garment and footwear sector

### Part I – Trade policy developments

#### 1. Introduction

The garment and footwear sector has been the backbone of Cambodia's economy over the past two decades. Developments in trade policy, both recent and expected, could have a significant effect on the sector. This, in turn, would affect the Cambodian economy and workers' wages and working conditions.

This fifth issue of the ILO's Cambodian Garment and Footwear Sector Bulletin examines the possible implications of recent trade policy developments, including the withdrawal of the United Kingdom from the European Union; Cambodia's elevation from 'least developed country' (LDC) status to a lower middle-income country; and the improved access for Cambodian travel goods exports to the United States market.

Part I focuses on implications of these policy developments, while Part II contains a regular update of key statistics related to the garment and footwear sector in Cambodia.<sup>1</sup>

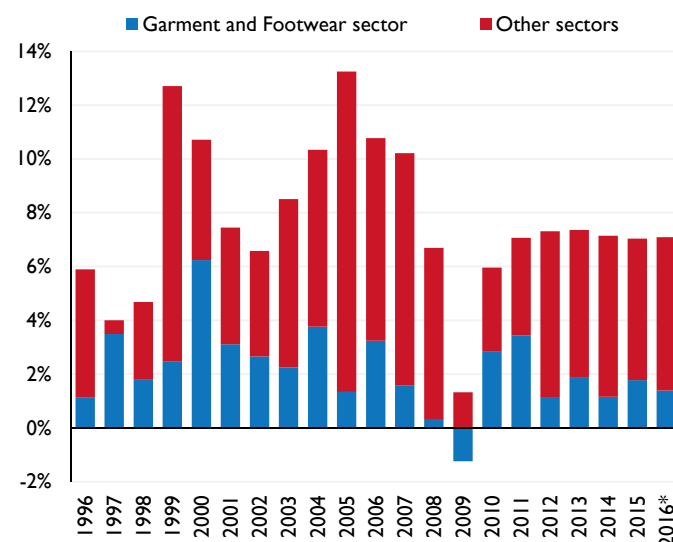
#### 2. Importance of the garment and footwear sector to Cambodia's economy

In 2015, the garment and footwear sector's value added represented 11 per cent of the economy and the sector contributed nearly two percentage points of the country's seven per cent GDP growth.<sup>2</sup> The sector's development has been driven by exports, with heavy dependence on the EU and US markets. Last year, some 80 per cent of Cambodia's total merchandise exports were garment and footwear products and they were mainly shipped to the EU (43 per cent) and US (29 per cent) markets.<sup>3</sup>

Cambodia's garment and footwear sector has grown impressively over the past two decades, starting from US\$ 80 million in exports in 1996 to become a US\$ 6.8 billion export

industry in 2015. It is the mainstay of the country's economy, earning billions of dollars of foreign exchange, employing hundreds of thousands of workers (87 per cent of whom are female)<sup>4</sup>, and playing an important role in alleviating poverty.<sup>5</sup>

Figure 1: Sectoral composition of Cambodia's real GDP growth (per cent)



\* IMF Projection (IMF Article IV Report No. 16/340, November 2016) and Cambodia's National Institute of Statistics (NIS)

Source: Cambodia's National Institute of Statistics, IMF and the Ministry of Economy and Finance

Trade policy changes that affect garment exports could have significant implications for the Cambodian economy. Three recent developments could have an effect on the sector, either positive or negative. These are:

- A. The United Kingdom's planned withdrawal from the European Union ("Brexit");
- B. The upgrading of Cambodia's economic status from an LDC to a lower middle-income country; and
- C. The US Government's decision to grant Cambodia preferential, duty-free access to the US travel goods market, from 1 July 2016.

<sup>1</sup> The analysis in this Bulletin is based on official statistics from various official sources including the European Commission (Eurostat), UNCTAD, Cambodia's Ministry of Commerce, the Ministry of Labour and Vocational Training, the Cambodia Investment Board, the General Department of Customs and Excise, the National Institute of Statistics and the National Bank of Cambodia. The ILO wishes to acknowledge and thank the Ministry of Labour and Vocational Training; the Ministry of Commerce; the Cambodia Investment Board; General Department of Customs and Excise, the National Institute of Statistics and the National Bank of Cambodia for their support and the data used in this publication. Any errors should be attributed to the ILO.

<sup>2</sup> Cambodia's National Institute of Statistics

<sup>3</sup> Cambodia's General Department of Customs and Excise (GDCE)

<sup>4</sup> Ministry of Commerce's statistic records of garment and footwear workforce (June 2016)

<sup>5</sup> Joint Report, the Ministry of Commerce of Cambodia and the Asian Development Bank (ADB): Cambodia's Garment Industry: Meeting the Challenges of the Post Quota Environment (October 2004, p. iii)

## A. The United Kingdom's planned withdrawal from the European Union ("Brexit")

The UK's departure from the EU could potentially have negative implications for Cambodia's export sector and economy. These negative implications could come about because:

- i) Depreciation of the UK's real exchange rate against the US dollar means that British consumers' spending on imported goods, including Cambodian-produced garments and footwear, may decline; and
- ii) Post-Brexit, the UK may not preserve the same level of preferential access for Cambodian exports;

### The importance of the EU market for Cambodia

The EU is Cambodia's largest export market; it absorbed nearly half (45 per cent) of Cambodia's garment and footwear exports during the first half of 2016.<sup>6</sup> The EU became the largest market for the sector's exports in 2014, surpassing the US market for the first time on record. The importance of the EU market has been increasing (see Figure 2), with Cambodia's garment and footwear exports to the EU market increasing from US\$ 645 million in 2009 to US\$ 2.9 billion in 2015. This increase was partly due to the 'Everything But Arms' scheme and the relaxation of the 'Rule of Origin'.<sup>7</sup>

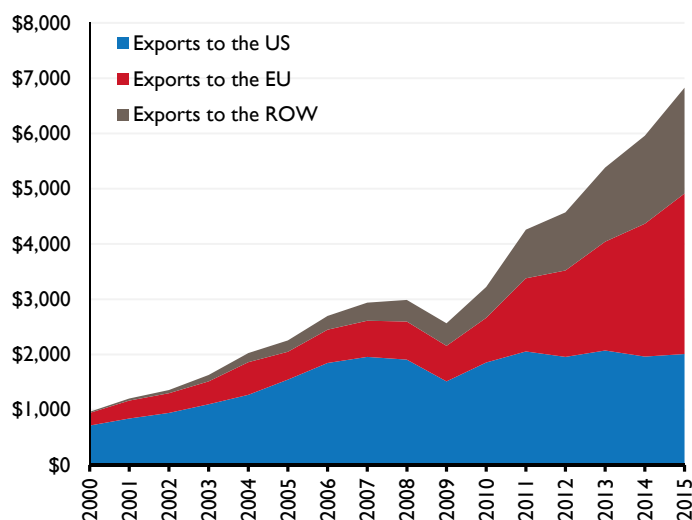
**Table 1: Share of EU's imports of garment and footwear products from Cambodia (by selected country, in per cent)**

