

COUNTRY STRATEGY PAPER

2004-2006

CAMBODIA

NB: The National Indicative Programme (chapter 6) limits its scope to budget years 2005–2006. It is part of the Country Strategy Paper, which gives the framework for cooperation 2004–2006.

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PREAMBLE

The Council Regulation (EEC) N° 443/92 of 25 February 1992 on financial and technical assistance to, and economic co-operation with the developing countries in Asia and Latin America (“ALA Regulation”), which applies to Cambodia, indicates that, whenever possible, indicative five-year programming shall be established for each country. The Regulation also foresees that the indicative multi-annual guidelines that apply to the main partner countries shall be adopted in coordination with a committee composed of representatives of the EU Member States. The multi-annual strategic planning is based on a Country Strategy Paper (CSP), which sets out the co-operation framework for the time period covered by the CSP. The CSP is translated into operational guidelines, laid down in the multi-annual National Indicative Programmes (NIPs).

The previous EC-Cambodia Country Strategy Paper, covering 2000-2003, was agreed with the Royal Government of Cambodia and approved by the ALA Committee in 2000. With the establishment of a common framework for CSP a National Indicative Programme, covering the years 2002-2004, was approved by the ALA Committee in 2002. **As the previous CSP was prepared before the common framework for CSPs was agreed, it covered only the years 2000-2003. It has therefore been agreed that the new CSP will cover the period 2004-2006 in order to be in line with other CSPs in Asia. The CSP 2004-2006 therefore covers activities to be committed in 2004 from the NIP 2002-2004 as well as activities foreseen in the new NIP covering 2005-2006.**

The General Affairs and External Relations Council (GAERC) of March 2003 fixed four criteria against which to assess the validity of the CSPs and the need for possible changes of the CSP and/or the National Indicative Programme. Mid-Term Review (MTR) missions were fielded to verify the CSPs against these criteria. The MTR for Cambodia was carried out during the first quarter of 2003. As the MTR observed, the new priorities in external EU/Community policies (TRTA, JHA issues etc) are sufficiently covered in the current CSP/NIP, taking into account EC resources available. However, considering the cross-border nature of issues such as human trafficking and the existing regional co-operation in combating drug trafficking, additional activities on the regional level could be considered. Changes in the international context were not deemed to have had a significant impact on the framework for EC-Cambodia relations. The development inside ASEAN is being addressed bilaterally and through regional EC-ASEAN programmes.

The MTR concluded that the CSP remained relevant and highlighted that a new CSP, covering 2004-2006, should be prepared as the current one was due to expire at the end of 2003. The MTR also concluded that the focal sectors foreseen in the NIP 2002-2004 were complementary to co-operation activities by EU Member States and other donors, and that no revision of the NIP 2002-2004 was required.

This document therefore covers the EC-Cambodia Country Strategy Paper 2004-2006 and the National Indicative Programme 2005-2006.

THE EC-CAMBODIA COUNTRY STRATEGY PAPER 2004-2006

Executive Summary

Cambodia is still in the process of emerging from a severely traumatic post-crisis situation.

Violence, domestic and public, remains endemic. Weak law enforcement exacerbates the situation, resulting in significant impunity, fuelled by corruption. Although important steps have been taken to establish a multi-party democracy and to address governance and human rights issues, Cambodia still needs to progress further towards a fully functioning democracy.

According to IMF and Asian Development Bank (ADB) data, real GDP growth reached 5.2% in 2003. Real GDP growth in 2004 is expected to reach around 4-4.5%. In 2005, GDP growth may decelerate even further, due to increased competition arising from the textiles quota liberalisation. The share of garment exports in total domestic exports was 85% in 2002, and although tourism receipts totalled only ¼ of the value of garment exports, these two sectors are by far the mainstays of the Cambodian export structure. Cambodia's garment export industry, totalling 1,6B US\$ in 2003, will face stiff competition from other garment exporters when trade among World Trade Organization (WTO) members is fully liberalised in 2005.

