

**Cambodia's New Growth Strategy**  
An Assessment of Medium and Long-term Growth for  
Resilient, Inclusive, and Sustainable Development

**Background Paper** **8**

# **Cambodia Economic Diversification Pathways**

**Kelly Wyett**  
FEBRUARY 2025



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**CDRI – Cambodia Development Resource Institute**  
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## List of acronyms

AIP	Agro-Food Industrial Park
ASEAN	Association of Southeast Asian Nations
CAPRED	Cambodia Australia Partnership for Resilient Economic Development
CDC	Council for the Development of Cambodia
CDRI	Cambodia Development Resource Institute
COI	Complexity Outlook Index
ECI	Economic Complexity Index
EV	Electric Vehicle
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
GI	Geographical Indication
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit (German development agency)
LDC	Least Developed Country
MEF	Ministry of Economy and Finance
MISTI	Ministry of Industry, Science, Technology & Innovation
MLVT	Ministry of Labour and Vocational Training
MOC	Ministry of Commerce
MOI	Ministry of Interior
NIS	National Institute of Statistics
OECD	Organisation for Economic Co-operation and Development
RCA	Revealed Comparative Advantage
RCEP	Regional Comprehensive Economic Partnership
RGC	Royal Government of Cambodia
SEZ	Special Economic Zone
SDF	Skills Development Fund
SME	Small and Medium-sized Enterprise
SPS	Sanitary and Phytosanitary Standards
USD	United States Dollar

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<sup>1</sup> See Wyett and Bateman (2024) "Timor-Leste Economic Diversification Pathways", forthcoming.



# មាតិកាធ្វើពិពិធកម្មសេដ្ឋកិច្ចកម្ពុជា

## សេចក្តីសង្ខេប

កំណើនសេដ្ឋកិច្ចកម្ពុជាយ៉ាងឆាប់រហ័ស ក្នុងរយៈពេលពីរទសវត្សរ៍ចុងក្រោយនេះ បានជំរុញជាចម្បងដោយសារបរិវត្តកម្មរចនាសម្ព័ន្ធ ពីព្រោះកម្លាំងពលកម្មបានផ្លាស់ប្តូរពីវិស័យកសិកម្ម ទៅការងារដែលមានផលិតភាពខ្ពស់ក្នុងវិស័យផលិតកម្ម និងសេវាកម្ម។ ទោះជាយ៉ាងណាក៏ដោយ គំរូកំណើនដែលគ្របដណ្តប់ដោយផលិតកម្មកាត់ដេរ ទេសចរណ៍ និងសំណង់ ឥឡូវនេះកំពុងប្រឈមនឹងកំហិតនានា ដែលទាមទារឱ្យមានការផ្លាស់ប្តូរឆ្ពោះទៅរកសេដ្ឋកិច្ចដែលកាន់តែមានពិពិធកម្ម និងភាពធន់។ របាយការណ៍នេះស្វែងយល់ពីមាតិកាធ្វើពិពិធកម្មសេដ្ឋកិច្ចកម្ពុជា ដោយកំណត់ពីឧបសគ្គ និងឱកាសសំខាន់ៗ ដើម្បីជំរុញកំណើនប្រកបដោយចីរភាព និងបរិយាបន្ន។

ការសិក្សានេះបានគូសបញ្ជាក់ពីសារៈសំខាន់នៃពិពិធកម្មសេដ្ឋកិច្ច ដើម្បីលើកកម្ពស់ភាពប្រកួតប្រជែង និងភាពស្មុគស្មាញសេដ្ឋកិច្ចរបស់កម្ពុជា។ ការធ្វើពិពិធកម្មក៏កាត់បន្ថយការពឹងផ្អែកលើវិស័យមួយចំនួន ធ្វើឱ្យប្រសើរឡើងនូវភាពធន់នឹងការប៉ះទង្គិចពីខាងក្រៅ និងជួយសម្រួលដល់ផលិតកម្មទំនិញ និងសេវាកម្មដែលមានតម្លៃខ្ពស់។ របាយការណ៍នេះ អនុវត្តក្របខ័ណ្ឌសេដ្ឋកិច្ច ដែលស្មុគស្មាញនិងការវិភាគគម្លាតផលិតផលដើម្បីកំណត់មាតិកាធ្វើពិពិធកម្មដែលអាចសម្រេចបាន ដោយដកស្រង់ករណីសិក្សាពីអាស៊ាន និងតំបន់ផ្សេងទៀត។ របាយការណ៍គូសបញ្ជាក់ថា អន្តរកាលយឺតរបស់កម្ពុជាពីផលិតកម្មកាត់ដេរ ទៅជាឧស្សាហកម្មដែលស្មុគស្មាញ ដូចជាគ្រឿងអេឡិចត្រូនិក និងការផលិតរថយន្ត គឺដោយសារតែមានឧបសគ្គទាំងការប្រមូលផ្តុំចំណេះដឹង និងភាពប្រកួតប្រជែង។

ពិសេសជាងនេះទៅទៀត ឧបសគ្គក្នុងការប្រកួតប្រជែង រួមមាន ការអនុវត្តបទប្បញ្ញត្តិមិនច្បាស់លាស់ និងមិនស៊ីសង្វាក់គ្នា ថ្លៃកសិកម្មនិងថាមពលខ្ពស់ និងគម្លាតជំនាញក្នុងតួនាទីបច្ចេកទេស និងអ្នកគ្រប់គ្រង។ ការប្រមូលផ្តុំចំណេះដឹង ត្រូវបានរារាំងដោយទំនាក់ទំនងខ្សោយរវាងក្រុមហ៊ុនក្នុងស្រុក និងក្រុមហ៊ុនបរទេស (ជាពិសេសក្រុមហ៊ុនផលិតដែលផ្តោតលើការនាំចេញ)។ ទោះបីជាមានការទាក់ទាញការវិនិយោគផ្ទាល់ពីបរទេស (FDI) ក៏ដោយ ប៉ុន្តែក្រុមហ៊ុនបរទេសភាគច្រើនមិនបានរួមចំណែកដល់ការធ្វើពិពិធកម្មឧស្សាហកម្មទេ ដោយសារក្រុមហ៊ុនបរទេសដំណើរការជាចម្បងក្នុងរចនាសម្ព័ន្ធជាច់ដោយឡែក ដោយមានការផ្ទេរបច្ចេកវិទ្យាតិចតួចបំផុតទៅឱ្យក្រុមហ៊ុនក្នុងស្រុក។

ដើម្បីដោះស្រាយបញ្ហាប្រឈមទាំងនេះ របាយការណ៍បានកំណត់មាតិកាធ្វើពិពិធកម្មបឋមចំនួនពីរ៖ ១) ការធ្វើអន្តរកាលពិភពលោក ទៅការកែច្នៃកសិកម្ម និង ២) ការពង្រីកផលិតកម្មកាត់ដេរទៅជាអេឡិចត្រូនិក ផលិតរថយន្ត និងគ្រឿងម៉ាស៊ីន។ ការកែច្នៃកសិផលផ្តល់នូវវិធីសាស្ត្រ “ការព្យួរផ្លែឈើទាប” ដោយប្រើមូលដ្ឋានកសិកម្មដែលមានស្រាប់របស់កម្ពុជា ដើម្បីអភិវឌ្ឍចំណីអាហារ និងផលិតផលកសិកម្មដែលមានតម្លៃខ្ពស់ជាង។ ទន្ទឹមនឹងនោះ ការផលិតគ្រឿងអេឡិចត្រូនិក និងរថយន្ត

បង្ហាញពីឱកាសជាយុទ្ធសាស្ត្របន្ថែមទៀត ក្នុងការធ្វើសមាហរណកម្មទៅក្នុងបណ្តាញផលិតកម្មសកល និងលើកកម្ពស់ភាពស្មុគស្មាញសេដ្ឋកិច្ចកម្ពុជា។ ការសិក្សាក៏សង្កត់ធ្ងន់លើសក្តានុពល “ឧស្សាហកម្ម បៃតង” ជាពិសេសនៅក្នុងការផលិតគ្រឿងបន្លាស់រថយន្តអគ្គិសនី (EV)។

អនុសាសន៍ខាងគោលនយោបាយផ្តោតលើ គោលដៅសម្របសម្រួលរបស់រដ្ឋាភិបាល ការលើកកម្ពស់ FDI គោលនយោបាយឧស្សាហកម្ម និងការបើកដំណើរការកំណែទម្រង់បរិស្ថាន។ វិធានការសំខាន់ៗ រួមមាន ការកំណត់គោលដៅលើកទឹកចិត្ត FDI ដល់ក្រុមហ៊ុនឈានមុខគេក្នុង ឧស្សាហកម្មអាទិភាព ការកែលម្អបរិយាកាសវិនិយោគសម្រាប់ឧស្សាហកម្មដែលជាយុទ្ធសាស្ត្រ ការពង្រឹងទំនាក់ទំនងរវាងក្រុមហ៊ុនក្នុងស្រុក និងសាជីវកម្មពហុជាតិ ការពង្រីកអន្តោប្រវេសន៍ដែលផ្អែកលើជំនាញ ការកែលម្អសេវាវិញ្ញាបនប័ត្រ និងហេដ្ឋារចនាសម្ព័ន្ធតុលាការផ្សេងទៀត និងការទាញយកប្រយោជន៍ពីតំបន់សេដ្ឋកិច្ចពិសេស (SEZs) សម្រាប់ឧស្សាហកម្មអាទិភាព។

## Abstract

Cambodia's rapid economic growth over the past two decades has been driven primarily by structural transformation, as labour shifted from agriculture to higher-productivity jobs in manufacturing and services. However, the country's growth model—dominated by garment manufacturing, tourism, and construction—is now facing limitations, necessitating a shift towards a more diversified and resilient economy. This report explores pathways for economic diversification in Cambodia, identifying key constraints and opportunities to foster sustainable and inclusive growth.

The study underscores the importance of economic diversification in enhancing Cambodia's competitiveness and economic complexity. Diversification also reduces dependency on a few sectors, improves resilience to external shocks, and facilitates the production of higher-value goods and services. The report applies an economic complexity framework and product space analysis to identify viable diversification pathways, drawing on case studies from ASEAN and beyond. It highlights that Cambodia's slow transition from garment manufacturing to more complex industries, such as electronics and automotive production, is due to constraints in both knowhow accumulation and competitiveness.

