AN EXAMINATION ON THE EFFECTIVENESS OF FOREIGN DIRECT INVESTMENT REGULATIONS IN CAMBODIA’S AGRICULTURE SECTOR

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Abstract

Over the past two decades, Cambodia has undergone a significant transition, reaching lower middle-income status in 2015. Authorities aspire to attain upper middle-income status by 2030. Driven by garment exports and tourism, Cambodia’s economy has sustained an average growth rate of 7.7% between 1995 and 2018, making it among the fastest-growing economies in the world. As global demand peaked in 2018, economic growth is estimated at 7.5%, compared to 7% in 2017 and is expected to remain robust over the medium term. (World Bank Group, May 2019) It was believed that one of the contributing factors for its economic growth was the increase in foreign direct investment (FDI) which already reached USD3.239 billion in 2018 (World Bank, 2019). Among all sectors, the Royal Government of Cambodia (RGC) sees agriculture as a driving force of economic growth and poverty reduction, with the emphasis on modernization of agriculture, for which FDI was believed to be the key.

However, in reality, agriculture FDI has caused many social and environmental problems in Cambodia, some of which developed into serious conflicts with local communities and indigenous people. In particular, the Economic Land Concession (ELC) policy, as the prime strategy for promoting agriculture FDI, has led to many land disputes that are still ongoing. While private sector investments and business operations in agriculture have generally negatively affected local communities and indigenous people, some organizations believe that the private sector, and in this case foreign investors, can play a crucial role in reaching solutions by adopting and implementing responsible and inclusive business practices.

The Royal Government of Cambodia has recently amended the “Law on Investment” to adopt the automatic approval system of the investment projects, which must be completed within 31 working days after the receipt by the Council for the Development of Cambodia (CDC) of the investment proposal, unless they are among the fields prohibited in the negative list or investment project related to the national interest/ environmental sensitivity. An investment approval will be issued not to an investor or investing enterprise but to a project. A project which receives the investment approval is called a Qualified Investment Project (or “QIP”). The amended “Law on Investment” governs all QIPs and defines the procedures by which any person establishes a QIP. The investment incentives are granted automatically to a QIP. The CDC is expected to act as One-Stop Shop and obtain all of necessary licenses required from relevant ministries entities listed in the Conditional Registration Certificate (CRC) for investment on behalf of the investment applicant. A QIP may be in the form of a joint venture. A joint venture may be formed between Cambodian entities, between Cambodian entities and foreign entities or between foreign entities. There is no limitation based on nationality or the share-holding proportion of each shareholder, except in the case a joint venture owns or intends to own land or an interest in land in Cambodia. In such a case, the maximum combined share-holding of all foreign parties must not exceed 49%. However, despite the success of attracting foreign direct investment in Cambodia, several challenges remain, mostly relating to the regulations of investment, including whether the current legal framework government investment in the country contributes positively towards attracting investment that boost the economy or detracts from the country as a prime investment destination.

The paper was written as a scoping and mapping process in order to inform the Royal Government of Cambodia, foreign investors and private sector, as well as communities and civil society about responsible and inclusive foreign direct investment and business practices so that all stakeholders involved can play a role in preventing or resolving human rights violations and conflicts and community participations at the early stage of investment, specifically in the country’s agriculture sector.

Keywords: Foreign Direct Investment, Sustainable Development Goals (SDGs), Economic Land Concessions (ELCs), Quantified Investment Project (QIP), Council for the Development of Cambodia (CDC), Qualified Investment Project (QIP).
Introduction

International and non-governmental organizations (NGO) have expressed critical concerns as to the potential effects of ELC holders’ activities on the poor local communities located nearby. International evidence regarding the costs and benefits of such investment suggests that though large-scale agricultural land exploitation could restrict local communities’ access to land and water, it could also contribute to the country’s economic development through investors’ participation in developing essential local infrastructure for agricultural expansion, particularly irrigation.

In a recent report conducted by the World Bank on Foreign Direct Investment in the agriculture sector in Cambodia, it was argued that through legal and regulatory frameworks for FDI are not the primary drivers of investment decision, they can tip an investment decision in favor of a particular economy. Strong, stable legal and regulatory frameworks help create transparent environments conducive for investment.