	2000	2005	2010	2015	HI 2016
UK	30.1%	24.3%	28.0%	27.2%	24.3%
Germany	31.0%	50.1%	24.5%	22.1%	20.4%
Netherlands	7.1%	4.0%	15.3%	12.6%	12.0%
Spain	2.7%	6.2%	9.2%	10.5%	12.4%
France	11.6%	5.8%	4.2%	8.4%	10.5%
Italy	0.7%	1.3%	6.7%	7.8%	7.2%
Belgium	3.9%	2.3%	6.0%	3.8%	5.3%
Sweden	4.5%	2.0%	1.9%	1.4%	1.4%
Others	8.4%	4.0%	4.2%	6.2%	6.5%
Total EU 28	100%	100%	100%	100%	100%
o/w Euro19	63.1%	73.3%	68.8%	69.2%	71.7%

Source: EuroStat (retrieved on 18 October 2016)

The UK market is the most significant component of Cambodia's garment and footwear exports to the EU market.<sup>8</sup> Within the 28 EU member state countries, the UK has been the top buyer of Cambodia's exports from 2010 onwards; it alone absorbed nearly one-third of Cambodia's garment and footwear exports to the entire EU market last year. The UK market is of paramount importance for Cambodia's garment and footwear exports.

**Figure 2: Cambodia's garment and footwear exports to its major markets (2000-2015)**



Source: GDCE, Ministry of Economy and Finance

### Cambodia's current trade arrangements with the EU

The EU's 'Everything But Arms' (EBA) scheme gives the 49 Least Developed Countries, as classified by the UN, full duty-free and quota-free access to the EU market for exports of all products, except arms and ammunition.<sup>9</sup> Cambodia is one of these 49 countries. 'Everything But Arms' is part of the EU's 'Generalized System of Preferences' and an important scheme to help developing countries boost their economies by providing them with tariff preferences when selling on the EU market. Britain, as an EU member, extends tariff-free access to Cambodian garment and footwear products under the EBA scheme.

**Table 2: EBA beneficiaries in Asia and some selected non-EBA beneficiaries in Asia (considered as Cambodia's competitors):**

EBA beneficiaries in Asia	Selected non-EBA Beneficiaries in Asia
Afghanistan	China
Bangladesh	Indonesia*
Bhutan	Thailand
Cambodia	Viet Nam*
Lao PDR	
Myanmar <sup>10</sup>	
Nepal	
Timor-Leste	

Source: European Commission

([http://trade.ec.europa.eu/doclib/docs/2014/october/tradoc\\_152839.pdf](http://trade.ec.europa.eu/doclib/docs/2014/october/tradoc_152839.pdf))

\* Eligible for EU General Arrangements GSP (Standard GSP) which grants duty reductions for ca. 66% of all EU tariff lines to countries of low or lower-middle income, which do not benefit from other preferential trade access to the EU market. China and Thailand graduated out of the Standard GSP scheme on 1 January 2015.

<sup>6</sup> Cambodia's General Department of Customs and Excise (GDCE).

<sup>7</sup> Information from Cambodia's Ministry of Commerce website. Available online at: <http://www.moc.gov.kh/en-us/faqs/catid/5/contentid/14>

<sup>8</sup> European Commission's EUROSTAT.

<sup>9</sup> The EBA scheme was adopted by EU Council resolution 416/2001, with effect from 5 March 2001 (<http://www.moc.gov.kh/en-us/faqs/catid/5/contentid/14>),

<sup>10</sup> Following the decision by the Conference of the International Labour Organization (ILO) to lift its negative opinion on Myanmar on 13 June 2012, the EU reinstated GSP preferences for the country on 19 July 2013, with retroactive application as from 13 June 2012. GSP preferences were withdrawn from Myanmar in 1997 due to serious and systematic violations of the principles of the ILO Convention on forced labour.

There are also a number of other countries in Asia who are beneficiaries of the EU's EBA scheme, including Bangladesh, Lao PDR, and Myanmar which are competing for the important market share of the EU. The EBA utilisation rate<sup>11</sup> has increased over time (from 83.1% to 87.1%)<sup>12</sup> and it varies substantially from country to country. Bangladesh is by far the biggest user of the EBA scheme, followed by Cambodia. In 2014, these two beneficiaries together accounted for 85.4% of all imports where EBA preferences were used.<sup>13</sup>

### What might Brexit mean for the Cambodian garment and footwear sector?

It is unclear whether Cambodia's preferential access to the UK market will remain after Britain withdraws from the EU. Some possibilities are:

- The UK maintains the current preferential trade arrangements (duty-free and quota free) for all Least Developed Countries (LDCs); or
- The UK reverts to WTO rules, under which countries with which it doesn't have a free trade agreement (FTA), such as Cambodia, would no longer automatically receive preferential access.

If the UK reverts to WTO rules, Cambodian policy makers may pursue an FTA to maintain preferential access.

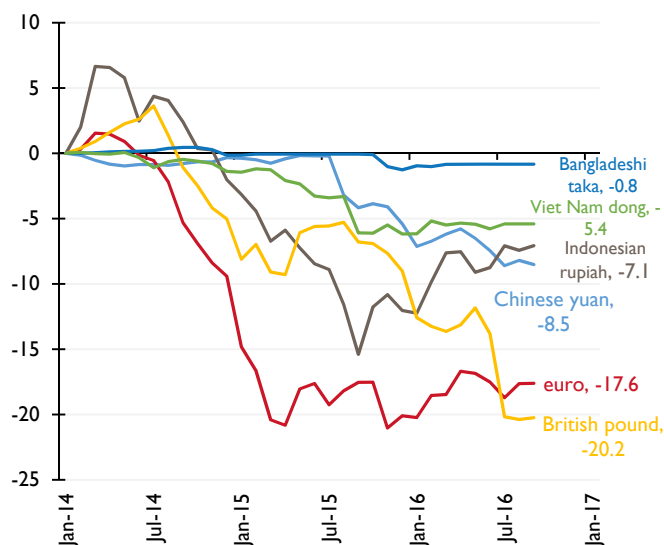
### Depreciation of the British pound against the US dollar

The British pound has depreciated significantly against the US dollar in recent months and it appears that the depreciation is likely not temporary. According to the IMF<sup>14</sup>, the pound has depreciated consecutively for the 24 months ending in September 2016. The value of the pound was around 20 per cent lower in the third quarter of 2016 than it had been in the same quarter of 2015.