A variety of conditions, ranging from malnutrition, illiteracy, gender discrimination, limited access to social services to weak social capital, contribute to the country's socio-economic inadequacies. Poverty in rural areas is most acute. 80% of the poor live in rural areas and are dependent upon agricultural production and natural resource extraction for their livelihoods.

Cambodia faces multiple challenges in education, including a low-skilled population characterized by low productivity, a high number of out-of-school youth due to persisting deficiencies of the formal school system, and a very young and rapidly growing population increasing the demand for education services. In addition, the health status of the Cambodian population is among the lowest in the Western Pacific region. The high cost and low quality of health care in Cambodia, is estimated to consume about 11% of household income.

The Cambodian authorities have embarked on an ambitious reform programme. The key priority of the government is to foster broad based economic growth with the private sector playing the lead role, to improve the access of the poor to social services, to promote sustainable management and use of natural resources and to improve governance.

The overarching goal of EC-Cambodia co-operation is to target poverty reduction in rural areas. The co-operation policy, outlined in this paper, aims to support the implementation of this and other EU policy objectives. Taking into consideration the activities of other

donors as well as experience from previous EC co-operation with Cambodia, the paper concludes that the EC's co-operation programme should focus on two focal sectors:

Taking into account relevant economic sectors that have a bearing on rural areas, including trade, the first focal area for EC-Cambodia co-operation will be **pro-poor economic development**. The EC strategy in this focal area will target rural livelihoods. While development of agriculture is emphasised - particularly as regards small-scale irrigation, crop diversification and improved technologies - attention will also be given to the development of local SMEs, their access to market and trade enhancing measures.

Considering that poverty alleviation in the rural areas is closely linked with development in health and education, support to the **social sector** will be the second focal area for EC support. Crosscutting and complementary themes to the focal sectors are related **governance and democratisation issues**.

In addition, human resource development will form an integral part of all EC development programmes, as will environment and gender issues. As regards gender issues, women and children form a particular focus for Cambodia under the EIDHR and the participation of women in human resource development activities is encouraged.

The implementation of EC cooperation activities in Cambodia will be complemented by an increased focus on policy dialogue in the identified focal sectors. The Commission will, through policy dialogue, support the RGC's move towards SWAPs in the focal sectors.

Abbreviations

ADB	Asian Development Bank
AFTA	ASEAN Free Trade Area
ALA	Asia Latin America
ASEAN	Association of Southeast Asian Nations
AUNP	Asean University Network Programme
CAR	Council for Administrative Reform
CFSP	Common Foreign and Security Policy
CG	Consultative Group
CPP	Cambodian People's Party
CSP	(EC) Country Strategy Paper (for Cambodia)
DAC	Development Assistance Committee
DFID	Department for International Development (UK)
DTIS	Diagnostic Trade Integration Study
EC	European Commission
ECOSORN	"Economic and Social Relaunch of the Northwestern provinces"
ECHO	EC Humanitarian Office
EIDHR	European Initiative for Democracy and Human Rights
EFA	Education for All
ESP	Education Strategic Plan
ESSP	Education Sector Support Programme
EU	European Union
FDI	Foreign Direct Investment
FTA	Free Trade Agreement
FUNCINPEC	Front Uni National pour un Cambodge Indépendant, Neutre, Pacifique et Coopératif
GAERC	General Affairs and External Relations Council
GAP	Governance Action Plan
GMO	Genetically Modified Organisms
HDI	Human Development Index
HRMIS	Human Resource Development Information System
HSP	Health Sector Strategic Plan
ICC	International Criminal Court
IDA	International Development Association
IFAPER	Integrated Fiduciary Assessment and Public Expenditure Review
IFC	International Finance Corporation
IMF	International Monetary Fund
JHA	Justice and Home Affairs
JICA	Japan International Co-operation Agency
MAFF	Ministry of Forestry and Fishery
MDG	Millennium Development Goals
MEF	Mid-Term Expenditure Framework
MFI	Multinational Financial Institutions
MoC	Ministry of Commerce
MoEF	Ministry of Economy and Finance