More specifically, competitiveness constraints include uncertain and inconsistent regulatory enforcement, high logistics and energy costs, and a skills gap in technical and managerial roles. Knowhow accumulation is constrained

by weak linkages between domestic and foreign firms (especially export-oriented manufacturing firms). Despite attracting significant foreign direct investment (FDI), much of it has not contributed to industrial diversification, as foreign firms primarily operate in enclave-like structures with minimal technology transfer to local firms.

To address these challenges, the report identifies two primary diversification pathways: (1) transitioning from agriculture to agro-processing; and, (2) expanding from garment manufacturing into electronics, automotive, and machinery production. Agro-processing offers a "low-hanging fruit" approach, leveraging Cambodia's existing agricultural base to develop higher-value food and agricultural products. Meanwhile, electronics and automotive manufacturing present a more strategic opportunity to integrate into global production networks and enhance Cambodia's economic complexity. The study also emphasises the potential of "green industries," particularly in electric vehicle component production.

Policy recommendations focus on targeted government facilitation, FDI promotion, industrial policy, and enabling environment reforms. Key measures include targeting FDI incentives to pioneer firms in priority industries, improving the investment climate for strategic industries, strengthening linkages between local firms and multinational corporations, expanding skills-based immigration, improving certification services and other quality infrastructure, and leveraging SEZs for priority industries.

## 1. Introduction

### 1.1. Motivation

Cambodia's economy has experienced rapid growth over the past two decades. Such growth was mostly driven by increased factors of production,<sup>2</sup> with more moderate improvements in productivity (Figure 1). Improvements in productivity in turn mostly came from structural transformation as workers left agriculture for higher-productivity jobs in manufacturing, services and other industries (Penn World Table 2021; World Bank 2021).<sup>3</sup>

However, there are clear signs that the current growth strategy has reached its limits. Cambodians are already among the hardest working populations in the world,

with very high annual working hours (Figure 2) and very high rates of employment. Growth has been heavily reliant on a few sectors— garment manufacturing, tourism and construction—and dominated by large firms, many of them foreign-owned. This growth pattern has been neither inclusive nor resilient, leaving the economy vulnerable to external shocks.

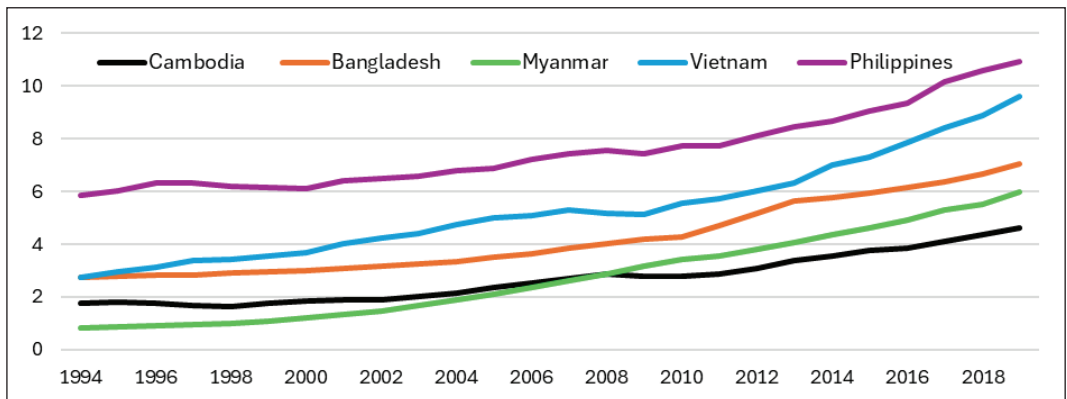
Indeed, Cambodia's exports are dominated by the garment sector, which accounted for 42 percent of exports in 2022. Services, primarily tourism, contributed 21 percent, while agriculture made up 13 percent (Atlas of Economic Complexity 2024) (Figure 3). In contrast to exports, Cambodia imports a wide range of products, partly due to undiversified local production (Figure 4).

In the medium-term, faster growth depends on activating a new phase of structural transformation through increased productivity within sectors, especially the manufacturing sector, and diversification into higher complexity sub-industries.

2 Specifically, average hours worked have increased around 8 hours and the capital-output ratio has more than doubled since the early 1990s. Source: Penn World Table (2021).

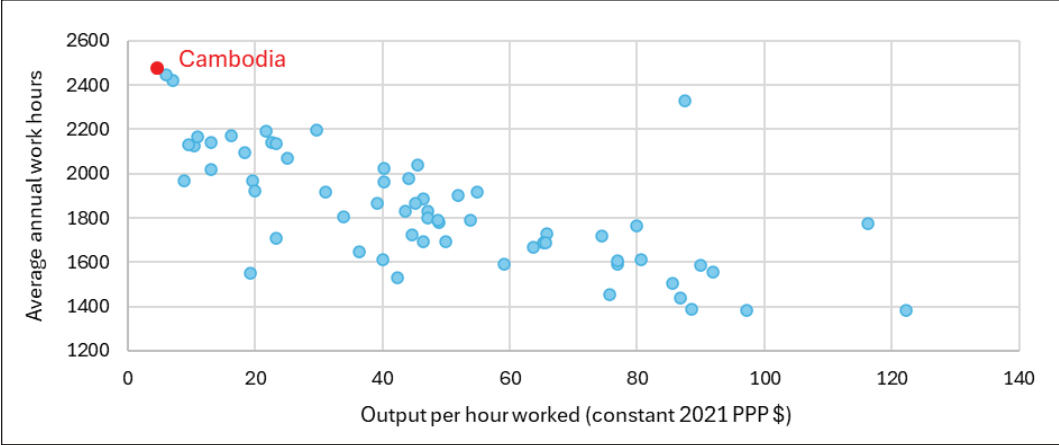
3 Total productivity grew by 178 percent over 1997-2019, while within-sector productivity grew significantly slower, indicating a large contribution from employment shifts between sectors.

Figure 1: Cambodia's productivity growth trails comparator countries (output per hour worked; constant 2021 international PPP \$)



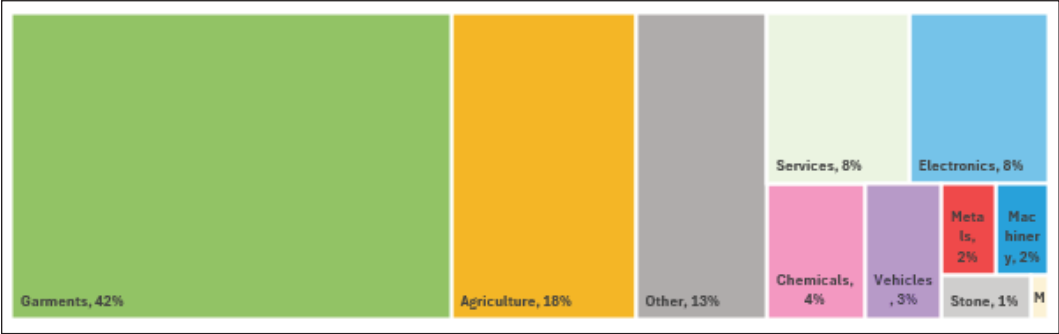
Source: Authors' calculations based on Penn World Table (2021) and World Development Indicators by World Bank (2021)

Figure 2: Cambodians work long hours at low productivity



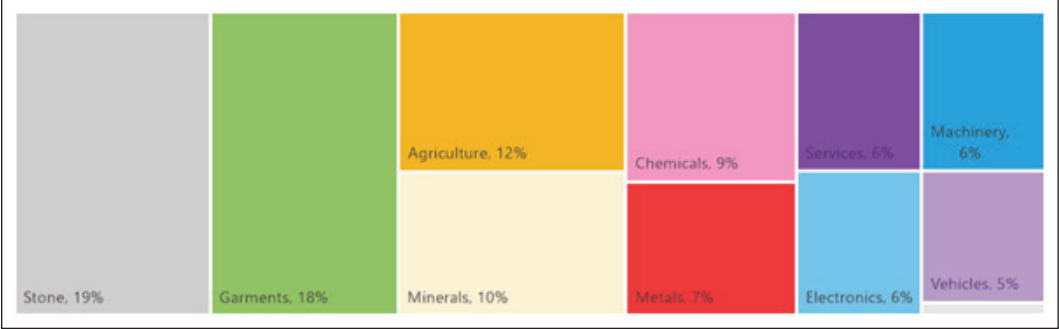
Source: Authors' calculations based on World Bank World Development Indicators and Penn World Table (2021).  
Note: Showing all countries for which data was available.

Figure 3: Cambodia's exports are dominated by garments, 2022 (% total)



Source: Authors' calculations based on international trade data from the Atlas of Economic Complexity (2024).

Figure 4: Imports are very diversified, reflecting undiversified domestic production, 2022 (% total)



Source: Authors' calculations based on international trade data from the Atlas of Economic Complexity (2024).

## 1.2. About this report

This report summarises research conducted by the Cambodia Australia Partnership for Resilient Economic Development, or CAPRED, to support CDRI's study entitled "Cambodia's New Growth Strategy: An Assessment of Medium and Long-term Growth for Resilient, Inclusive, and Sustainable Development." This report aims to guide CAPRED and CDRI's policy dialogue on diversification and identify potential activities where these organisations can support the Royal Government of Cambodia's (RCG) efforts to diversify the economy.

This report is a summary of a more detailed paper to be subsequently published on CAPRED's website.<sup>4</sup>

This report is organised as follows:

- Chapter 1 discusses the methodology.
- Chapter 2 details why diversification is important, how it happens and what facilitates diversification, and then assesses economic diversification in Cambodia.
- Chapter 3 evaluates Cambodia's constraints to diversification.
- Chapter 4 discusses how Cambodia can overcome these constraints.
- Chapter 5 proposes priority industries for diversification.
- Chapter 6 recommends policies to facilitate diversification in Cambodia.