The significant depreciation of the pound means that imported products have become more expensive for the British consumers. This includes goods imported from Cambodia. Cambodia is a highly dollarized-economy, with a minimum wage and many other costs denominated in USD.<sup>15</sup>

Although Britain has not yet withdrawn from the EU, the depreciation of its exchange rate means that the trading environment has already become more difficult for the Cambodian garment and footwear sector. If this depreciation is long-lasting, this difficulty will endure.

**Figure 3: Exchange rate of selected economies against the US dollar (percentage change since Jan 2014)**



Source: IMF and the Central Bank of Bangladesh

The currencies of some other major garment and footwear exporting countries have also depreciated against the US dollar, including the Chinese yuan, Vietnamese dong and Bangladesh taka. These countries' exports have therefore become more competitive relative to Cambodian exports. The Chinese yuan depreciated by 6.4 per cent against the US dollar between the third quarter of 2015 and the third quarter of 2016, while the Vietnamese dong depreciated by 1.2 per cent per over this same period. The Bangladeshi taka also depreciated by nearly 1 per cent.<sup>16</sup> The depreciation of these other garment producing countries' currencies means that their exports will not be negatively affected by the British depreciation to the same extent as Cambodia. British imports are likely to decline overall (due to the real depreciation of the GBP) while the composition of its remaining imports shifts, at the margin, away from Cambodian products.

Brexit could pose short-term risks to Cambodian garment and footwear exports via its effect on Britain's exchange rate, while longer-term risks are posed by the potential loss of tariff-free access to the UK market.

### B. The upgraded economic status of Cambodia

In July 2016, the World Bank reviewed the economic status of its 189 member countries and 28 other economies with populations of more than 30,000.<sup>17</sup> It divided economies into

<sup>11</sup> The utilisation rate of a given preferential regime is calculated as the share of imports eligible to this regime (reference from Fabien CANDAU & Sébastien JEAN, No 2005 – 19 December).

<sup>12</sup> This rare refers to year 2014 (2015 rate is not yet available)

<sup>13</sup> EU Commission Report to the European Parliament and the Council (dated 28 January 2016) on Generalized Scheme of Preferences (GSP) over 2014-2015 period.

<sup>14</sup> IMF's Exchange Rate Archives by Month. Available online at [http://www.imf.org/external/np/fin/data/param\\_rms\\_mth.aspx](http://www.imf.org/external/np/fin/data/param_rms_mth.aspx)

<sup>15</sup> As an indication of the extent to which the Cambodian economy is dollarized, it should be noted that foreign currency deposits account for 83 per cent of the country's broad money (according to monetary database of the National Bank of Cambodia).

<sup>16</sup> IMF's Exchange Rate Archives by Month. Available online at [http://www.imf.org/external/np/fin/data/param\\_rms\\_mth.aspx](http://www.imf.org/external/np/fin/data/param_rms_mth.aspx) and Treasury of the UN Operational Exchange Rates, available online at <https://treasury.un.org/operationalrates/OperationalRates.php#V>

<sup>17</sup> <http://www.worldbank.org/> (calculation uses its Atlas method)

four income groups according to 2015 gross national income (GNI) per capita as follows:

- 1 - Low income, \$1,025 or less;
- 2 - Lower middle income, \$1,026–4,035;
- 3 - Upper middle income, \$4,036–12,475; and
- 4 - High income, \$12,476 or more.

Cambodia's GNI per capita reached US\$ 1,070 in 2015, up from US\$ 1,020 in 2014.<sup>18</sup> Cambodia therefore qualified for a reclassification and graduation from low to lower-middle income status. Cambodia shares its new status with 52 other economies, including Viet Nam, Indonesia and the Philippines. Cambodia is one of only six countries to be reclassified upward by the World Bank in 2016<sup>19</sup>, although it continues to be classified as an LDC by the United Nations for the time being.<sup>20</sup>

While the upgrading reflects Cambodia's economic advancement, there is a potential downside. Cambodia's LDC status has meant that it is eligible for the EU's EBA scheme, under which it can access the 28 EU member country markets duty-free and quota-free. These preferential arrangements may eventually be withdrawn as Cambodia is no longer an LDC, which would harm Cambodia's competitiveness.

What happens when a country is no longer considered 'least developed' by the UN? According to the European Commission, "when countries successfully move up the development ladder, their efforts are recognized and they are no longer considered 'least developed' by the UN. Thus, EBA preferences are no longer required. The smooth progression into this change in status is guaranteed by a generous transition period of three years, during which time EBA preferences will continue to apply. This helps mitigate possible trade flow shocks and is a reflection of the EU's commitment to the continued progress of the developing world".<sup>21</sup> The UN's classification of economies is multidimensional, relying on more than just GDP per capita, but the upgrading of Cambodia's status by the World Bank could be an indication that an upgrade by the UN may follow.

Because of this transition period, Cambodia's exports to the EU are likely to be unaffected in the short term, but Cambodia needs to be well prepared to deal with the medium-term implications of the change in its developmental status.

### C. Preferential access to the US travel goods market

The US government recently amended its Generalized System of Preferences (GSP) and announced that it has granted Cambodia tariff-free access for travel goods exports to the US

market, effective 1 July 2016.<sup>22</sup> The US has only granted travel goods GSP status to a small number of 'least-developed beneficiary countries' and African Growth and Opportunity Act countries.

The removal of US customs tariffs on Cambodian-made travel products such as suitcases, handbags, wallets, vanities and similar products is widely believed to be an important trade policy to help boost Cambodia's travel goods export-oriented industry. Cambodian travel goods previously faced US tariff rates of between 3.4 and 20 per cent, and can now enter the US market duty-free. The US is currently the largest export destination for Cambodian travel goods.

**Table 4: Cambodia's travel goods exports to its major markets (million US\$)\***

	2014	2015
To the US market	US\$ 21.0	US\$ 50.4
Approximate duty paid (MFN)	US\$ 3.4	US\$ 8.5
Average duty rate paid	16.5%	16.5%
Duty rate range	3.4% to 20%	3.4% to 20%
To the EU 28 market	US\$ 8.1	US\$ 27.5
Duty free	0.0%	0.0%
<b>Total exports</b>	<b>US\$ 57.3</b>	<b>US\$ 91.6</b>
% of exports to US markets	36.6%	55.0%
% of exports to EU markets	14.1%	30.0%
% of total exports to EU and US markets	50.8%	85.0%
% of total global travel goods export markets	0.09%	0.15%

Source: US International Trade Commission, EuroStat and UNCTAD  
 \* Note: Refer to Harmonized Tariff Schedule 4 digit (4202) travel goods categories which include (travel goods, vanity cases, binocular and camera cases, handbags, wallets, cutlery cases and similar containers of various specified materials)