MoEYS	Ministry of Education, Youth and Sport
MoH	Ministry of Health
MoRD	Ministry of Rural Development
MS	Member States (of the European Union)
MTR	Mid-Term Review
NEAP	National Environment Action Plan
NGO	Non-Governmental Organisation
NIP	National Indicative Programme
NPRS	National Poverty Reduction Strategy
ODA	official development assistance
OECD	Organization for Economic Co-operation and Development
PAP	Priority Action Programmes
PERC	Rehabilitation Programme for Cambodia
PLG	Partnership for Local Governance
PRGF	Poverty Reduction and Growth Facility
PRSP	Poverty Reduction Strategy Paper
RGC	Royal Government of Cambodia
SEDP	Socio-Economic Development Plan
SME	Small and Medium Enterprise
SOCB	state-owned commercial banks
SPS	Sanitary and Phyto-Sanitary measures
SRP	Sam Rainsy Party
SWAp	Sector Wide Approach
SWiM	Sector Wide Management
SWOT	Analysis of Strengths, Weaknesses, Opportunities, Threats
TBT	Technical Barriers to Trade
TREATI	Trans-Regional EU-ASEAN Trade Initiative
TRTA	Trade Related Technical Assistance
UK	United Kingdom
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
UNESCO	United Nations Education, Scientific and Cultural Organization
UNFPA	United Nations Population Fund
UNICEF	United Nations Children's Fund
UNIDO	United Nations Industrial Development Organization
USAID	United States Agency for International Development
UXO	Unexploded ordnance
WB	World Bank
WFP	World Food Programme
WHO	World Health Organization
WTO	World Trade Organisation

Cambodia at a glance

INDICATOR	VALUE	YEAR(S)
Area	181.000 sq. km	
Population	14.2 million	2003
Annual population growth	2,2%	1996-2002
GDP (US\$)	3.9 billion	2003
GDP per capita	280 \$	2003
Real GDP growth (%)	5.0	2003
Consumer price inflation (average %)	1.7	2003
Current account balance (US\$)	-218.1 million	2003
Life expectancy	54 years	2002
Infant mortality rate (per 1.000 births)	97	2001
Maternal; Mortality (per 100.000 births)	437	2002

Sources: WB, ADB, UNDP

1. EUROPEAN UNION POLICY OBJECTIVES

Article 177 of the *Treaty of the European Communities* sets out the three broad objectives for Community development co-operation. These are: fostering of sustainable economic and social development; the smooth and gradual integration of the developing countries into the world economy; the fight against poverty. This article also states that Community policy should contribute to the general objective of developing and consolidating democracy and the rule of law and encouraging the respect for human rights and fundamental freedoms.

Further to the Commission's Communication on "*The European Community's Development Policy*"¹, the Joint Council and Commission Declaration on Development Co-operation of November 2000 states that Community development policy is grounded in the principle of sustainable, equitable and participatory human and social and environmental development. Promotion of human rights, democracy, the rule of law and good governance are integral elements of EC policy, as well as the link between trade and development, support for regional integration and co-operation. The Declaration also specifies that, in line with the macro-economic framework, the Community must also continue its support in the social sectors (health and education).

¹ COM (2000) 212 final of 26.04.2000

The Treaty establishing the European Community foresees that the EC and the Member States shall co-ordinate their policies on development co-operation and shall consult each other on their assistance programmes, including in international organisations and during international conferences. Efforts must be made to ensure that the Community development policy objectives are taken into account in the formulation and implementation of other policies affecting the developing countries. Furthermore, as laid down in Article 20 of the Agreement, systematic account shall be taken of mainstreaming into all areas the following cross-cutting themes: gender and environmental issues, institutional development and capacity building.