## 1.3. Methodology

We employ an economic complexity framework (a measure of a country's productive knowledge) and apply this lens to industry prioritisation. We undertake product space analysis to help identify feasible diversification pathways and apply the growth diagnostics methodology (Velasco, Rodrik and Hausmann 2005) to understand the constraints to achieving competitiveness.

Our analysis is also based off of dozens of case studies<sup>5</sup>, especially from other member countries of the Association of Southeast Asian Nations, or ASEAN, that illustrate how countries have successfully developed, or failed to develop, new industries and diversify their economies. These case studies explain how countries accumulate the knowhow needed to develop new industries and how government intervention supports diversification.

This analysis was validated by CAPRED's field experience working with the government and private sector in Cambodia on issues ranging from trade and investment attraction to agro-processing promotion, renewable energy, SME development, climate finance, public-private dialogue and women's economic empowerment.

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<sup>4</sup> See [www.capred.org](http://www.capred.org)

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<sup>5</sup> Only a limited number of case studies are directly cited in this report.

## 2. The importance of economic diversification

Economic diversification involves expanding a country's economy by developing a wide range of industries and sectors, rather than depending on one or a few dominant industries. This process reduces economic risks, enhances resilience and dynamism, enables the production of more complex products and fosters higher employment and economic growth.

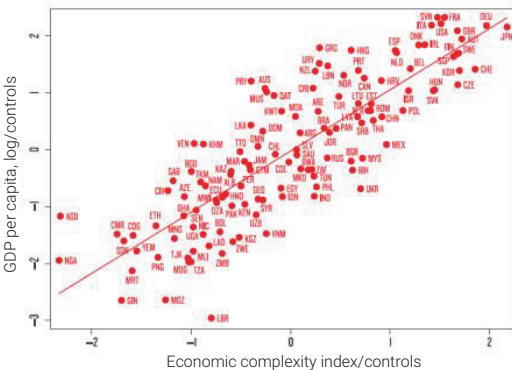
Diversification contributes to increasing economic complexity—the diversity and sophistication of an economy’s productive output, which reflects its underlying productive “knowhow.” Empirical evidence shows a strong correlation between a country’s complexity (measured by the economic complexity index [ECI]) and the income per capita it can generate. Indeed, complexity can explain about 75 percent of the variation in income between countries after controlling for a country’s natural resource rents (as countries with natural resources can be rich without being

complex) (Figure 5). Economic complexity is also important for future growth. That is, countries whose economic complexity is greater than what we would expect, given their level of income, tend to grow faster than those that are 'too rich' for their current level of economic complexity (Figure 6).

Our research indicates that while Cambodia's exports are still dominated by garments, they have diversified significantly over the past 15 years, particularly due to the emergence of the electronics and vehicle (primarily bicycle) sectors. This diversification has improved Cambodia's economic complexity. By 2022, Cambodia ranked as the 77th most complex country on the Economic Complexity Index (ECI), climbing 42 places since 2009 (Figure 7).

However, the diversification from garment manufacturing to more complex manufactured products has been slower in Cambodia compared to other Asian

Figure 5: Relationship between a country's ECI and GDP per capita



Source: Hausmann et al. (2014)

Figure 6: Relationship between a country's ECI and GDP per capita growth

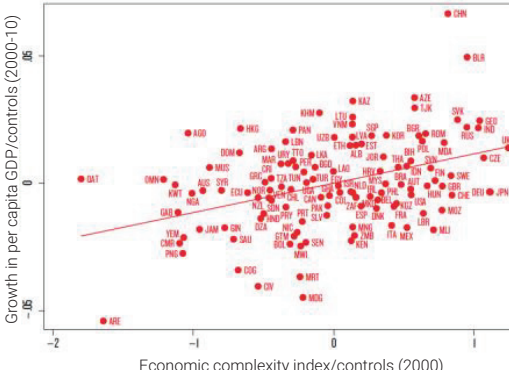
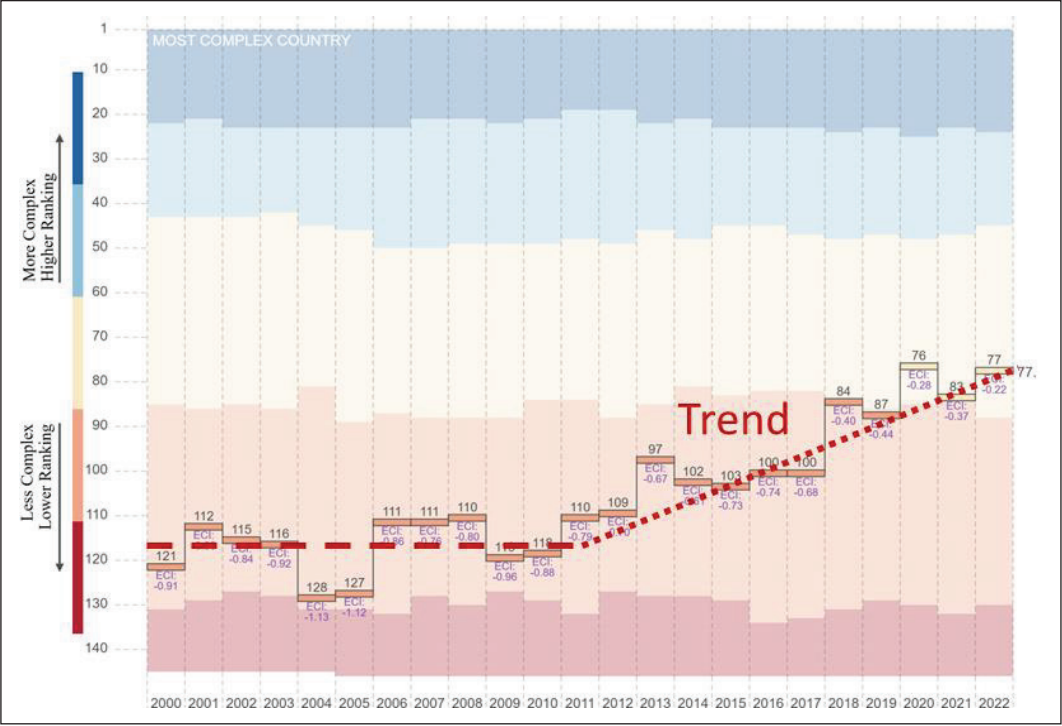
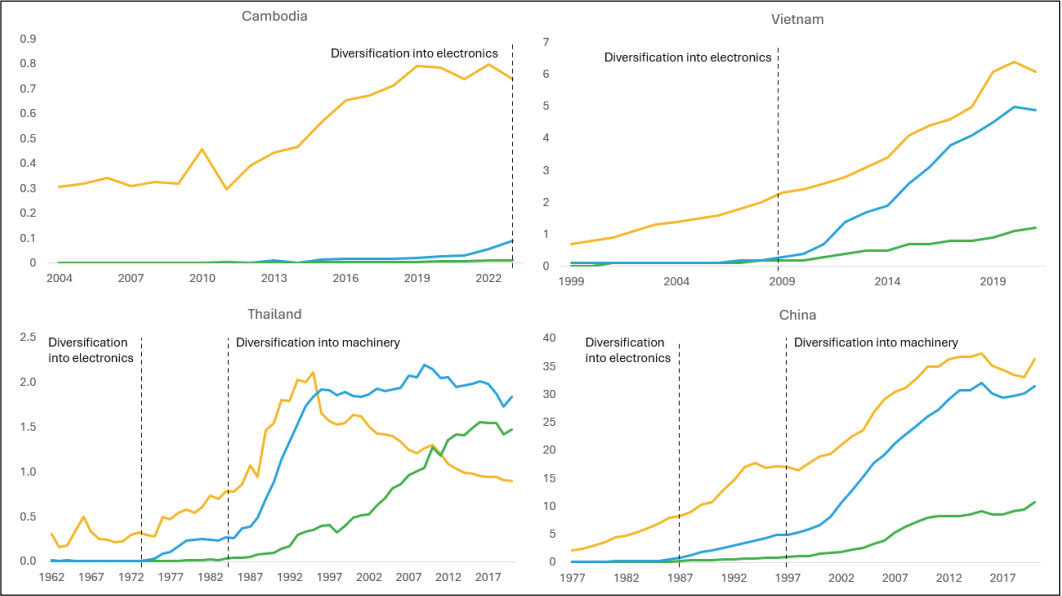


Figure 7: Cambodia's economic complexity ranking (out of 145 countries)



Source: Atlas of Economic Complexity (2024)

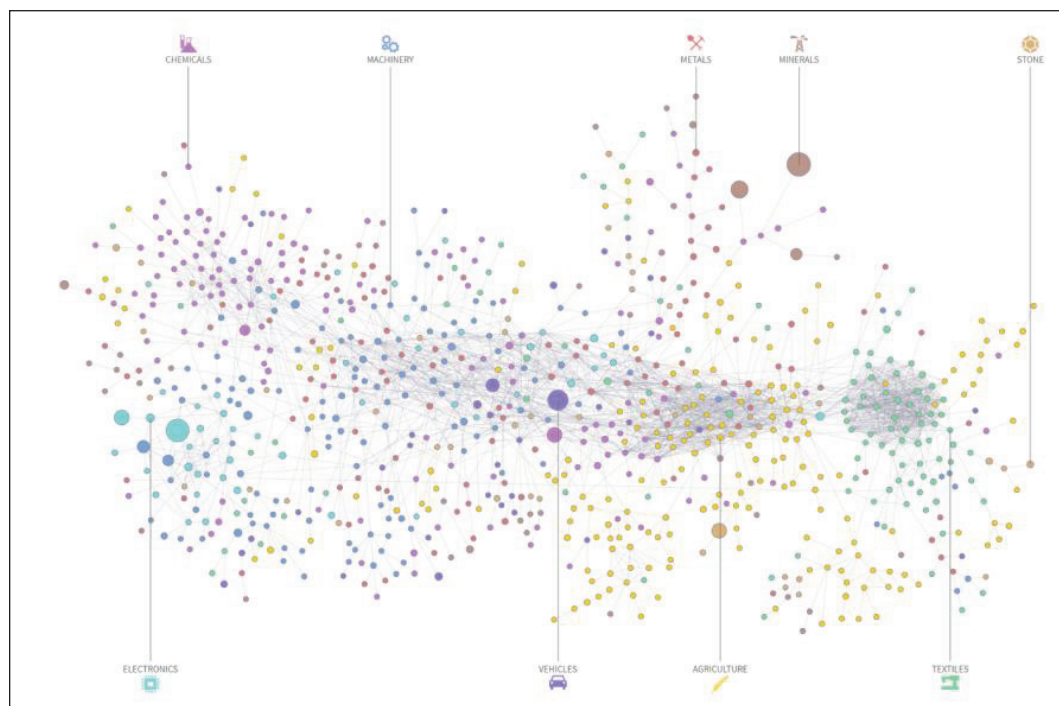
Figure 8: Diversification away from garment manufacturing is occurring slower in Cambodia than in other Asian countries (% world trade)



Source: Authors' calculations based on international trade data from the Atlas of Economic Complexity (2024).