Cambodia's travel goods industry remains in its infancy. Last year, Cambodia exported travel goods worth merely US\$ 91.6 million, representing only 1.3 per cent of its total garment and footwear exports. The US accounted for 55 per cent of Cambodia's 2015 travel goods exports. However, the growth dynamics of Cambodia's travel goods export industry appear to be very strong, with exports rising by 60 per cent in 2015 over 2014 levels. Cambodia's Ministry of Commerce and the Garment Manufacturers Association of Cambodia (GMAC) are optimistic that the zero tariff rate preferential treatment by the US will expedite the sector's growth momentum and attract more investment into the sector in the near future, which in turn would generate more job opportunities for Cambodians.<sup>23</sup>

<sup>18</sup> World Bank GNI per capita, Atlas method (current US\$)

<sup>19</sup> World Bank analytical classifications (GNI per capita in US\$, Atlas methodology)

<sup>20</sup> UN 2016, *World Economic Situation and Prospects 2016*, p.163

<sup>21</sup> European Commission Note 2014, "Everything But Arms (EBA) – Who Benefits?" ([http://trade.ec.europa.eu/doclib/docs/2014/october/tradoc\\_152839.pdf](http://trade.ec.europa.eu/doclib/docs/2014/october/tradoc_152839.pdf))

<sup>22</sup> Press Release of the US Embassy in Cambodia on 6 July 2016 on "Duty Free Access for Travel Goods Made in Cambodia" <https://kh.usembassy.gov/duty-free-access-travel-goods-made-cambodia/>

<sup>23</sup> According to the articles of the Phnom Penh Post and the Fresh News (dated 7 July 2016) reporting words of the Cambodia's Minister of Commerce and the Chairman of the Garment Manufacturers Association in Cambodia (GMAC)

The travel goods and handbags sector is a relatively high value industry compared to other industry segments, such as cut-make-trim garment operations. It therefore needs a higher level of skills from the workforce and investment in machinery and business processes to compete on quality. Preferential access for Cambodian made-travel goods to the US market will improve Cambodia's competitiveness relative to some of its peers. There is significant scope for growth - Cambodia's travel goods exports as a share of the total global travel goods export market was only 0.15 per cent in 2015. The US is the world's top buyer of travel goods; it imported US\$ 12 billion of travel goods in 2015, representing 20.2 per cent of global imports of travel goods in 2015, up from 18.7 per cent in 2014). The opening of tariff-free access to this market poses a significant opportunity for Cambodia.

**Table 5: Top 5 developing economy exporters of travel goods to global market (in % of global travel goods market)**

	2000	2005	2010	2015
Developing economies	68.5%	60.3%	65.5%	65.6%
China	23.5%	31.1%	44.4%	46.1%
Hong Kong, China	28.7%	20.3%	13.2%	7.7%
Viet Nam	1.0%	1.3%	1.9%	4.0%
India	2.0%	2.2%	1.8%	2.0%
Singapore	0.3%	0.7%	0.8%	1.3%
Others	31.5%	39.7%	34.5%	34.4%
Total	100%	100%	100%	100%

Source: UNCTAD (Retrieved on 1 November 2016)

China is the top travel goods exporter in the world, with its 2015 travel goods exports representing 65.6 per cent of the global travel goods market. Viet Nam and Singapore have been gaining global share of travel goods market in recent years. Cambodia may be able to capture some of this market share in the future.

### 3. Conclusion

The Cambodian garment and footwear sector is likely to continue to be the largest exporting sector of its economy, at least over the medium term. Recent developments in trade policies are expected to pose both risks and opportunities for the country's export sector.

**Brexit:** The UK is a crucial market for Cambodia, as the largest importer of Cambodian garment and footwear products among the 28 EU member states. Brexit is already having an effect on Cambodia via its effect on the value of the pound; more significant effects are possible over the longer term if preferential trade access is lost. Without preferential access to the UK market, Cambodia would face greater competitive pressure with potentially negative consequences

for its garment and footwear exports and ultimately employment in the sector.

**Upgraded economic status:** The World Bank has upgraded Cambodia from a least developed country (LDC). This may presage a similar upgrade from the UN. If this occurs, Cambodia could ultimately lose its access to the EU's EBA scheme for LDCs. This will not occur for at least three years, as there are transitional arrangements in place. The Cambodian garment and footwear sector has some time to prepare for an environment in which its competitive advantage is reduced through loss of EBA status, but it will need to adapt to this reality over the medium-term.

**Travel goods GSP from the US:** The US market has been shrinking in relative importance as a destination for Cambodian garment and footwear exports. However, the opening of the duty-free access to the US travel goods market by the US for imports from Cambodia represents a significant opportunity for the sector. Cambodian industry stakeholders expect to see a boost of travel goods investment and exports in the coming years. The Cambodian government has been presenting and disseminating this new trade policy of the US to its potential and prospective investors. There are substantial opportunities.

It should be noted that GSP privileges can be withdrawn. The Office of the US Trade Representative was recently quoted as saying that "country's GSP privileges could be limited or withdrawn if it is found to be in violation of internationally recognised standards for worker rights, among other things."<sup>24</sup> Compliance with international labour standards should therefore be a crucial element of Cambodia's industry strategy.

**Other developments:** There are other potential trade policy developments that could affect Cambodia, including a free trade agreement between the EU and Viet Nam. The text of the agreement was published on 1 February 2016. It will be presented by the European Commission to the EU Council of Ministers for approval and ratification by the European Parliament. The agreement would eliminate nearly 99 per cent of tariffs on trade between Viet Nam and the EU.<sup>25</sup> This could erode Cambodia's competitiveness in of garment and footwear export products. The Trans-Pacific Partnership (TPP), if enacted, could also have significant ramifications for Cambodia and other countries in the region. The TPP would create a trading bloc that would include Viet Nam and Malaysia, but not Cambodia. The prospects of the TPP being enacted are unclear.

<sup>24</sup> Quoted it from the Phnom Penh Post, dated 7 July 2016 that referenced from the Office of the US Trade Representative (USTR)

<sup>25</sup> The EU and Viet Nam Finalise Landmark Trade Deal, Brussels 2 December 2015, available at (<http://trade.ec.europa.eu/doclib/press/index.cfm?id=1409>)

## Part II - Statistical update

Part II of this Bulletin provides a regular update regarding recent developments in the sector.