The Commission communication "*A new partnership with South East Asia*"² identifies six strategic priorities, and outlines actions by which the EU's relationship with ASEAN and the countries of South East Asia could be improved. In particular, the EU should work to support regional stability and the fight against terrorism; contribute to the protection of human rights and to the spreading of democracy, good governance and the rule of law; mainstream justice and home affairs issues; further strengthen our mutual trade and investment flows with the region and support the development of the less prosperous countries of the region.

In its communication on conflict prevention³ the Commission has announced its intention to focus more clearly its co-operation on addressing root causes of conflict in an integrated way. Within this framework, the Commission will aim to incorporate specific conflict prevention measures in its development programmes.

2. THE POLICY AGENDA OF CAMBODIA

The "Rectangular Strategy" of the RGC foresees four main axes: the social stability, the regional and international integration, the partnership with the international community and the private sector for the development of the country, and the macro-economic development. Good Governance features at the core of the new strategy. It includes the adoption of the law against corruption (that will set up an independent institute to control public finances), the reform of the administration (with an increase of public servants' salaries of 10-15% per year, the simplification of procedures, etc.) and the army (with the demobilisation of soldiers) and the legal & judicial reform (adoption of new codes, setting up of Commercial Court, Administrative Court and Juvenile Court). Agriculture, infrastructure, employment and development of human resources are the priority sectors identified in the strategy.

Cambodia is committed to achieving the Millennium Development Goals (MDG) and has identified a set of specific international development targets by 2015. Although much household survey data has been gathered over the last decade, the data is not comparable due to differences in methodology and coverage. The government has established a poverty monitoring and analysis system which will be the main tool for regular reporting on progress in achieving the development goals. Cambodia presented its first MDG

² COM (2003) 399 final of 09.07.2003

³ COM (2001) 211 final of 11.04.2001

report in 2001. The report does not cover the full set of MDG but should rather be seen as the foundation for future expanded MDG reports.

The Second 5year Socio-Economic Development Plan 2001-2005 (SEDP II) was adopted by the Royal Government of Cambodia on 29th July 2002. The strategy of the SEDP II can be summarised as follows;

- i) to foster broad based economic growth with equity, with the private sector playing the lead role;
- ii) to promote social and cultural development by improving the access of the poor to education, health, water and sanitation, power, credit, markets, information and appropriate technology;
- iii) to promote sustainable management and use of natural resources and the environment, and
- iv) to improve the governance environment through effective implementation of the Governance Action Plan (GAP).

The line ministries designated to play a key role in poverty reduction are the Ministry of Education Youth and Sport (MoEYS), the Ministry of Health (MoH), the Ministry of Agriculture Forestry and Fishery (MAFF) and the Ministry of Rural Development (MoRD).

A National Poverty Reduction Strategy (NPRS) was adopted in December 2002, building on the Interim Poverty Reduction Strategy and the SEDP II. The EC participated in the consultation process throughout the preparation of the NPRS. The NPRS includes a comprehensive set of performance indicators, and establishes mechanisms for tracking progress in achieving targets over time.

By preparing and offering a strategic poverty reduction document the Royal Government of Cambodia expects that its development partners will increasingly align their assistance with this programme. The Government intends to link the NPRS process to the Consultative Group (CG) process. This mirrors the statement by the Council and the Commission on 10th November 2000 on EC Development Policy that stresses support to national PRSPs where they exist.

It is foreseen that the next Socio-Economic Development Plan and the corresponding NPRS will be merged and presented as one document in 2005.

The priority actions required to implement the Government's Poverty Reduction Strategy are structured under four pillars: promoting opportunities, expanding capabilities, reducing vulnerability, and improving security and governance.

The EC's Country Strategy Paper (CSP) 2004-2006 closely follows the priority sectors identified in the NPRS by the Royal Government of Cambodia. These sectors are sub-divided into three headings, namely:

Poverty and inequity challenges: rural development, basic education and health.