Figure 9: The product space



Source: The Atlas of Economic Complexity (2024)

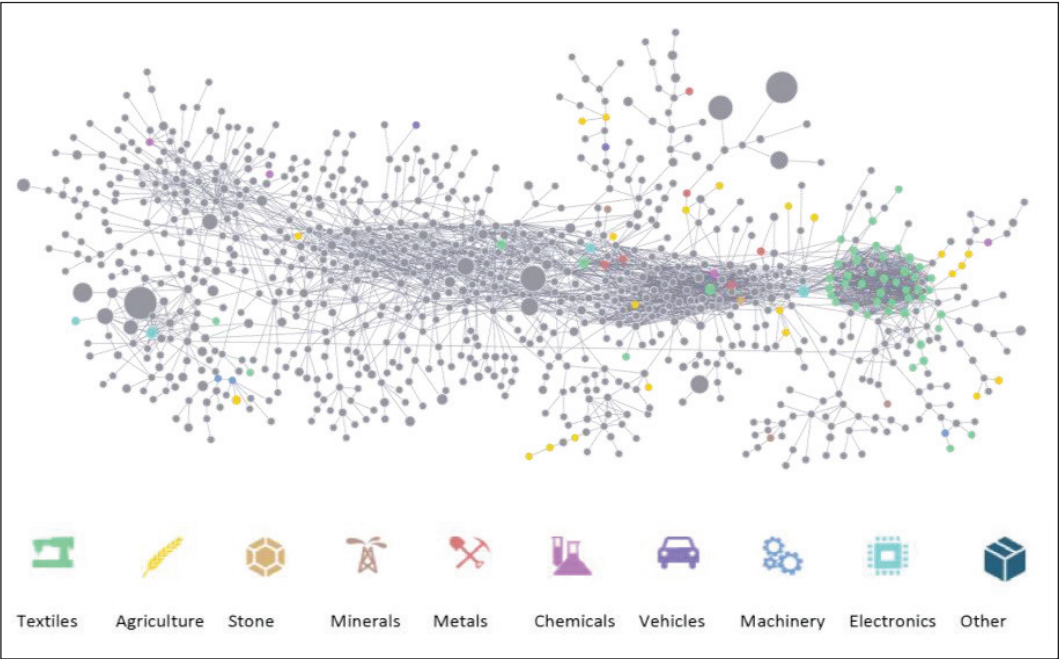
Notes: Each node is a product, and its size is determined by its share of world trade. The structure of the product space is defined by links between products based on the probability that both are exported by the same countries. The colour of each product node corresponds to its sector, defined empirically as collections of products that are

countries that industrialised in previous decades (Figure 8). This is likely due to greater global competition and stricter constraints on industrial policy from trade agreements, which limit protective measures for new industries. Additionally, Cambodia's slower accumulation of industrial knowhow, evidenced by the limited number of Cambodian-owned garment factories and low share of Cambodians in senior positions (around 45 percent), contributes to this slow diversification (Ministry of Labour and Vocational Training 2024). Indeed, across all industries, most exports are produced by foreign firms, while Cambodian-owned firms mainly serve

the domestic market (National Institute of Statistics 2022; World Bank 2023).

The key obstacle to diversification is the difficulty of acquiring new productive knowhow in the absence of supporting industries. To overcome this, countries typically expand into industries that are "adjacent" to their existing strengths—producing goods that require similar capabilities, such as moving from shirts to pants, rather than from shirts to engines. Therefore, the most effective diversification strategies focus on leveraging current industries as a foundation for developing new, related industries.

Figure 10: Cambodia’s position in the product space (2021)



Source: Atlas of Economic Complexity (2024).  
Notes: Coloured nodes show products that Cambodia exports with an RCA>1. Grey nodes show all other products.

The product space is a visual representation of the similarities between products covering all exported goods, but not services (Figure 9). A tightly connected product space implies that neighbouring products differ in only a few of their requisite capabilities, making them more viable candidates for diversification.

Cambodia’s position in the product space reflects the dominance of garments in its export basket (Figure 10). Of Cambodia’s exports, those in the more densely connected and central areas of the product space provide the best opportunities for diversification (including electric motors, solar panels, tyres and bicycles).

Emerging research (see Hausmann 2018) shows how countries accumulate the

knowhow required to diversify and the role of government policies and strategies in attracting, developing and retaining this invaluable resource. Importantly, it shows that knowhow flows through incredibly slow and narrow channels. Traditional tools like urbanisation, education and digital connectivity fall short in effectively disseminating the knowhow necessary for diversification and improving productivity. The policy takeaway is straightforward: knowledge resides in people. The path forward lies in attracting skilled individuals through foreign direct investment (FDI), skills-based immigration and other labour mobility (such as returned migrants, diaspora and labour exchanges between firms).

### 3. Cambodia's constraints to diversification

Diversification requires knowhow and competitiveness. That is, a country needs to know how to make a product and to be able to do so at a competitive price-quality point.

- **Knowhow:** The productive knowledge that goes into producing products (goods and services), as well as the knowledge of what can be produced competitively in a country
- **Competitiveness:** A country's ability to sell its products on global markets, taking into account product quality, price, innovation and market access

#### 3.1. Lack of knowhow

Diversification is path dependent; a country's ability to accumulate new knowhow and diversify into higher-complexity industries depends on their existing level of diversification and connectedness to other products (measured by the Complexity Outlook Index [COI]). Cambodia's COI is slightly below average, reflecting the dominance of garment exports and limited diversification into other industries. However, Cambodia's COI has been steadily improving in line with recent diversification into electronics and vehicles. Overall, Cambodia has a moderate number of opportunities to diversify using existing knowhow.

Cambodia also faces constraints in terms of utilising labour mobility to accumulate new knowhow. While Cambodia has attracted significant FDI over the last 20 years (equivalent to 10 percent of its GDP, one of the highest rates across ASEAN), a minority of this has been invested in new

industries.<sup>6</sup> Furthermore, productivity spillovers and linkages between foreign and domestic firms are rare. Most FDI firms rely on imported inputs and do not create backward linkages or share knowledge, which restricts technology transfer and productivity growth through global value chain participation. This is especially apparent in the garment industry, where over 95 percent of exporters are foreign-owned (World Bank 2021).

Immigration, another key path for accumulating knowhow, is also not especially restricted. Cambodia is the second most open country to migrants according to one measure, allowing 99 percent of nationalities to enter without a prior visa (Henley Openness Index 2024). However, government policy does not target migrants with new skills or actively facilitate other forms of targeted labour mobility, such as returned migration.

#### 3.2. Poor competitiveness

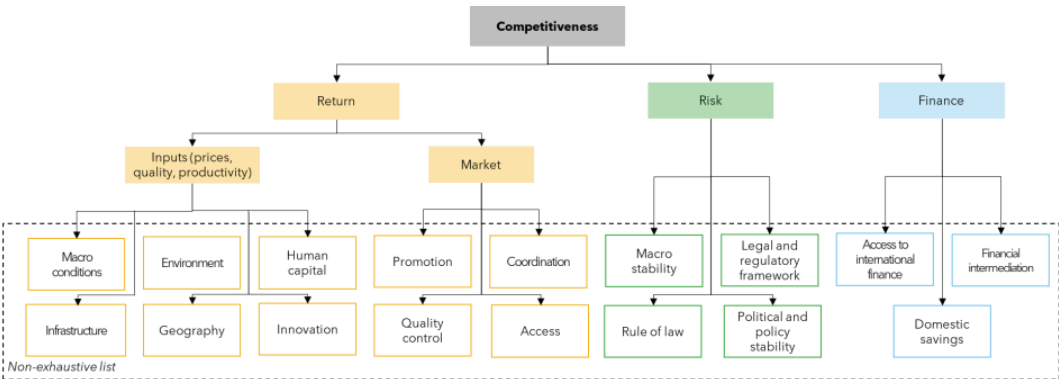
Given the many constraints to Cambodia's competitiveness, there is a need to identify the most binding constraints, and hence the policies that are likely to provide the 'biggest bang for the reform buck.' CAPRED has developed a framework for doing so based on the growth diagnostics literature (Velasco, Rodrik and Hausmann 2005) (Figure 11).

The framework highlights that investors' decisions to start or expand a business, as well as their profitability, depend on

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6 National Bank of Cambodia data on FDI by sector

Figure 11: A framework for identifying constraints to competitiveness



Source: Based on Hausmann, Rodrik and Velasco (2005)

investment attractiveness (encompassing risk and return), and their ability to finance that investment at an appropriate cost.

As discussed above, productivity growth has been slower in Cambodia than competing countries. Unsurprisingly, we find the most binding constraints in the country to be directly or indirectly about productivity.

**High infrastructure costs**

High infrastructure costs (specifically, poor logistics and high energy costs) are a significant but not always binding constraint to Cambodia’s competitiveness. Poor logistics, especially regarding transportation infrastructure, significantly raise operational costs and risks for investors, particularly in manufacturing. While projects like the Phnom Penh-Sihanoukville Expressway have improved connectivity, rural areas remain poorly connected, increasing business costs outside urban centres and special economic zones. Indeed, Cambodia ranks 115th out of 138 countries in the Logistics Performance Index. Lengthy border and export formalities further hinder trade, limiting Cambodia’s ability to integrate into global value chains. High energy costs

and unreliable power supplies also raise operational costs and risks, especially in energy-intensive manufacturing.