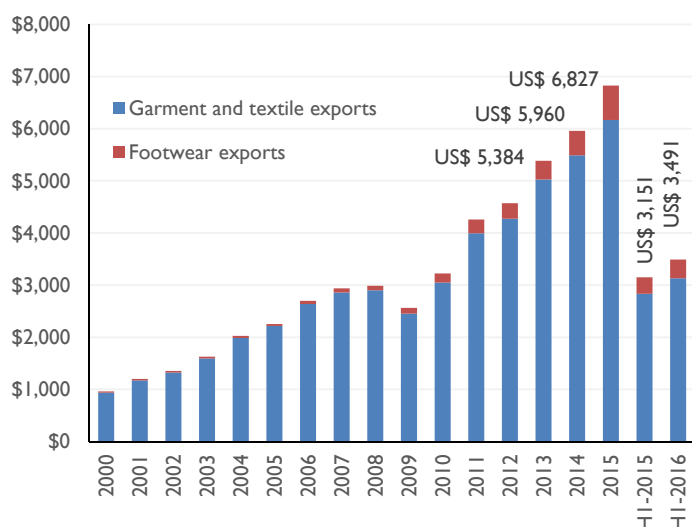
### I. Garment and footwear exports

According to Cambodia's General Department of Customs and Excise (GDCE), Cambodia's garment and footwear sector continued to grow during the first half of 2016, with exports expanding by 10.8 per cent to US\$ 3.5 billion in the first six months of the year. Garment and footwear exports made up 73 per cent of Cambodia's total exports of goods in the first six months of 2016.

Footwear exports grew by 13.4 per cent to US\$ 359 million in the first half of 2016 while exports of garments increased by 10.5 per cent to US\$ 3.1 billion during this same period.

The European Union (EU) market continued to be the largest buyer of Cambodia's garment and footwear products, accounting for 45 per cent of Cambodian exports in the first half of 2016, while the US market accounted for 25 per cent. The remaining 30 per cent was shipped to other markets, mainly Canada and Japan.

**Figure 4: Cambodia's garment and footwear exports, 2000–2016 (US\$ million)**



Source: Cambodia's General Department of Customs and Excise

Cambodia is among the top 10 exporters of garments and footwear among developing economies. Cambodia's global share of the garment and footwear export market rose from 0.7 per cent in 2005 to 1.5 per cent in 2015.<sup>26</sup>

China remains the world's top exporter of garment and footwear, accounting for 37.6 per cent of global exports,

followed by Viet Nam on 5.9 per cent, Italy's 5.2 per cent and Bangladesh with 4.4 per cent. Viet Nam and Bangladesh have both significantly increased their market share over the past decade. Viet Nam expanded its global market share from 2.1 per cent in 2005 to 5.9 in 2015 while Bangladesh increased its global share from 2.0 per cent in 2005 to 4.4 per cent in 2015. Cambodia also doubled its global share over this same period, from a lower base.

**Table 6: Cambodia's garment and footwear exports as share of global garment & footwear exports (per cent)**

	2005	2010	2011	2012	2013	2014	2015
Developing economies	64.9	68.4	68.1	69.8	69.8	69.6	71.2
1. China	25.7	35.1	35.3	37.5	37.8	37.8	37.6
2. Viet Nam	2.1	3.3	3.6	4.0	4.3	4.8	5.9
3. Bangladesh	2.0	3.3	3.6	3.7	3.9	3.9	4.4
4. Hong Kong, China	9.2	6.3	5.4	5.0	4.4	3.9	3.7
5. India	2.7	2.7	3.0	2.9	3.2	3.2	3.5
6. Turkey	3.3	2.8	2.6	2.7	2.7	2.7	2.6
7. Indonesia	1.8	2.0	2.0	2.0	1.9	1.8	1.9
8. Cambodia	0.7	0.9	0.9	1.0	1.1	1.2	1.5
9. Pakistan	1.0	0.9	0.8	0.8	0.8	0.8	0.8
10. Mexico	2.1	1.0	0.9	0.9	0.9	0.8	0.8
Others	35.1	31.6	31.9	30.2	30.2	30.4	28.8
World	100	100	100	100	100	100	100

Source: UNCTAD

### 2. New investments, factory openings and closures

**a – New investment:** new foreign investment continued to flow into Cambodia's garment and footwear sector during the first half of 2016. The Cambodian Investment Board (CIB) approved 60 new investment projects across all sectors, of which 25 were garment projects and six were in footwear.

While a large proportion of newly approved investment projects are in the garment and footwear sector, the value of these projects represented only seven per cent of the US\$ 1,782 million worth of all new approved investment. This ratio has declined from 28 per cent in 2014 and 10 per cent in 2015, indicating that there were increasingly higher valued investment projects in sectors other than garment and footwear.

China remains the leading source of investment in the field of garment and footwear sector in Cambodia. Of the approved new investment (in value terms) in the garment and footwear sector during the first 6 months of 2016, investors from mainland China represented 38 per cent, the UK accounted

<sup>26</sup> Cambodia's share of developing economies' garment and footwear exports was 2.0 per cent in 2015.

for 13 per cent, Taiwan provided 8 per cent, Hong Kong represented 4 per cent, with the remaining 37 per cent coming from elsewhere. The FDI-driven garment sector in Cambodia has remained concentrated in low-value-added activities, with Cambodian garment factories are mostly engaged in cut-make-trim processes. Design and higher-level production, export, and management decisions are predominantly made at the headquarters of the foreign parent companies, and technology spill-overs have been limited to date.<sup>27</sup>

**b – Opening, closure and operating factories:** according to the Ministry of Commerce, the number of operating garment and footwear factories fell by 95 in the first half of 2016. These net closures comprised 88 fewer garment factories and seven fewer footwear factories. In gross terms, 122 factories closed, while 27 new factories opened. The difference between these two is the net closures figure of 95<sup>28</sup>.

Some of the recorded closures represent garment factories that actually ceased operations over the period, while some of the recorded closures pertain to factories that actually ceased operations earlier. The Ministry updated its database by reclassifying a number of factories that had been inactive for months, and in some cases, had closed down but had not provided official notice. The total number of garment and footwear factories that are effectively operating stood at 604 at the end of June 2016, down from 699 at the end of 2015.<sup>29</sup>

It should be noted, that garment exports have continued to grow strongly. The sector's exports rose by 10.8 per cent in the first half of 2016 over the same period in 2015. This suggests that a large proportion of the recorded net factory closures are the result of statistical corrections, rather than actual factory closures.