Economic challenges: fiscal reform, trade and private sector development.

Governance and democratisation challenges: legal and judicial reform, decentralisation and donor coordination.

Seven key points are to be made regarding the NPRS:

i) The National Poverty Reduction Strategy was prepared through extensive consultations with line ministries, the private sector, civil society organisations and donors. This is to be commended considering the country's long history of conflict and civil war, which formally ended with the signing of the Paris Peace Agreements in 1991, although the last Khmer Rouge only agreed to lay down their arms as late as 1998.

ii) Considering the extent of the agreed reform programme and the need for comprehensive sectoral strategies, a major challenge for the new Government is to ensure that the priorities of the NPRS are linked to the Government's Medium-term Expenditure Framework (MEF). This would place the NPRS in a central position in the preparation of the national budget, and provide individual line ministries with greater opportunities to achieve the stated NPRS targets.

iii) A strong emphasis is put on the need to improve rural livelihoods through the promotion of sustainable agricultural development and a diversification of agricultural produce, and a need to invest in small and medium sized enterprises with value-added processing capacities

iv) The Education Strategic Plan (ESP) for 2001-2005 was jointly endorsed by the RGC and donors/NGOs in mid 2001 to achieve the goal of "Education for All" (EFA) within eight years. The Education Sector Support Programme (ESSP) aims to ensure that public resources primarily benefit the poor and includes interventions targeting the most vulnerable groups. Challenges remain numerous, considering the low salaries of teachers and a lack of infrastructure and material.

v) The NPRS confirms the importance of trade as a critical component of poverty reduction. Taking advantage of a recently concluded trade diagnostic study, prepared for the then up-coming accession to the WTO in September 2003, the NPRS reflects upon a range of trade issues, including an analysis of the risks associated with multilateral trade liberalisation.

vi) Gender issues are particularly well-addressed throughout the NPRS. The disaggregation of indicators by gender has been done for education, health, and the legal sector in order to better address the participation of women in society and in development programmes.

vii) Governance issues are clearly addressed in the NPRS, identifying the fight against corruption as a cross-cutting issue critical for reducing poverty, and facilitating the important process of decentralisation. However, while the GAP was developed to tackle

problems within national governance institutions and systems, its rapid implementation will be the real sign of the government's commitment to deal with these issues.

3. ANALYSIS OF THE POLITICAL, ECONOMIC AND SOCIAL CONTEXT

3.1 Political Situation

After twenty years of conflict and civil war, the signing of the Paris Peace Agreements in October 1991 launched Cambodia on a process of democratic reconstruction and transition to a market economy. This process, which was backed by a UN presence until the first parliamentary elections in May 1993, facilitated the foundation of a constitutional monarchy with King Sihanouk as Head of State, and led to the appointment of a power-sharing government comprising two parties. Two co-prime ministers were appointed, Prince Norodom Ranariddh of the royalist FUNCINPEC party and Hun Sen of the Cambodian People's Party (CPP).

The process came to a halt in July 1997 when First Prime Minister Prince Norodom Ranariddh was ousted after armed clashes between supporters of the two main government coalition parties.

The national elections of July 1998 resulted in a National Assembly composed of three parties: Cambodian Peoples' Party (CPP), Front Uni National pour un Cambodge Indépendant, Neutre, Pacifique et Coopératif (FUNCINPEC) and the Sam Rainsy Party (SRP). Post-election negotiations resulted in the formation of a coalition government between the CPP and FUNCINPEC in late November 1998, with the SRP as the opposition. At the same time, the creation of the Senate was suggested by the King. Senators have been appointed by the political parties present in the National Assembly and by the King. The mandate of the current Senators is now foreseen to come to an end by March 2005.

In February 2002, Commune Councillors of all the 1621 Communes were elected for a five-year mandate, allowing a multi-party system at the commune level to strengthen local democracy and the participation of the population in local development.