**Skills gap**

Cambodia’s skills gap is another significant but not always binding constraint. This gap is characterised by both quantity (a shortage of workers in specific technical areas) and quality (inadequate preparedness among graduates for high-demand sectors) constraints. According to a recent survey, 74 percent of businesses report challenges in hiring qualified staff, with 30 percent citing under-qualification as a critical barrier. The gap is especially prevalent in construction, manufacturing and engineering, where there is a persistent lack of workers with technical skills, management experience and quality control expertise. “Soft skills” are another critical gap identified in all sectors (EuroCham 2024).

Cambodia’s labour productivity, although showing improvement, remains significantly lower than that of its regional and global peers. This undermines the country’s competitive advantage derived from its relatively low labour costs.

## **Weak rule of law**

The rule of law ensures the consistent and transparent application of a country's legal and regulatory framework, creating a stable foundation for property rights, contract enforcement, and accountability. However, in Cambodia, significant gaps exist between the legal framework and its implementation. While reforms such as the 2021 Investment Law have improved regulations on paper, domestic and foreign investors face persistent challenges, including unclear laws, inconsistent application of regulations and prolonged legal dispute resolutions. Such challenges are consistently cited as the number one constraint faced by domestic firms and foreign investors alike. Cambodia also scores lower than other middle-income countries for the following World Bank governance indicators: rule of law, control of corruption, and regulatory quality.

Inconsistent implementation of taxation is a major pain point for the private sector. Foreign firms in particular report frequent audits, informal payment demands, unclear laws and inconsistent tax burdens. The unpredictability of tax policies and enforcement, especially compared to more stable tax environments in Vietnam and Thailand, deters compliance and raises perceived risks.

While weak rule of law directly undermines competitiveness by increasing risks for investors, the way firms adapt to this constraint indirectly affects Cambodia's productivity. This adaptation promotes informality and drives large domestic firms to concentrate on non-tradable sectors such as construction and banking.

## **Industry-specific constraints**

As well as the economy-wide constraints discussed above, there are binding constraints specific to the industries we recommend Cambodia target for diversification.

In agriculture,<sup>7</sup> these include:

- The dominance of smallholder farming, characterised by inconsistent production volumes, variable quality of raw materials, outdated machinery, inadequate skills and restricted access to capital collectively hinder the efficiency and scalability of their operations.
- The absence of a reliable market and fragmented value chains, characterised by weak linkages between farmers, processors and buyers, and the lack of long-term contracts limit the development of economies of scale and reduce competitiveness.
- Missing inputs essential for improving product quality, including quality infrastructure (QI), regulatory frameworks for food quality standards, modern technology and skilled labour limit the ability of producers to meet international market requirements.

These constraints are exacerbated and taken advantage of by importers of raw agricultural products in Cambodia's neighbouring countries.

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<sup>7</sup> See World Bank (2021) "A Strategy to Diversify Cambodia's Growth Model"; ADB (2021) "Cambodia Agriculture, Natural Resources, and Rural Development Sector Assessment, Strategy, and Roadmap"

The electronics industry faces two additional constraints, including the lack of primary domestic production and a shortage of skilled workers (see Ven and Hing 2019; Royal Government of Cambodia 2022; Botineau, Monti and Pocock 2023).

These constraints partly explain why Cambodia's transition from a garment-dominated economy to one that includes electronics has been slower compared to other countries.

## 4. Overcoming Cambodia's constraints to diversification

### 4.1. Overcoming constraints to knowhow accumulation

As discussed above, Cambodia's economy is characterised by a moderate level of complexity (measured by the Economic Complexity index [ECI]) and moderate opportunities for diversification (measured by the Complexity Outlook Index [COI]). This situation suggests a dual approach to knowhow accumulation:

- **Take strategic bets:** Fully exploit multiple policy levers and public investment to achieve diversification in targeted strategic industries
- **Exploit low-hanging fruit:** Address bottlenecks to jump the small distances to nearby new industries

We use the product space methodology to identify the most suitable "strategic" and "low-hanging" industries, taking into account an industry's relatedness, complexity and connectivity (Figure 12). Doing so shows that:

- **Agro-processing** is the best industry for a "low-hanging fruit" approach, given its high relatedness and moderate complexity.

- **Electronics** is the best industry for a "strategic bets" approach, given it has the highest relatedness score of the high-complexity industries.

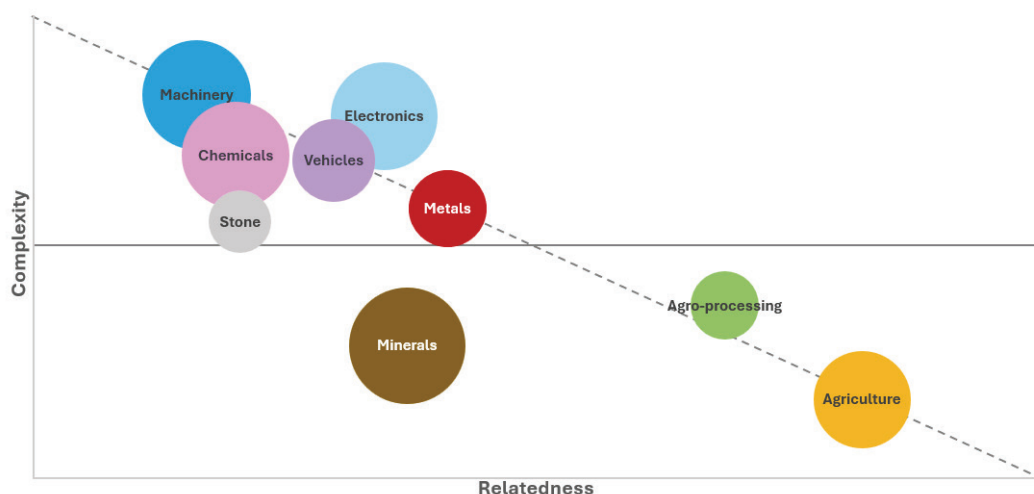
### 4.2. Overcoming constraints to competitiveness

Given Cambodia's constraints to international competitiveness and diversification, it is important to consider what diversification approaches might be possible. We identified three overlapping strategies. Priority industries should align with at least one of these strategies, and ideally, all three.

- Promote specialty, niche and premium products where international competition is low and demand is less price-sensitive; that is, industries where **the constraints are less relevant**.
- Promote industries that exploit Cambodia's potential competitive advantages; that is, **compensate for constraints**.
- Promote industries where the constraints to competitiveness are less binding; that is, **avoid constraints**.



Figure 12: Cambodia's sector diversification frontier by industry in 2022



Source: Authors' calculations using the latest data from the Atlas of Economic Complexity (2024)

Note: Bubble size relates to the size of global trade

Of course, longer term, Cambodia will need to tackle its binding competitiveness constraints to sustain growth; that is, it will need to **address constraints**. We recommend several policies for doing so in the recommendations section below.

### **Promote specialty, niche, and premium products**

Such products tend to fulfil a specialist demand, enabling high margins to be charged on relatively simple products. Such products often have a 'high quality' or a 'cultural' brand value. Examples include Fiji water, Italian fashion brands like Gucci, luxury Swiss watch brands like Rolex, premium Korean cosmetic brands like Sulwhasoo and Scottish Whiskey brands like Glenfiddich.

Cambodia has been successful in adopting this strategy for several agricultural products, although such products make up only a small fraction of Cambodia's agricultural exports. Examples include

organic rice, specialty rice varieties, organic moringa and Kampot pepper. Results include:

- Certified organic rice exported to Europe and the US, typically receives a 20–30 percent price premium compared to conventional rice (Grow Asia 2022)
- Following Geographical Indication registration in the EU, Kampot pepper exports surged by over 250 percent in 2017 compared to the 2013–2016 average (FAO 2023a)

Garment manufacturing is another industry where firms can receive premium pricing through ethical and environmental standards. However, the adoption of such standards remains limited in Cambodia due to barriers such as the cost and complexity of obtaining certifications, reliance on imported textiles and the focus on low and mid-tier consumer markets.

### **Exploit Cambodia's potential competitive advantages**

We recognise several potential competitive advantages that Cambodia is already using to attract investors seeking a production base for new export-oriented industries, including:

- **Macroeconomic and Political Stability.** Cambodia's dollarised economy, with 80-90 percent of transactions in USD, supports macroeconomic stability by minimising exchange rate risks and maintaining low inflation. This stability enables better long-term business planning, especially for export-driven industries like manufacturing (AMRO 2024a). Political stability over the past two decades has further enhanced the country's investment appeal by delivering relatively consistent and predictable policies. Indeed, a 2024 AmCham survey highlighted political stability as a key draw for 74 percent of investors.
- **Market Access.** Historically, Cambodia's Least Developed Country (LDC) status has provided reduced or zero tariffs for most exports to most countries. However, Cambodia aims to graduate from such status in the future. In the absence of LDC status, Cambodia will still benefit from several preferential trade agreements, including the ASEAN Economic Community and the Regional Comprehensive Economic Partnership, offering access to over 2.2 billion consumers (ASEAN Secretariat 2023). Existing free trade agreements with countries like China, South Korea and Japan also enhance its ability to integrate into global supply chains (GIZ 2023; AMRO 2024a).
- **Growing Workforce and Domestic Market.** With over 50 percent of the population under 30, Cambodia has a young and affordable workforce ideal for labour-intensive industries like garments, agro-processing and electronics assembly. This demographic dividend, supported by a growing 30-49 age group, boosts consumer spending and credit markets. Unlike aging neighbouring countries, Cambodia's youthful population offers long-term labour supply and economic growth potential (World Bank 2023; Mekong Strategic Capital 2024).
- **Agricultural Potential.** As one of the top ten global rice producers and the world's second-largest producer of raw cashews, Cambodia has an agricultural surplus that positions it well in regional markets, particularly in food-importing countries. This foundation presents a compelling opportunity for FDI, especially as demand grows in neighbouring economies (FAO 2023b). Plans for agri-food industrial parks aim to enhance agro-processing and attract sustainable investment in higher-value segments, positioning agriculture as a key growth area.
- **Renewable Energy Opportunities.** Cambodia's abundant solar and hydropower resources support its renewable energy potential, with 62 percent of energy already from renewables (UNFCCC 2023). The government's commitment to net-zero emissions by 2050 and the growing global interest in sustainable projects offer early-stage opportunities for investors in solar energy and renewable exports within ASEAN (AMRO 2024b).