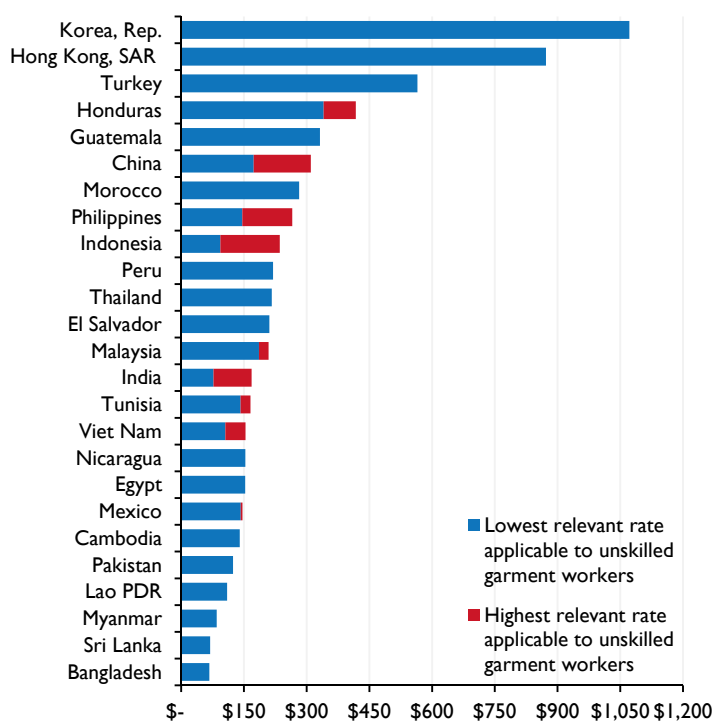
### 3. Employment and wages

According to the Ministry of Commerce, employment in the registered garment and footwear factories totalled 610,000 employees during the first half of 2016, a 0.6 per cent increase relative to the first six months of 2015.<sup>30</sup> The total wage bill of the industry reached US\$ 116 million a month, up from an average US\$ 109 million a month in 2015.

Minimum wages have risen in recent years across many major garment and footwear exporting countries in the region, including Cambodia. Cambodia's minimum wage in 2016, set at US\$ 140 a month, is higher than those of Pakistan (US\$ 124), Lao PDR (US\$ 110), Myanmar (US\$ 85) and some parts of Viet

Nam. Viet Nam has four different types of minimum wages with highest rate is set for the main cities (US\$ 154) and lowest rate (US\$ 106) is set for rural areas.

**Figure 5: Monthly minimum wages in the garment industry for the top 25 apparel-exporting countries** (as of 1 January 2016)



Source: ILO compilation based on national sources. Exchange rates are from IMF, except for Bangladesh and Viet Nam, which were sourced from xe.com (Use exchange rate of 1<sup>st</sup> January 2016).

Like many workers elsewhere, Cambodian workers are also entitled to other allowances and fringe benefits on top of the minimum wage. These include a monthly attendance bonus of US\$ 10, transportation & accommodation allowance of US\$ 7, and US\$0.5 per day of meal allowance for overtime. On average, workers' earnings are typically higher than the minimum wage, even though the base wage is commonly equal to or close to the minimum.

The average monthly earnings of Cambodia's garment and footwear workers increased from US\$ 145 in 2014, to US\$ 175 in 2015 and to US\$ 190 during the first half of 2016. In inflation-adjusted (real) terms, the average monthly wage<sup>31</sup> rose from US\$ 127 in 2014 to US\$ 151 in 2015 and to US\$ 161 in the first half of 2016.

<sup>27</sup> IMF: China's Changing Trade and the Implications for the CLMV Economies, Asia and Pacific Department, September 2016 (p. 57)

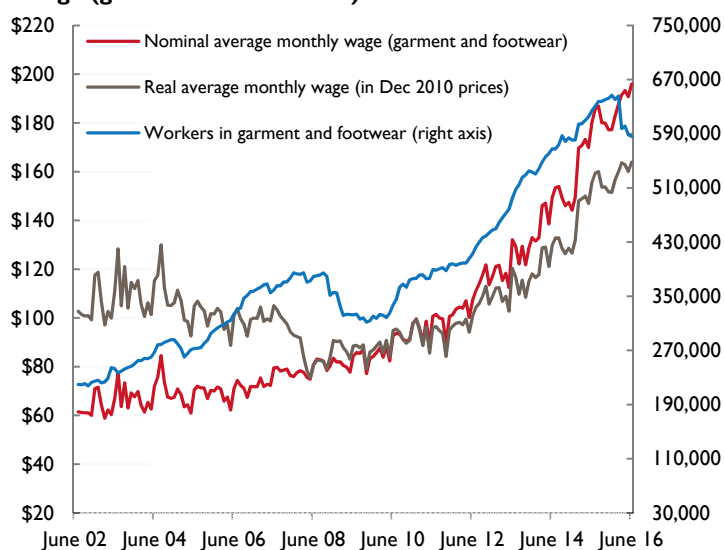
<sup>28</sup> The Ministry of Commerce had not yet released full-year factory opening and closure figures for 2016 at the time of publication. Statistics from the MoLVT have been quoted in the media (Fresh News on 7 January 2017 and the Phnom Penh Post on 10 January 2017); these statistics state that 141 garment and footwear factories closed down in 2016, while 149 new garment and footwear factories opened during the year.

<sup>29</sup> The number refers to exporting factories that are officially registered with the Ministry of Commerce only. Some sub-contractor factories (which are not directly exporting, nor officially registered) are not included.

<sup>30</sup> Based on six-month averages of monthly employment figures.

<sup>31</sup> ILO calculation based on December 2010 prices.

**Figure 6: Employment, nominal and real average monthly wage (garment and footwear)**



Source: Ministry of Commerce, National Institute of Statistics (NIS)

Some stakeholders have expressed concerns that the sector's productivity has not kept pace with real wage gains. The Garment Manufacturers Association in Cambodia (GMAC) has appealed for a renewed focus on productivity<sup>32</sup> and called upon clothing buyers to implement more sustainable purchasing practices. The GMAC is also in discussion with the Ministry of Labour and Vocational Training to launch a 'Productivity Campaign'.<sup>33</sup> The Prime Minister of Cambodia, during a televised-speech on the national television, dated 7 November 2016, suggested to strengthen technical capacity of current workers in the sector in order to improve output and quality<sup>34</sup>.

#### 4. Other policy developments relating to the garment and footwear sector

- The government will again raise the salary tax threshold from its current level of 800,000 riels (or US\$ 200) to a new threshold of 1,000,000 riels (US\$ 250), effective January 2017.<sup>35</sup> The revision of the tax threshold will reduce the number of workers, including garment and footwear workers, who are liable to pay income tax. This is the second increase of the threshold in two years.
- In addition, Cambodia's Ministry of Economy and Finance released a Circular indicating that non-salary allowances will no longer be included in monthly salary tax calculations.<sup>36</sup> Benefits that shall no longer be included in the salary tax calculation are:

1. Transportation and accommodation allowances.
2. Meal allowances provided to all workers without consideration of roles or positions.
3. National Social Security Fund or social well-being fund that are provided to workers/employees without consideration of roles and positions.
4. Health insurance or life insurance premiums and benefits that are provided to workers/employees without consideration of roles or positions.
5. Baby allowance or expense on baby day care centre.
6. Severance pay for employment termination or indemnity for dismissal.

The exemption of such benefits from tax has been in place for some time for garment and footwear workers; last year, the Ministry of Economy and Finance issued a similar circular to exclude non-salary allowances for their salary tax calculation.<sup>37</sup> This year Circular is aimed at supporting other low income earners in other non-garment and footwear sectors also.

