Cambodia

Impacts of Global Financial Crisis

Cambodia’s economy has significant vulnerabilities to the global economic crisis. Cambodia is a small open economy with a dynamism based on a non-diversified export basket (rice, garments and tourism) and on foreign-financed investment (private and public). The authorities’ instruments to respond to the crisis are limited by a high dollarization, small fiscal space, and reliance on donor financing.

The economy is expected to contract by 1% in 2009 and its possible recovery in 2010 is conditional on the external environment. Most indicators point to a sharp slowdown in the economy, although some indicators suggest a possible bottoming out in the first half of 2009 and little data is available on the informal sector. While agriculture and the informal economy will provide well-needed income, only a recovery in the tradable sector (including tourism) will drive growth to the levels Cambodia is now used to.

Capital inflows have been reduced sharply. Foreign direct investment contracted over 50% in the fourth quarter from the previous year, and non-resident deposits were sharply reduced in the final months of 2008. The impact is visible in construction, including with large projects being scaled down or frozen.

The impact of the crisis on livelihoods is significant but varies across the population. Only a fifth of all households have a job in sectors directly affected by the crisis (garments, construction, and tourism). Urban households and richer households are more likely to be affected through these sectors, but the income impact is greatest amongst poorer and rural households, for whom these jobs, if present, account for a far larger share of income.

Infrastructure Challenges

There is no analysis yet on the potential impacts of global economic crisis on the infrastructure sector. However, it could be expected that the pace of Cambodia to overcome infrastructure constraints would slow down if donor assistance declines. Main infrastructure constraints include high costs of electricity (over 15 US cents per kwh), very low electrification rate in rural areas (3.5%), poor road conditions, lack of rural road accessibility, and low level of accessibility to clean water.

Infrastructure Investments

The Government recognized the impacts of the crisis and launched the preparation of a three-pronged response (macroeconomic and financial sector policies; fiscal policies; and sector responses). The Government is making effort to remove infrastructure constraints as well as to cope with the current financial crisis.
The Government has secured a concessional loan of US$80 millions from the Chinese Exim Bank to construct a loop-line around Phnom Penh, and also approached the Chinese Exim Bank for a package of concessional loan amounting to US$200 millions to support rural electrification program. For first phase, the Chinese Exim Bank is considering to release US$ 30 million.

The WB is also considering to provide a grant and credit package amounting to US$30 to 40 million to co-finance the RE program. The preparation of joint financing is scheduled in early second half of CY 2009. With AusAID grant, the WB is preparing an additional financing of US$ 10 million to the on-going Rural Electrification and Transmission Project.

Japan has agreed to provide a grant of US$20 millions for implementation of Phase 3 of National Road 1, and planned to finance the construction of 2nd Mekong Bridge ($US74 millions). Japan also committed to provide a 40% increase on top of the existing grants and loans.

Government has just signed an agreement with an Australian firm, AusAID and ADB on the railway project with the total amount of US$115 millions.

OPEX through ADB provided US$ 7 millions additional amount to the on-going Road Asset Management Project co-financed by WB, ADB/AusAID and RGC.

China committed and agreed to provide a large amount of loans on construction and rehabilitation of roads, bridges, and railways.

Korean has committed in June 2009 to provide US$60 millions to improve Cambodia Road Network and sewage system.

ADB is preparing a Rural Road Asset Management Project (US$ 15 millions), with Board date in 2010.
Lao PDR

Impacts of Global Financial Crisis

Lao PDR is weathering the global financial crisis better than many of its neighbors. The real sector continued to perform fairly well, but fiscal management (especially budget deficit and off-budget spending) became a serious concern. The impacts of the crisis are felt through falling foreign direct investment, prices and demand for exports, especially for resource sectors and agriculture. Tourism and manufacturing (garments) are less affected by the crisis in early 2009 but remain vulnerable. The slowdown of power demand growth in the GMS will slow the pace of hydropower development. Hydropower FDI will decline in 2009.

GDP, which grew at about 7 percent in 2008, is projected to slowdown to 5 percent in 2009 due to the global economic crisis. Running fiscal deficit, GOL is facing significant revenue shortfalls in FY2009 due to the impact of the global financial crisis and expenditure pressures from Southeast Asia Games and other infrastructure projects.

The GOL’s revenue collection is expected to drop from 14.2 percent of GDP in FY2008 to 13.2 percent of GDP in FY2009 due to decline in mining and non-resource revenues. The expenditure has increased to about 22.8 percent of GDP from 17.6 percent in FY2008 due to GOL’s plan to stimulate economy and promote domestic consumption, increased public wage spending as well as preparation for the Southeast Asia Games and local infrastructure development. The overall budget deficit is expected to be high in FY2009. The decline in revenues coupled with expenditure pressure have effectively resulted in abandonment of the recent prudent fiscal policy, as off-budget financing and direct lending by the Bank of Laos have started and intensified this year.