- **Strategic Location.** Cambodia's central location in ASEAN makes it a competitive manufacturing hub amid global supply chain shifts, and a suitable candidate for "Country +1"<sup>8</sup> strategies, where firms establish secondary factories near existing operations to enhance resilience and sustainability (GIZ 2023).

### ***Promote industries where the constraints to competitiveness are less binding***

To identify new industries capable of thriving within Cambodia's constraints, it is essential to examine sectors and firms that have already demonstrated competitiveness and analyse the strategies underpinning their success. The garment industry offers valuable insights in this regard. Its reliance on foreign ownership and export-oriented markets significantly reduces interactions with the domestic regulatory environment. Firms in this sector predominantly use imported inputs, minimising dependence on local supply chains, and frequently operate within Special Economic Zones (SEZs), which provide streamlined regulations. Additionally, the industry has capitalised on international partnerships that enforce best practices in governance. Effective industry representation through the Garment Manufacturers Association in Cambodia has further strengthened the sector by facilitating structured engagement with the government on rule of law and regulatory

matters, ensuring a more predictable business environment (Ear 2009).

To address logistical challenges, garment producers, and other export-oriented manufacturing firms, often locate near key trade routes, such as Sihanoukville port or the borders with Vietnam and Thailand. To mitigate the risk of power outages, they operate in SEZs with independent electricity supplies or invest in private generators.<sup>9</sup>

**Other export-oriented manufacturing industries that could apply these strategies include the assembly of electronics, vehicles and other low-complexity products like toys and furniture.**

However, such strategies are neither optimal nor sustainable in the long term. In particular, operational isolation reduces opportunities for technology transfer, domestic supplier linkages and broader economic spillovers. As such, Cambodia must ultimately address its constraints to improve competitiveness, integrate domestic firms and maintain ongoing diversification into more complex industries.

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8 For example, many multinational companies and their suppliers, particularly in electronics and garments (including Samsung, Apple and Nike), have adopted a "China +1" approach by maintaining production in China while shifting part of their operations to Vietnam. This move is driven by lower labour costs, trade agreements (e.g., CPTPP, EVFTA) and Vietnam's growing infrastructure.

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9 CAPRED interviews with manufacturing firms across several SEZs (2025)

## 5. Proposed diversification pathways

Given the constraints, opportunities and suggested strategies discussed above, we recommend Cambodia pursue the two diversification paths discussed below. Here we provide an indicative view of what is possible and how diversification from current production to more complex industries can occur.

*Throughout this report, we define short-term as within five years, medium-term within a decade and long-term as over a decade.*

### 5.1. Agriculture to agro-processing

#### Industry overview

Cambodia's agro-processing sector remains underdeveloped, despite the country's abundant agricultural resources and diverse agricultural base. Most existing processing is of relatively low complexity, such as rice milling, cassava starch production and processing pepper. More complex processed products include cereal preparations, dairy products and vegetable oils. Estimates of the share of processed products in agricultural exports range from 5 to 12 percent (see Sok, Yang and Tynarth 2021; General Department of Customs and Excise Data 2024).

#### Justification for prioritisation

Our decision to recommend agro-processing for diversification is driven by the following considerations:

- Agro-processing is the best industry for a "low-hanging fruit" approach given its high relatedness and moderate complexity.

- Diversification into agro-processing typically facilitates ongoing diversification into chemical products that rely heavily on inputs derived from agriculture (including cosmetics, biofuels, bioplastics, cleaning products, vitamins and pharmaceuticals).
- Agro-processing offers opportunities to promote specialty, niche and premium products.
- Agro-processing offers opportunities to use the following competitive advantages: unprocessed agricultural production, market access, a growing workforce, macroeconomic and political stability, renewable energy potential and strategic location and proximity to key manufacturing hubs.

Agro-processing also offers opportunities for job creation, alignment with trade and FDI trends in the ASEAN region and integration with global and regional value chains.

#### Diversification opportunities

Agro-processing presents two broad diversification pathways in Cambodia.

- **Short term: scale up and increase the complexity of existing agro-processing industries.** Cambodia currently processes small portions of its key crops, such as rice, cassava, maize, cashew, banana, mango and pepper. However, much of this processing is limited to small-scale and low-complexity operations. The figure highlights value chains in ASEAN for three of Cambodia's

major crops, detailing typical products, processing steps, complexity levels and major firms, showcasing room for growth in both market share and value addition.

- **Medium term: developing new agro-processing industries.** Using the product space methodology, we identify diversification opportunities that balance viability (relatedness to current capabilities) and favourability (higher complexity and connectivity). Promising new agro-processing sub-industries include beverages and liquids (such as beer and vinegar), processed cereal products (such as noodles and rice paper) and other processed foods (such as coffee concentrates, baking powder and sauces).

## 5.2. Garments to electronics, automotive and machinery

### *Industry overview*

The electronics industry in Cambodia emerged around 2011, driven by FDI from Japanese firms seeking to diversify production from Thailand. By 2023, the industry had grown significantly, with 99 firms operating and employing around 54,000 people (Botineau, Monti, and Pocock 2023), and electronic products accounting for 7.5 percent of exports in 2022 (Atlas of Economic Complexity 2024).

The vehicles and machinery sectors are relatively less established in Cambodia. In 2022, vehicles and machinery accounted for 3.3 and 1.6 percent of exports respectively, with bicycles making up 85 percent of vehicle products (Atlas of Economic Complexity 2024).

As is typical across other countries, Cambodia's electronics, vehicle and machinery production includes low-complexity products (such as insulated wires and cables), and final product assembly. These entry points align with Cambodia's competitive advantages of low labour costs and market access.

All three industries are dominated by foreign firms and rely heavily on imported components, resulting in low value addition and weak integration within the domestic economy. For example, local content accounts for only 26 percent of bicycle and motorcycle manufacturing (CDC 2022). Similarly, around 75 percent of electronic exports are offset by imported components (Botineau, Monti, and Pocock 2023).

### *Justification for prioritisation*

Our decision to recommend electronics (and subsequently, vehicles and machinery) for diversification is driven by the following considerations:

- Electronics is the best industry for a "strategic bets" approach given it is the most viable of the high-complexity industries.
- Diversification into electronics typically facilitates ongoing diversification into other high-complexity manufacturing industries like vehicles and machinery.
- Electronics offers opportunities to take advantage of the following competitive advantages: favourable trade agreements with major export markets, a growing workforce, macroeconomic and political stability, renewable energy potential and strategic location and proximity to key manufacturing hubs.

- Like garment manufacturing, electronics is also an industry where the constraints to competitiveness are less binding

Electronics, vehicles and machinery also offer opportunities for job creation, alignment with trade and FDI trends in the ASEAN region and integration with global and regional value chains.

**Finally, all three industries overlap significantly with “green industry.”**

In particular, the shift toward electronic vehicles, or EVs, presents a significant opportunity for Cambodia. Unlike internal combustion engine vehicles, EV components are of moderate complexity and relatively lightweight, making them suitable for cost-competitive production in Cambodia. By leveraging its existing base of wiring harness manufacturers and implementing supportive policies, Cambodia can position itself as a regional hub for EV component production.

### ***Diversification opportunities***

Diversification opportunities over time in electronics, vehicles and machinery are summarised in Figure 13 and explained in more detail below.

### ***Electronics***

**In the short term**, Cambodia can expand its presence within the electronics value chain to establish a resilient foundation by producing versatile components that cater to a wide range of end products.

**In the medium term**, Cambodia can advance up the value chain by focusing on higher-value assembly and targeting more complex product segments, especially consumer, industrial and network electronics.

**In the long term**, Cambodia can pursue more complex products including:

- Automotive electronics: targeting advanced components to integrate further into the regional automotive value chain, particularly in response to the rise of EVs
- Medical technology : Developing entry-level electronics components for this high-growth global sector

Cambodia could also work towards becoming an integrated electronics production hub, spanning the entire value chain from design and component manufacturing to sub-assembly and final assembly.

### ***Vehicles and machinery***

**In the short to medium term**, Cambodia can focus on realising the potential of recent FDI deals in vehicle assembly, especially the announced BYD EV assembly plant. Cambodia can also build its manufacturing base by cementing the foundation in nascent industries and establishing itself as a regional assembly hub. Focus areas include:

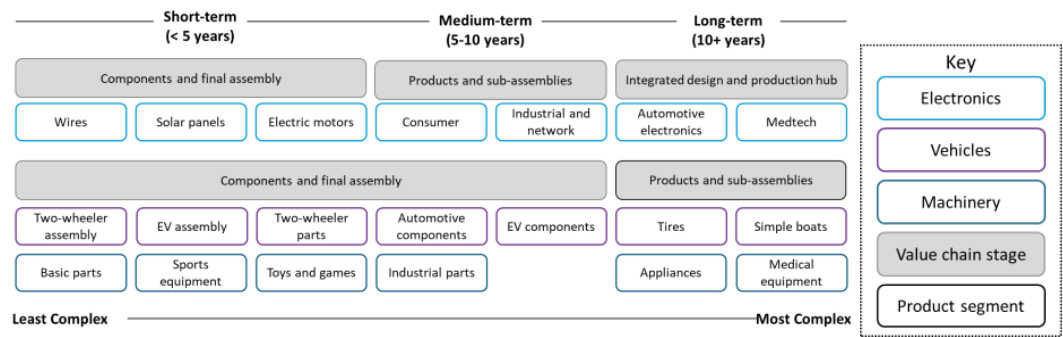
- Simpler, labour-intensive vehicle components, such as wiring harnesses, tyres, seats and basic electronics and electrical components (like sensors, switches and basic communication devices)
- Basic parts (like pumps, pulleys and ball bearings)
- Basic equipment (such as sports equipment, toys and games)
- Simple machines like appliances
- Domestic production of the inputs to bicycles and motorcycles to increase

value addition and strengthen domestic supply chains

**In the long term**, Cambodia can move up the value chain into more complex, higher value-added components. Key focus areas include:

- Traditional automotive components such as radiators, thermal systems and safety electronics
- EV components such as converters, inverters, vehicle control units, electric motor casings and battery pack assembly
- More complex industrial parts such as turbines, valves and filters
- More complex equipment, such as medical devices

Figure 13: Diversification pathways in electronics, vehicles and machinery



Source: Modified from Royal Government of Cambodia (2022).