- The National Social Security Fund (NSSF), a government-run insurance scheme covering workers' injuries, work-related illness and travel-related accidents, has been in place since mid-2008 (1<sup>st</sup> phase). On 6 January 2016, the NSSF's coverage was broadened to include healthcare services<sup>38</sup> (its 2<sup>nd</sup> phase) by commencing implementation from 1 May 2016 and starting from Phnom Penh, Kandal and Kampong Speu with a continual roll-out to other provinces<sup>39</sup>. According to the NSSF's half-year report, by June 2016, the NSSF has signed agreements with some 93 public hospitals and healthcare centres (including a few private healthcare centres) to provide these new healthcare services to its beneficiaries (its insured workers/employees).

<sup>32</sup> GMAC letter dated 20 Oct. 2015

<sup>33</sup> GMAC press release dated 24 May 2016.

<sup>34</sup> Fresh News (Cambodia) dated 7 November 2016

(<http://m.freshnewsasia.com/index.php/en/localnews/38814-2016-11-07-08-53-43.html>)

<sup>35</sup> Notice # 048 of the General Department of Taxation (GDT) of the Ministry of Economy and Finance (MEF) dated 6 January 2015, and, the Intervention report of the Minister of Economy and Finance during the 2017 Budget debate at the National Assembly (on 22 November 2016). The Cambodia's 2017 Budget Law was approved by the National Assembly on 22 November 2016.

<sup>36</sup> Ministry of Economy and Finance's circular #011 (dated 6 October 2016) on "Implementation of Obligation of Tax on Fringe Benefits"

<sup>37</sup> Ministry of Economy and Finance's circular #002 (dated 20 January 2015) on "Implementation of Obligation of Tax on Salary and Fringe Benefits"

<sup>38</sup> Government's sub-decree #01, dated 6 January 2016.

<sup>39</sup> Ministry of Labour and Vocational Training, Prakas #093 on "Setting of Timeframe and Phase of Implementation of the Social Security Scheme on Healthcare"



**Annex Table I. Cambodian garment and footwear industry – selected indicators**

	2014				2014	2015				2015	2016				2016
	Q1	Q2	Q3	Q4		Q1	Q2	Q3	Q4		Q1	Q2	HI	-	
<b>I. Economic output</b>															
<b>GDP (% real growth)</b>	-	-	-	-	7.1	-	-	-	-	7.0	-	-	-	-	7.0
<b>GDP (% nominal growth)</b>	-	-	-	-	10.0	-	-	-	-	8.9	-	-	-	-	12.0
<b>GDP (current prices, US\$ million)</b>	-	-	-	-	16 703	-	-	-	-	18 083	-	-	-	-	19 368
Value added (garment and footwear, current prices, US\$ million)	-	-	-	-	1 683	-	-	-	-	1 915	-	-	-	-	-
Value added (garment and footwear, % of GDP)	-	-	-	-	10.1	-	-	-	-	10.6	-	-	-	-	-
<b>2. Garment and footwear exports</b>															
<b>2a. Growth of total garment and footwear exports</b>															
<b>Garment and footwear exports (US\$ million) <sup>1/</sup></b>	1 464	1 379	1 625	1 493	5 960	1 549	1 602	1 995	1 681	6 827	1 773	1 718	3 491	-	-
% growth (year-on-year)	19.7	9.6	3.6	11.9	10.7	5.8	16.1	22.8	12.6	14.5	14.5	7.2	10.8	-	-
Garment exports (US\$ million) <sup>1/</sup>	1 359	1 271	1 502	1 357	5 489	1 400	1 434	1 832	1 501	6 167	1 605	1 527	3 132	-	-
% growth (year-on-year)	19.8	8.7	1.8	9.1	9.3	3.0	12.9	21.9	10.6	12.3	14.7	6.5	10.5	-	-
Footwear exports (US\$ million)	105	109	122	135	471	149	168	163	180	660	168	191	359	-	-
% growth (year-on-year)	19.2	20.1	33.1	50.6	30.8	41.7	54.4	33.6	33.0	40.0	12.9	13.8	13.4	-	-
<b>Retained imports of garment materials (US\$ million)</b>	-584	-672	-643	-671	-2 571	-616	-816	-813	-705	-2 949	-710	-846	-1 556	-	-
<b>2b. Garment and footwear exports by main destination</b>															
<b>Total exports (garment and footwear, US\$ million)</b>	1 464	1 379	1 625	1 493	5 960	1 549	1 602	1 995	1 681	6 827	1 773	1 718	3 491	-	-
To United States (garment and footwear) <sup>1/</sup>	531	452	511	469	1 964	491	494	585	439	2 009	429	440	870	-	-
To European Union (garment and footwear) <sup>1/</sup>	533	559	674	639	2 404	617	686	844	757	2 904	793	777	1 570	-	-
To rest of world (garment and footwear) <sup>1/</sup>	400	368	440	385	1 593	440	422	566	486	1 914	550	501	1 051	-	-
<b>Total exports (garment, US\$ million) <sup>1/</sup></b>	1 359	1 271	1 502	1 357	5 489	1 400	1 434	1 832	1 501	6 167	1 605	1 527	3 132	-	-
To United States (garment) <sup>1/</sup>	512	437	494	446	1 889	462	461	557	408	1 888	400	409	809	-	-
To European Union (garment) <sup>1/</sup>	482	500	616	575	2 173	546	600	768	670	2 583	714	679	1 393	-	-
To rest of world (garment) <sup>1/</sup>	365	334	392	337	1 427	392	373	508	424	1 696	491	439	930	-	-
<b>Total exports (footwear, US\$ million)</b>	105	109	122	135	471	149	168	163	180	660	168	191	359	-	-
To United States (footwear)	19	15	17	23	74	29	33	28	31	121	29	32	61	-	-
To European Union (footwear)	51	59	58	64	231	72	86	76	86	321	79	97	177	-	-
To rest of world (footwear)	36	34	48	48	166	49	49	58	62	218	60	62	122	-	-
<b>3. New Investment, factory openings and closures</b>															
<b>3a. New Investment Project</b>															
<b>Total CIB approved investment projects</b>	44	48	42	15	149	37	26	30	31	124	37	23	60	-	-
<b>Thereof: Garment and footwear projects <sup>1/</sup></b>	25	32	15	6	78	19	19	20	14	72	22	9	31	-	-
Garment projects	24	29	13	6	72	17	12	15	13	57	18	7	25	-	-
Footwear projects	1	3	2	0	6	2	7	5	1	15	4	2	6	-	-
<b>Total CIB approved projects (US\$ million)</b>	446	382	626	150	1 604	2 873	255	279	513	3 920	955	827	1 782	-	-