This study aims to examine the validity of some of the concerns expressed in Cambodia over the potential effects of FDI in agriculture and its sub-sectors, including crops, livestock, food processing, forestry and fisheries. It then analyses the policy and regulatory environment and institutions governing and facilitating such FDI, as well as prevailing business models, in the acquisition of agricultural land. The study tries to conclude by providing some policy recommendations in response to the challenges facing the sector. Thus, the study seeks to explore the correlation between the effectiveness of FDI regulations and the resulting host country’s economic development, with Cambodia as a case study for analysis.

The study is of the view that there is a deficit in the regulations of FDIs in Cambodia, specifically in the agriculture sector, which explains the failure in achieving policy objectives for economic development. The following questions guided the researcher in answering this vital issue:

- What is the state of legal and regulatory framework for FDI in Cambodia?
- What is the critical imperative for review of legal and regulatory framework for FDI in Cambodia?
- How extensive are foreign direct investors embed themselves in Cambodia’s local communities through their entrepreneurial activities in economic land concession development?
- How extensive do FDIs contribute to local development?
- How do Korean companies operate economic land concessions in local Cambodian communities?
- To what extent do Koran investors perform their entrepreneurial activities in the economic land concession development?
- How do Korean investors interact with their stakeholders in local communities?
- What value added do Korean companies generate in local communities and the Cambodian agriculture sector?

Since South Korean investors dominate investments in the agriculture sector in Cambodia, the following sub-research questions were explored in this study:

- How extensive do FDIs contribute to local development?
- How do Korean companies operate economic land concessions in local Cambodian communities?
- To what extent do Koran investors perform their entrepreneurial activities in the economic land concession development?
- How do Korean investors interact with their stakeholders in local communities?
- What value added do Korean companies generate in local communities and the Cambodian agriculture sector?

The objective of this study is to examine the efficacy of legal, regulatory, and institutional framework of foreign direct investment in Cambodia for the envisaged economy development, specifically in the agriculture sector.

Chinese and South Korean Investments

While Chinese investments are in the area of construction, South Korean FDIs are concentrated in the agriculture sector. The noticeable rise in foreign direct investment (FDI) in agricultural land in Cambodia in recent years has sparked concerns among civil society groups and international organizations as to the potential impacts on poor local communities’ access to resources. Growing interest from foreign investors in agriculture, particularly in agro-industrial crops like rubber, cassava, sugarcane and corn, has likewise raised concern about the potential effects of such investments on community livelihoods, the environment and national food security.

Agriculture has traditionally been a steady contributor to the national economy, employing a significant proportion of the rural workforce and generating substantial foreign exchange earnings. Now in its sixth legislature, the Cambodian government is focusing even more strongly on promoting the sector by relaxing taxes related to agricultural products and developing rural infrastructure such as roads and irrigation.

Meanwhile, the government, with the support of development partners, has provided technical assistance to rural people engaged in rice farming, fisheries (aquaculture) and livestock production. It has also renewed efforts to improve the irrigation system so as to reduce farmers’ dependency on rain, particularly in rice production, and bolster resilience to climate change. As the agriculture sector is one of the main drivers of economic growth in
Cambodia, a market mechanism has been set up to promote trade and channel agricultural products to local and international markets. To help the sector become more competitive, soft infrastructure related to rules and regulations, bureaucratic procedures and costs of doing business has been improved.

**The Current Account Deficit**

The current account deficit widened to 10.4 percent of GDP in 2018, from 9.7 percent of GDP in 2017, but remained fully financed by foreign direct investment (FDI). FDI is estimated to have reached a record high of more than $3.0 billion or 13.4 percent in 2018. Burgeoning exports and strong FDI inflows have contributed to further accumulation of gross international reserves, which in 2018 reached $10.1 billion or about six months of prospective imports.