## 6. Recommendations

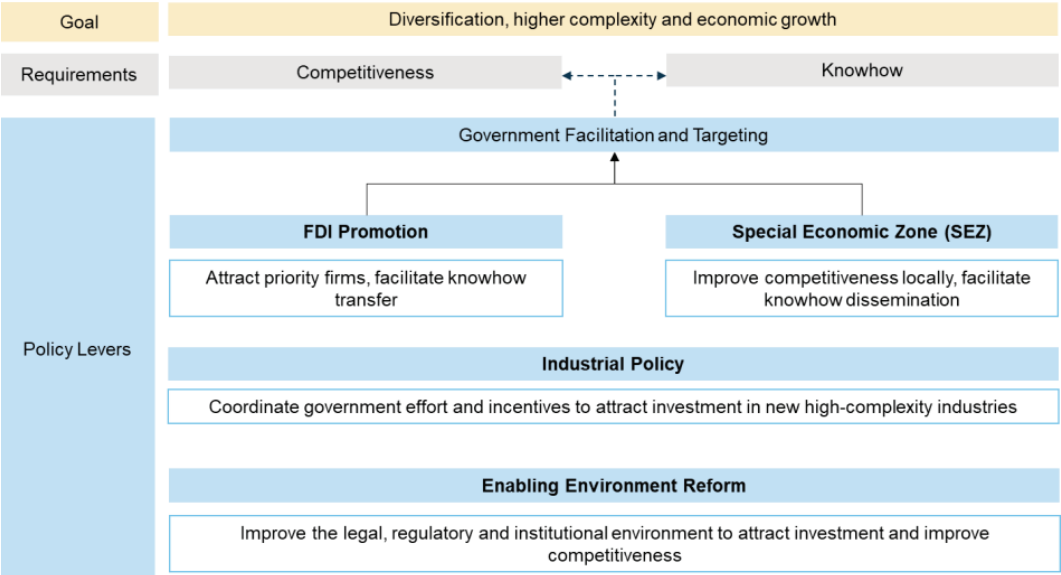
**A wide body of research and strategies already exists on economic diversification and the constraints to private sector development in Cambodia (e.g. OECD 2018; World Bank 2021; AMRO 2024c).** While these documents comprehensively address Cambodia’s competitiveness challenges and the industries with diversification potential, they do not sufficiently discuss how to achieve diversification. Relatedly, their recommendations focus on improving competitiveness with limited emphasis on facilitating diversification through the accumulation of knowhow.

Another challenge with the existing literature is the sheer volume of recommendations. While reform prioritisation is usually discussed, dozens of recommendations still end up on the high-priority list. This ‘laundry list’ approach can encourage ‘policy reform fatigue’ (Velasco, Rodrik and Hausmann 2005).

Given these findings, we offer a tailored, non-comprehensive list of both high impact and “low-hanging” recommendations.<sup>10</sup> We add to the existing literature by focusing our recommendations on:

<sup>10</sup> Referring to policy actions that are relatively easy to implement, quick to achieve, and potentially provide immediate benefits.

Figure 14: Policy levers to accelerate growth through diversification into higher complexity industries



Source: Authors

- How to acquire **knowhow** and facilitate diversification
- Alleviating the **binding constraints** to competitiveness, discussed above
- How the government can best use **financial incentives and other industry support** to facilitate diversification
- What is **politically supportable and administratively feasible within the short to medium term**, (or close to feasible with assistance from organisations like CDRI or other development partners)

Note that the Overview Report, as well as its background papers, include detailed recommendations addressing several of the constraints identified by this report, especially skills, governance and effective policy implementation. As such, we cover these constraints in less detail.

As shown in Figure 14, the government has several policy levers to achieve these goals. Each is discussed in turn below.

### 6.1. Government facilitation and targeting

#### *Further target government reforms and fiscal support to priority industries*

Currently, government agencies and strategies prioritise many industries. Such broad priorities effectively result in little to no actual targeting. In other words, if everything is a priority, nothing is a priority.

Instead, the government should consider providing more support to fewer firms. This support should go to industries discussed above to compensate for the market failures in the diversification process and other competitiveness constraints. This applies to all government support, especially regarding: FDI promotion, fiscal incentives like tax breaks, trade promotion,

subsidised loans and grants and skills development programmes. Existing firms in well-established exporting industries have already demonstrated that they are internationally competitive and therefore do not require ongoing government support.

**Recommendation: RGC (led by Ministry of Economy and Finance) should proceed with the planned evaluation of tax expenditures**, focusing on the effectiveness of fiscal incentives in attracting FDI, promoting diversification, and boosting competitiveness. The evaluation should:

- Identify which sectors gain the most from existing incentives and whether these translate into tangible benefits such as technology transfer, skills upgrading, and domestic value addition.
- Benchmark Cambodia's incentives with regional competitors to ensure alignment with global best practices and avoid unnecessary tax losses.
- Identify redundant incentives.
- Assess whether firms can easily access incentives for knowhow accumulation and competitiveness (e.g., for labour exchanges, skills development, or technology adoption), and identify barriers such as lengthy or complex application processes that may deter use.

Based on the findings, RGC should then:

- Retarget incentives to pioneer investors in priority sectors.
- Adopt performance-based incentives to further tie expenditure to outcomes such as job creation, local sourcing, and skills development.

- Improve transparency and access by simplifying and clarifying the incentive regime and application processes to reduce investor uncertainty and increase uptake of effective incentives.
- Establish ongoing monitoring and adjustment to keep incentives aligned with evolving priorities.

## 6.2. FDI promotion and SEZs

FDI is a tried and trusted path for accumulating the knowhow required to diversify into new industries. It can also generate demand for goods and services from domestic firms. We recommend strategies and policies to not only attract FDI, but ensure that it facilitates knowhow transfer to domestic workers and firms.

### *Attract and facilitate FDI in agro-processing and electronics, including through the use of SEZs*

Cambodia has attracted significant FDI over the last 20 years; however, a minority of this has supported diversification into new priority industries. The required policy response is therefore to improve FDI quality by targeting pioneer firms in priority industries. FDI incentives are also a critical tool, but they are not sufficient on their own.

The RGC should not only seek higher quality FDI, but also actively encourage the transfer of knowhow from foreign firms to domestic firms and workers to drive ongoing diversification and sector growth. This requires targeted policies that: (1) promote labour mobility through expatriate visas and exchange programmes; (2) encourage foreign investors to invest in skills development and promote local workers to senior technical and managerial



positions over time and (3) establish stronger linkages with local firms.

Several existing government policies set out similar recommendations. In particular, the Council for the Development of Cambodia's (CDC) "Automotive and Electronics Sectors Development Roadmap" makes the case for prioritising electronics and contains a detailed plan for attracting FDI in this sector.

**Recommendation: We recommend that the RGC scale up their efforts (primarily through the CDC) to identify and then support pioneer entrepreneurs looking to invest in priority industries that can generate the greatest knowhow and other positive spillover effects.** Specifically, the CDC should:

- Receive additional resources and capacity for investment promotion and facilitation
- Leverage Article 28 of the Law on Investment to offer additional flexible incentives for pioneer firms in priority industries
- Better coordinate with the Ministry of Commerce (MOC) and pool resources to conduct joint investment and trade promotion activities abroad
- Ensure existing incentives (from the Law on Investment) are easier to access and delivered on time
- Actively encourage foreign investors to use existing tax incentives for skilled labour exchanges and on-the-job training
- Focus investment facilitation efforts on common constraints like land availability and tenure, infrastructure (especially renewable energy), QI) and logistics (especially through the use of SEZs), as

well as expediting approvals (such as Environmental Impact Assessments)

- Establish and regularly update a database of state-owned or otherwise available land suitable for investors in priority industries (both individual-purpose plots and dedicated SEZs)
- Digitise FDI-associated processes to enhance efficiency and fairness (by automating tasks, reducing bureaucratic delays and ensuring transparent procedures)
- Coordinate with the Ministry of Labour and Vocational Training to make flexible long-term visas available for senior technical expatriates employed by foreign investors in priority industries
- Promote cross-border collaboration through programmes such as Thailand Plus One

**Recommendation: The RGC, led by the Ministry of Economy and Finance, should proceed with the planned evaluation of the Skills Development Fund** and investigate how the fund could better target the skills needed by foreign investors in priority industries. Depending on the results of the evaluation, pilot initiatives could be developed to improve such targeting.

***Fast track the approval and implementation of the planned agro-processing industrial park***

Ongoing cross-ministry efforts to establish Cambodia's first agri-food industrial park are an excellent example of the government effort to attract FDI and establish SEZs in a priority industry (agro-processing). Indeed, a recent feasibility study found that an agri-food industrial park could contribute an additional USD5.1 billion to the Cambodian



economy by 2045 and employ over 100,000 people while lifting over 20,000 people out of poverty each year.

**Recommendation: Fast track approval of the government's plans to develop an agro-processing industrial park led by the Ministry of Economy and Finance.** Specifically, the government should:

- Offer a targeted FDI incentive package, including supporting infrastructure
- Promote the “private sector led, government-linked” industrial park model
- Attract internationally experienced industrial park operators to run the agro-processing park
- Provide an on-site one-stop facilitation service for permits, taxes, customs, certifications, etc.

### 6.3. Industrial policy

Industrial policy refers to strategic efforts by the government to promote the competitiveness, innovation and expansion of key industries. Typical industrial policy tools include tax incentives, funding, subsidising research and development, trade policy (such as tariffs or free trade agreements) and targeted infrastructure investment.

Industrial policy also includes more direct industry interventions through dedicated public agencies; Such approaches can be especially successful when targeted and coordinated to address market failures.