	2014				2015				2016				2016		
	Q1	Q2	Q3	Q4	2014	Q1	Q2	Q3	Q4	2015	Q1	Q2		H1	
<b>Thereof: Garment and footwear projects (US\$ million) <sup>1/</sup></b>	<b>135</b>	<b>200</b>	<b>86</b>	<b>30</b>	<b>452</b>	<b>72</b>	<b>80</b>	<b>84</b>	<b>141</b>	<b>377</b>	<b>86</b>	<b>42</b>	<b>128</b>	-	-
Garment projects (US\$ million)	127	174	77	30	408	64	42	64	55	225	71	31	101	-	-
Footwear projects (US\$ million)	7	27	9	0	44	8	38	20	86	151	15	11	26	-	-
<b>3b. Factory openings and closures (registered factories) <sup>1/</sup></b>															
<b>Total garment and footwear factories (end of period)</b>	<b>548</b>	<b>576</b>	<b>597</b>	<b>626</b>	<b>626</b>	<b>640</b>	<b>655</b>	<b>680</b>	<b>699</b>	<b>699</b>	<b>589*</b>	<b>604</b>	<b>604</b>	-	-
Garment factories (e. o. p.)	488	515	532	558	558	572	585	607	626	626	526	538	538	-	-
Footwear factories (e. o. p.)	60	61	65	68	68	68	70	73	73	73	63	66	66	-	-
<b>Total net openings (garment and footwear) <sup>1/</sup></b>	<b>20</b>	<b>28</b>	<b>21</b>	<b>29</b>	<b>98</b>	<b>14</b>	<b>15</b>	<b>25</b>	<b>19</b>	<b>73</b>	<b>-110*</b>	<b>15</b>	<b>-95</b>	-	-
Garment factories	19	27	17	26	89	14	13	22	19	68	-100	12	-88	-	-
Footwear factories	1	1	4	3	9	0	2	3	0	5	-10	3	-7	-	-
<b>Openings (garment and footwear) <sup>1/</sup></b>	<b>22</b>	<b>33</b>	<b>25</b>	<b>29</b>	<b>109</b>	<b>14</b>	<b>16</b>	<b>26</b>	<b>19</b>	<b>75</b>	<b>12</b>	<b>15</b>	<b>27</b>	-	-
Garment factories	20	31	21	26	98	14	14	23	19	70	10	12	22	-	-
Footwear factories	2	2	4	3	11	0	2	3	0	5	2	3	5	-	-
<b>Closures (garment and footwear) <sup>1/</sup></b>	<b>2</b>	<b>5</b>	<b>4</b>	<b>0</b>	<b>11</b>	<b>0</b>	<b>1</b>	<b>1</b>	<b>0</b>	<b>2</b>	<b>122*</b>	<b>0</b>	<b>122</b>	-	-
Garment factories	1	4	4	0	9	0	1	1	0	2	110	0	110	-	-
Footwear factories	1	1	0	0	2	0	0	0	0	0	12	0	12	-	-
<b>4. Employment in the garment and footwear sector</b>															
<b>Total garment and footwear workers (period av., '000)</b>	<b>539</b>	<b>561</b>	<b>576</b>	<b>581</b>	<b>564</b>	<b>597</b>	<b>616</b>	<b>635</b>	<b>643</b>	<b>623</b>	<b>628</b>	<b>592</b>	<b>610</b>	-	-
% change (year-on-year)	17.6	16.5	11.7	9.1	13.5	10.7	9.8	10.3	10.7	10.4	5.3	-3.9	0.6	-	-
Workers in garment sector (period average, '000)	454	475	484	488	475	500	516	533	538	522	525	494	510	-	-
Workers in footwear sector (period average, '000)	85	87	92	93	89	97	101	102	106	101	103	98	101	-	-
<b>5. Wages and prices</b>															
<b>Minimum wage (garment and footwear sector, US\$)</b>	<b>100<sup>2/</sup></b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>128</b>	<b>128</b>	<b>128</b>	<b>128</b>	<b>128</b>	<b>140</b>	<b>140</b>	<b>140</b>	-	-
<b>Average monthly wage (garment and footwear, US\$)<sup>4/</sup></b>	<b>137</b>	<b>145</b>	<b>152</b>	<b>146</b>	<b>145</b>	<b>164</b>	<b>174</b>	<b>184</b>	<b>178</b>	<b>175</b>	<b>187</b>	<b>193</b>	<b>190</b>	-	-
Average monthly wage (garment workers, US\$) <sup>3/</sup>	139	147	153	146	146	165	176	188	181	178	190	195	193	-	-
Average monthly wage (footwear workers, US\$) <sup>3/</sup>	127	137	149	146	140	157	165	166	165	163	173	184	179	-	-
<b>Real average monthly wage (garment and footwear, constant Dec. 2010 US\$)<sup>3/ 4/</sup></b>	<b>121</b>	<b>127</b>	<b>131</b>	<b>127</b>	<b>127</b>	<b>143</b>	<b>151</b>	<b>158</b>	<b>152</b>	<b>151</b>	<b>160</b>	<b>162</b>	<b>161</b>	-	-
Real average monthly wage (garment, Dec. 2010 US\$) <sup>3/ 4/</sup>	123	128	132	127	128	144	152	161	154	153	162	164	163	-	-
Real average monthly wage (footwear, Dec. 2010 US\$) <sup>3/ 4/</sup>	113	119	129	127	122	137	143	142	141	141	148	154	151	-	-
<b>Consumer Price Index (period average) rebased, Dec. 2010=100</b>	<b>113.0</b>	<b>114.5</b>	<b>115.8</b>	<b>114.7</b>	<b>114.5</b>	<b>114.2</b>	<b>115.6</b>	<b>116.8</b>	<b>117.0</b>	<b>115.9</b>	<b>117.0</b>	<b>119.1</b>	<b>118.1</b>	-	-
<b>Inflation rate (CPI period average, y-o-y growth)</b>	<b>4.6%</b>	<b>4.8%</b>	<b>4.0%</b>	<b>2.1%</b>	<b>3.9%</b>	<b>1.0%</b>	<b>1.0%</b>	<b>0.8%</b>	<b>2.0%</b>	<b>1.2%</b>	<b>2.5%</b>	<b>3.0%</b>	<b>2.8%</b>	-	-

Note: GDP current prices, its real and nominal growth rate for 2016 is the IMF Projection (IMF's Article IV Report of Cambodia, November 2016)

1/ Includes textiles.

2/ Effective 1 February 2014.

3/ Based on Ministry of Commerce, effectively operating factories only. The data exclude foreign office workers and foreign managers.

4/ At December 2010 prices.

\*/ Note that a large proportion of the recorded closures are the result of the Ministry of Commerce's inspection and reclassification of on-going and temporary closed factories, which includes some inactive factories that closed down without notice to the Ministry.

Sources: National Institute of Statistics, Ministry of Commerce, National Bank of Cambodia, IMF and ILO Staff Calculation

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