**Recent Study Findings**

Recent findings from secondary sources and from the field research activities show the following:

- Three-quarters of the approved FDI inflows originated from China. In recent years, foreign investment from China has surged, mainly directed towards construction (infrastructure, commercial, and residential real estate), tourism, and to a lesser extent, manufacturing and agriculture.
- Cutting production and trade costs could help to mitigate the impact of Everything But Arms (EBA) suspension.
- After experiencing accelerated growth of 7.5 percent in 2018, the economy is expected to return to its long-term potential of about 7 percent. As exports moderate in line with deceleration in global demand, real growth is projected to ease to 7 percent in 2019. The robust economic growth is expected to result in continued poverty reduction.
- The longer-term outlook, however, depends on the country’s ability to productively absorb rising FDI inflows, while promoting domestic investment.
- The recent surge in FDI inflows has sustained a prolong construction boom brought about by China’s investment and South Korea’s FDIs in the agriculture sector.
- Private investment, largely driven by FDI inflows, climbed to new highs. In 2018, the value of approved investment projects increased to US$5.8 billion, of which two thirds was FDI. FDI inflows have grown by 24.8 percent, reaching a record high of more than US$3 billion, or 13.4 percent of GDP in 2018. Three quarters of the (approved) FDI originated from China.

With a rapidly expanding population and increasingly limited land, food security is another cause behind the growing concern in Cambodia. From our analysis of data on ELC investments and preliminary fieldwork on a number of FDI projects, and despite the traditional widespread informal paddy rice export to Thailand and Vietnam, we find that Cambodia will not suffer from food insecurity in the short and medium term. Nevertheless, in the long term, land use conflicts, water shortages and disappearing income sources compounded by the dramatic expansion in ELC investment in recent years could lead to a decline in household food consumption and a reduction in nutrition.

The growing interest in foreign direct investments (FDIs) in large-scale agricultural land from South Korea has been increasingly noted. Nevertheless, limited information about these FDIs is available from previous academic studies with regard to how they impact on local development. Previous research examining these issues focuses either on the monetary terms of FDIs or on the perspectives of the local community. There is also limited research that focuses on the perspectives of the investors and the dynamics and practices of the investments in the local community. Aiming to address these gaps in knowledge, this dissertation provides empirical evidence of three Korean FDIs in large-scale agricultural land in Cambodia. It analyses the perspectives of FDI investors and explores their embeddedness in the local community through entrepreneurship and stakeholder engagement in order to provide better understanding of the dynamics, practices and impacts of investments.

The research finds that the Korean investors do not (fully) embed themselves in their local settings due to barriers imposed by the investors and the local community. The research also finds that each of the Korean FDI companies examined contributes to local development differently—and not to their full potential—according to their operational patterns and extent of embeddedness in local communities. Moreover, the presence of these FDI companies does not help to increase local wages, as found in previous studies. In fact, as far as local community development is concerned, this study argues that the more entrepreneurial an investor, the more value is created for the local community.

The empirical findings of the study of the three Korean FDI companies and investors, particularly their entrepreneurship and stakeholder relationships, are critical to our understanding of the embedding process of the
FDI companies in Cambodia. The three theoretical concepts—entrepreneurship, stakeholder relationship and embeddedness—shed light on the ways these FDI companies operate in the ELCs in Cambodia and their interactions with local stakeholders that contribute to local development.

Some FDI companies and investors are entrepreneurial in their ELC development in Cambodia but are not fully embedded in the local community. The most entrepreneurial company in this study attempts to embed in the local community through establishing good relationships with local stakeholders. However, their attempts are unsuccessful due to divisions between the company, the investor and their stakeholders, especially in local communities. Nevertheless, all three companies are found to embed themselves in the agricultural sector in Cambodia. They establish and maintain good relationships with other stakeholders at the provincial and national level, but their relationships with local communities need a lot more work.

This research contributes to debates on the impact of FDIs on local development in several ways in terms of the analysis of the terminology of FDIs, methodology and scope and scale. In addition, the research findings contribute to the limited literature on Korean FDIs in Cambodia. This research also generates empirical findings about Korean investors, which will complement studies that try to counterbalance the current focus on the dominant Chinese investors in Cambodia. Given the potential impact of FDI companies on the local community, this PhD dissertation contributes to promoting rural sustainable development in Cambodia. It provides unique information about foreign investors that is useful for effective policy-making to enhance the positive contributions of FDIs to sustainable rural development. In summary, the empirical findings are expected to benefit different groups of academics and policymakers, as well as development investors and practitioners.

Conclusions

Agriculture has been a constant contributor to the national economy, employing a significant proportion of the rural workforce and generating substantial foreign exchange earnings. In its fourth legislature, the Cambodian government has focused even more strongly on promoting the sector by relaxing taxes related to agricultural products and developing rural infrastructure such as roads and irrigation. New measures have been taken to help local communities, including opening access to big fishing lots that used to be under private ownership.