#### **Promote linkages to SMEs**

Cambodia's economy has grown rapidly over the past two decades. However, this growth has been primarily driven by large firms, many of which are foreign-owned, in

only a few sectors: garment manufacturing, tourism and construction. This growth has been far from inclusive and has made the economy less resilient to external shocks.

Small and medium-sized enterprise (SME) linkages refer to supplier-buyer relationships between large firms and SMEs along industry value chains. SME linkages support broad-based economic growth by fostering SME competitiveness, innovation, employment and export growth. Strong linkages also facilitate productivity transfer while serving as attractive signals for new FDI.

Moreover, fostering stronger linkages with SMEs could offer Cambodia several advantages for the future, particularly as the country will face stricter requirements around local content requirements and rules of origin. By enhancing SME linkages, Cambodia could increase local production, which supports meeting the local content thresholds necessary to access preferential trade agreements.

Ideally, such linkages should be built with Cambodian-owned firms. However, in the short-term, foreign parts suppliers can also be encouraged to invest in Cambodia.<sup>11</sup>

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11 For example, a Chinese electronics manufacturer already located in Cambodia plans to relocate more elements of his supply chain to Cambodia. He noted Cambodia's competitive advantages, including lower labor and land costs compared to Vietnam and China. However, the shortage of local suppliers remains a key challenge, forcing the firm to import most inputs from China and Vietnam, increasing costs and lead times. To address this, the investor plans to encourage his Chinese suppliers to establish operations in Cambodia, streamlining the supply chain and reducing dependencies. CAPRED (2025) interview with a Chinese electronic manufacturing firm in the Bavet SEZ.

**The business environment and the limited capabilities of both local firms (especially SMEs) and local workers are cited by foreign firms as the main reasons for limited linkages** (Phurik-Callebaut 2020).

Recommendations to improve the enabling environment are discussed below, while this section recommends policies to improve SME capacity.

**Recommendation: Establish a SME linkages programme, potentially under Khmer Enterprise** (led by the Ministry of Industry, Science, Technology and Innovation). Essential elements of this plan include:

- Focus on industries that support Cambodia's larger diversification and competitiveness goals and provide the greatest opportunities for SME linkages and knowhow transfer. As discussed above, these include electronics and agro-processing.
- Work with industry associations to understand the needs of larger firms and ensure that SME support programmes are aligned with these needs
- Identify SMEs with the potential to reliably supply larger firms. Provide these SMEs with end-to-end support including financial aid, capacity building and matchmaking
- Provide market research and information services to help SMEs understand market demands and identify potential opportunities
- Establish platforms or events for matchmaking between SMEs and larger firms, such as trade fairs, networking events and online platforms

- Improve support on access to finance, including through partnerships with the Credit Guarantee Corporation of Cambodia, the Agriculture and Rural Development Bank (ARDB), SME Bank and the recently established Cambodia Climate Financing Facility
- Better coordination with the CDC and MOC on FDI and export promotion

***Renewable energy support for targeted firms and industries***

As discussed above, electricity costs are a commonly cited constraint to competitiveness. While much of Cambodia's electricity supply and associated costs are locked in over the medium term, small adjustments to energy policy can help reduce electricity costs and improve reliability for industries targeted for diversification.

An immediate policy to improve competitiveness is to adjust the rooftop solar compensation tariff. While it is important for Cambodia not to 'open the floodgates' and potentially destabilise the grid, the current law does not allow the government to adjust the compensation tariff flexibly across industries and geographic locations. Such policy flexibility for industrial parks is currently being pursued by Vietnam (The Investor 2025).

This proposal serves to improve competitiveness by reducing electricity costs and support diversification into new manufacturing industries, while also promoting climate resilience and green growth. At the same time, it does not require direct government expenditure, can be implemented rapidly and is not administratively difficult to implement.

**Recommendation: The RGC, led by the Ministry of Mines and Energy, should significantly lower or remove the compensation tariff for strategic industries**, such as agricultural processing (which has large economic multiplier effects), electronics manufacturing and other priority FDI sectors. For example, such an exemption is part of the incentive package for the government's proposed agro-industrial park. This would encourage new investment while avoiding grid destabilisation.

Expanding the nighttime electricity tariff is another policy move to reduce the impact of high electricity costs on Cambodia's competitiveness. Currently, the nighttime tariff—set at almost half the daytime rate—is available from 9 pm to 7 am. However, its impact is limited as the complex application process deters firms from taking advantage of the reduced rates, and the current start time is too late for many businesses to adjust their operations.

**Recommendation: Cambodia's electricity utility (Electricité du Cambodge, EDC) should amend the nighttime electricity tariff.** Specifically, EDC should extend the tariff start time to 6 pm to better suit business operations and simplify the application process to encourage broader participation. Additionally, EDC should prioritise access for key industries, such as agro-processing and electronics, and conduct awareness campaigns to increase uptake.

### ***Improve quality infrastructure***

QI refers to the system of public and private institutions, policies and services that ensure products, services and processes

meet established standards of quality, safety and efficiency. This includes elements of standardisation, accreditation, metrology, conformity assessment and market surveillance.

Quality control (including sanitary and phytosanitary measures) are essential for helping firms access and maintain access to export markets and target niche markets with higher prices.

Certification measures, including organic fairtrade, ethical and other sustainability certifications, are also essential for product differentiation and accessing niche markets with higher prices. This applies to both processed and unprocessed agriculture and forestry products.

Shortfalls in Cambodia's QI are currently constraining exports in the priority industries like electronics and agro-processing.

**Recommendation: The RGC, led by the Ministry of Industry, Science, Technology and Innovation, should continue with plans to develop a government-wide Roadmap for QI to improve standardisation, compliance and efficient certification of product quality.** The roadmap should identify gaps and impediments across Cambodia's QI institutions and regulations, recommend specific improvements and detail the budget and staff required to implement the recommendations.

### ***Promote skilled immigration, returned migration, and diaspora investment***

Immigration is one of the fastest and most direct ways to bring in knowhow. Immigration policies should focus on attracting foreigners bringing needed knowhow to generate new industries.

In particular, foreign investors almost always need to fill senior technical and managerial roles with experienced foreign workers while establishing a new business. For example, Thailand has made liberal immigration a key aspect of its FDI promotion. By enabling the growth of new industries, skilled migrants will create far more jobs for Cambodian workers than the few positions filled by foreign specialists. Over time, even these jobs can be transferred to Cambodian workers once the knowhow has been transferred. While Cambodia does not impose especially high barriers to immigration currently, it could do more to encourage skills-based immigration.

A country's migrants and diaspora also have the potential to create new industries by bringing knowhow and market connections. This process is already partly underway in Cambodia, where many returned migrants have started businesses upon their return. However, such businesses are usually not focused on new industries or exporting.<sup>12</sup> Several countries have launched successful programmes to repatriate skilled migrants or leverage large diaspora, including India, Taiwan, and China (World Bank 2006). Cambodia could learn from these experiences and implement a similar but contextualised programme.

**Recommendation: The Ministry of Industry, Science, Technology and Innovation, together with the Ministry of Labour and Vocational Training, should develop and implement a talent attraction**

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<sup>12</sup> CAPRED case study collection based on interviews, news articles, and other media.

**plan** targeted at skilled immigrants, and Cambodian migrants abroad diaspora with manufacturing knowhow.

## 6.4. Enabling Environment Reform

Business-enabling environment reform refers to the process of creating or improving legal, regulatory and institutional frameworks to support private sector development. Such reform is essential for lowering business costs, attracting new FDI, and ultimately, sustaining robust economic growth.

Although the CDC's introduction of the Single Portal System aims to streamline business registration, implementation at local levels needs to be more consistent. Provincial authorities often need more capacity and resources to process investment applications efficiently, leading to further delays and frustration. Similarly, efforts have been made to improve Cambodia's legal infrastructure, such as establishing the National Commercial Arbitration Centre. However, many foreign investors who prefer international arbitration lack confidence in Cambodian legal institutions and judicial independence.

### ***Prioritise the regulatory environment improvements required to enhance competitiveness in priority industries***

The regulatory requirements on businesses in Cambodia, delivered through services like registration, licensing and permits, are burdensome and lack clear policy objectives, necessitating comprehensive reform. As of 2023, approximately 5,105 services are provided by line ministries, state agencies and subnational administrations, managed through inter-ministerial Prakas

with the Ministry of Economy and Finance. Many of these services were established primarily to collect non-tax revenue, with little justification for their necessity or support for business sectors. The lack of a comprehensive review has led to a proliferation of non-functional services that impose unnecessary burdens on businesses.

**Recommendation 7: Conduct a regulatory review and impact assessment** (led by the Ministry of Economy and Finance, with collaboration from line ministries and the Ministry of Interior) with the goal of streamlining processes, decentralising services to the subnational level through One Window Service Offices and promoting digitalisation via online platforms at both national and subnational levels.

One Window Service Offices at the subnational level are a key mechanism for delivering administrative services to SMEs and citizens, but have yet to reach their full potential due to several challenges. These include uncoordinated functional transfers from line agencies, unclear legal frameworks (e.g., issues for street vendors without a permanent address) and complicated application processes imposed by line ministries. Additionally, efforts to digitalise these services by the Ministry of Interior have been hampered by insufficient funding and poor integration with national digitalisation initiatives.

**Recommendation 7: Realise the potential of One Window Service Offices through a combined approach of functional assignment and regulatory streamlining** (led by the Ministry of Economy and Finance, Ministry of Interior, and Ministry of Industry, Science, Technology and Innovation regarding the informal economy policy). Functions transferred to these offices should be reviewed and justified, and the application processes streamlined to reduce compliance burdens. Furthermore, increased support from the Ministry of Economy and Finance and development partners is essential to expand and strengthen digitalisation at One Window Service Offices and link them with national efforts, such as the CamDX business registration platform. Specifically, the government should:

- Link remaining ministries to the Single Window Service Offices and ensure clear approval procedures and cost transparency
- Digitise and streamline processing of registration, licensing, certification, taxation and customs systems/permits
- Accelerate the decentralisation of One Window Service Offices at the subnational level

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