Infrastructure Challenges

Lao PDR is a land-locked and mostly mountainous country at the early stage of economic development. Both the Government and donors stress the importance of infrastructure development for growth and poverty reduction. In particular, infrastructure development is emphasized as key to capitalize the regional opportunities created by the Greater Mekong Subregion (GMS) economic cooperation. Hydropower development for regional power trade is a major potential source of foreign exchange and government revenues. Regional highway development for cross-border trade is essential in turning the land-locked disadvantage into land-linked advantage.

The development of the country’s huge hydropower potential is at the early stage, requiring substantial foreign capital, ground work on financing mechanism, and enabling policy environment for improved private sector participation. At present, only 3% of the potential has been explored. Rural electrification rate is 60%. Access to safe drinking water is 60% for urban population and only 50% for rural population. Roads are the predominant mode of transport. Other modes of transport (inland waterways, air, and rail) serve very limited market segments. About 60% of the national roads and 65% of the
provincial roads are in poor or bad condition, some of which are impassable in the wet season. More than 20% of the rural populations do not have year-round access by road.

**Donor Response**

ADB has increased its support from $27 million in 2006 and $57 m in 2007 to $115 million in 2008. On top of that, ADB has allocated additional US$ 35 million from its global financial crisis response pool for 2009 and 2010, US$ 15 million of which has been allocated as budget support for 2009, and the remaining amount will be allocated is subject further discussion with GOL.

Decline of AusAid support has affected transport and water supply under which AusAID couldn't realize the indicative amount of US$ 20 m for water supply and another US$20 m for road sector.

JICA has indicated its supplementary budget to budget support around US$ 15 million.

The World Bank is preparing two projects, one for road sector and the other for rural electrification. Both are scheduled to the Board in FY10.
Thailand

Impact of the Global Financial Crisis

Thai economy has been through both political turmoil and global financial crisis in 2008. Real GDP growth in Thailand slowed down from 4.8 percent in 2007 to about 2.6 percent in 2008. Starting in October, the difficult political situation combined with the global financial crisis affected exports, tourism, and the confidence of consumers and investors, resulting in real GDP contraction of 4.3 percent in the forth quarter.

Export sector heavily hit by the global slowdown. Thai economy has been relying on export sector for growth since recovering from the 1997 financial crisis. The current global financial crisis is expected to dampen import demand from developed countries, which can lead to about 15.9 percent contraction in Thai export in 2009. This can be severe given that Thai export sector accounts for nearly 70 percent of GDP.

Private investment is expected to remain modest. The growth in private investment has been at an average of 2.7 percent annually for the last three years. FDI is expected to contract in 2009 as a result of the global financial crisis. This is because major foreign direct investors, namely Japan, Singapore, EU and US, have encountered strong contractions.

Public investment is expected to increase to uphold the economy in time of sluggish export. With the current government gaining relative stability, the government has put in place 2 stimulus packages to counter the impact of global financial crisis. The second round of stimulus package (i.e. SP2) consists of large investment components, mostly infrastructure-related, which could raise the investment growth to 7 percent in 2009 (from -4.8 percent in 2008).

Role of Infrastructure Development in Responding to the Crisis

Public sector investment in infrastructure is among the key initiatives in encountering the global financial crisis. The second stimulus package (SP2), approximately THB1.4 trillion or USD40 billion, consists mostly of infrastructure investment in the next three years. The government aims to motivate economic growth in the immediate term through infrastructure investment in place of the underperformed export, as well as to fill in the investment gap that suffered inactivity since the 1997 financial crisis.

The infrastructure investment program would not only uphold the economic activity in the short-term, but also build a strong foundation for growth and competitiveness in the longer term. The role of infrastructure development in Thailand under the current financial crisis situation is in two folds: (1) to stimulate the economy when the key
drivers, namely export, is dampened by the crisis; and (2) to build a strong foundation for
growth and competitiveness.

**Infrastructure investment as economic stimulus will face several challenges.** Timely
disbursement of these projects is one of the most important challenges to the SP2. Thai
government is aware of this challenge and is trying to create enabling environment that
ensure timely disbursement without compromising good governance practice. Another
challenge is the financing of these infrastructure investments. Thai government has
recently received the approval from the parliament to raise THB800 billion (or USD23
billion) from domestic (and partly foreign) debt market.

**Alternative financing options are explored in the light of tight fiscal space.** The
financing need for the SP2 has stimulated the thinking of new approaches in financing
infrastructure development (e.g. creating infrastructure fund, public private partnership).
This also impacts government officials initially in terms of building own capacity to
accommodate the new public financing alternatives, which includes the knowledge on
government fiscal risk management. Among other collaboration with Thai government,
the World Bank will provide support on alternative financing, such as initialization of and
capacity building for the PPP development.

**IFI Borrowing.** The Thai government plans to borrow approximately US$3 billion in
the near future from the World Bank, ADB, and Japan, for budget support and specific
investment in the highway and mass rail transit sectors. The government also indicates
more borrowing from IFIs in the next 3 years.