As the agriculture sector is one of the main drivers of Cambodia’s economic growth, a market mechanism has been set up to promote trade and channel agricultural products to local and international markets. To boost the sector’s competitiveness, soft infrastructure related to rules and regulations, red tape and costs of doing business has been improved. Attracting investment in the energy sector has also been prioritized because the price of electricity in Cambodia is still formidably high compared with other countries in the region.

With population growth and increasingly limited land, food security is an emerging concern in Cambodia. From our analysis of CDC investment data (2000–2017) and MAFF ELC investment data along with preliminary fieldwork on a number of FDI projects, we find that regardless of the traditionally widespread informal paddy rice export to Thailand and Vietnam, Cambodia will not suffer from food insecurity in the short and medium term. Nevertheless, in the long term, conflicts over land and water use, water shortages and loss of traditional income sources, all contributed to by the dramatic expansion in investment in ELCs in recent years, could lead to a decline in household food consumption and thereby a reduction in nutrition. Particularly at risk are subsistence farming households and those that cannot earn enough from growing rice.

Policy Recommendations

To ensure that opportunities for foreign investment in agriculture in Cambodia are sustainable and beneficial to all, the government and concerned stakeholders should consider taking the steps outlined below.

Central and Local government

- Environmental impact assessment should be conducted with wide participation from concerned stakeholders, particularly from communities close to project sites, prior to granting ELC approval. As impact assessments become more reliable and transparent, the number and scope of land conflicts will be reduced.
- To avoid land disputes and overlapping claims, MAFF and related institutions should demarcate ELC borders in consultation with adjacent communities.
- The government should monitor ELC operations more closely to prevent sub-standard forest clearance practices and such activities as filling in upstream water sources and excessive logging.
- Authorities at both central and provincial levels should hold frequent consultations with communities and companies so as to pre-empt problems.
- MAFF should regularly update and publicize the progress of ELCs’ operations on its website and via other public media to ensure greater transparency and generate more credibility.
The government should take food security seriously into account in the provision of ELCs in order to avoid problems of competing land use between industrial crop production for export and paddy rice production for domestic consumption.

Also on food security, the government should review overall policy on investment in agriculture, particularly in relation to ELCs given their recent drastic expansion, to ensure agricultural trade policy is not geared solely towards foreign exchange earnings.

To reduce land conflicts and ensure benefits from large-scale agricultural investment, whether private domestic or foreign, the government must take swift and prudent action to provide low cost secure land titles to rural communities by prioritizing those to be imminently affected by projects.

Future rules and regulations should put more emphasis on the protection of rural communities by conducting social impact assessment prior to project approval, and they should be in line with regulations on investor protection.

Eliminating unofficial fees and setting up computerized systems to process investment and business licensing applications and related administrative procedures is vital to improve the investment climate; this should be done using a step-by-step or ministry-by-ministry approach.

Dispute settlement mechanisms should be reviewed so as to build confidence among private sector firms.

Ministries should set up a department to provide clear guidance and assistance to investors when they need it and receive feedback.

Private Companies
- ELC holders should be more transparent and accountable to nearby communities and the general public by contributing more to the development and maintenance of local infrastructure.
- Companies should maintain good, frequent and direct communication with local communities such as through community social gatherings and the like.
- Resolution of conflicts, such as land disputes, should be based on a win-win approach like the model used by the DAK LAK rubber plantation project in Mondolkiri.
- Companies, ELCs and processing plants in particular should be more responsible for maintaining the environment quality and ecological systems in their project areas.
- Chemical substances used in factories should comply with environmental regulations to protect people and animals from harmful pollution and water sources from contamination.

Affected Communities
- Communities should maintain good, frequent and direct communication with companies through community social gatherings and the like.
- Communities should be more involved with education programs provided by the authorities and NGOs regarding their rights to property and how to resolve land conflicts.
- Communities should report any irregular operations of the ELC companies to the commune or provincial authorities immediately, for example the filling in of streams or excessive logging.

NGOs/Civil Society
- Local NGOs should raise community awareness regarding civil rights and how to exercise those rights.
- Community NGOs should closely monitor potential conflicts between local communities and ELC companies and compile accounts to inform the public.
- Civil society groups should advocate for better recognition of community rights by ELC companies and local authorities.

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