The last national elections took place on 27th July 2003. Although the atmosphere calmed down after the riots against the Thai embassy and some Thai business interests in Phnom Penh (29th January 2003), concerns remained during the pre-election period over the number of alleged political killings and the inflammatory, xenophobic rhetoric of some political parties during the campaign. However, compared with previous elections the atmosphere during the campaign period was less tense and there were fewer violent incidents. Following several months of political stalemate between the three main parties, the National Assembly agreed the new CPP-FUNCINPEC coalition government on 15 July 2004.

After long negotiations with the United Nations, the Law on the establishment of extraordinary chambers in the courts of Cambodia for prosecution of crimes committed during the period of Democratic Kampuchea, was promulgated in August 2001. The UN General Assembly approved, after additional negotiations, the Draft Agreement on the

modalities for the implementation of the Law, which set out the structure of international contributions (technical and financial) necessary for the process. This led to the signature of the Agreement by the RGC and the United Nations in June 2003. The Agreement will require ratification by the Cambodian side, amendments to the Law and an exchange of letters before the formal establishment of the extraordinary chambers. The political commitment of the RGC as well as international support will be critical for the implementation of the process.

Although Cambodia has made important gains in the field of human rights in the last decade, it is still a country in the early stages of a post-conflict situation. There are a number of human rights organisations and civil society groups engaging in advocacy, training and protection work in the human rights field, but much remains to be done. Violence, both public and domestic, the latter mainly affecting women and children, remains endemic. Weak law enforcement exacerbates the situation, resulting in significant impunity, fuelled by corruption. Even if important steps have been taken to establish a multi-party democracy and to address governance issues, Cambodia still needs to progress further towards a fully functioning democracy. Indigenous ethnic minorities account for less than 1 percent of the total population. Although discrimination against ethnic minorities is not a major problem, ethnic minority groups are mainly living in the poor and remote areas of the country and thereby facing additional difficulties as regards access to health and education.

3.2 Economic Situation, structure and performance

With a GNP per capita of 280 US\$ and rural earnings amounting to 40 US\$ a month per household, Cambodia is one of the poorest among East Asian countries.

Annual growth rates reached 7% between 1999 and 2001, driven largely by a buoyant garment export sector and the implementation of an internationally supported economic reform agenda. Foreign investment flows, however, declined sharply from 140.9m US\$ in 2001 to 47.8m US\$ in 2002⁴. According to IMF and Asian Development Bank (ADB) data, real GDP growth reached 5.2% in 2003, reflecting a strong rebound in agriculture. In 2003, the agricultural rebound offset weaker non-agricultural growth stemming from the SARS-related decline in tourism, and from election-related uncertainties. Real GDP growth in 2004 is expected to reach around 4-4.5%. In 2005, GDP growth may decelerate even further, due to increased competition arising from the textiles quota liberalisation⁵. Inflation in 2004 is expected to increase to an annual average of around 2.3%, reaching 3% in 2005. This is primarily due to higher oil and food prices.

The riel has stabilised against the dollar since 1999, halving the riel-denominated inflation rate to 3% between 1999 and 2002. The central bank has been intervening in the foreign exchange market to stabilize excessive short run exchange fluctuations. A high level of “dollarisation” exists in country, a situation that is not considered problematic in the short to medium term. Overall share of government spending maintains an upward

⁴ ADB figures 2003

⁵ almost 80% of Cambodian exports are represented by garments

trend reaching 17.6% of GDP in 2002. RGC recorded an overall fiscal deficit of 7.4% in 2002, higher than the government's aim of 6%. In 2003 fiscal discipline has slipped further due to election related spending.

Income distribution in Cambodia is highly uneven, with the poorest 20% sharing only 6.9% of national income and consumption. Poverty in rural areas is most acute. 80% of the poor live in rural areas and are dependent upon agricultural production and natural resource extraction for their livelihoods. Poor agricultural productivity growth in 2002 and modest services sector growth between 1994 and 2001, as evidenced by average annual growth rates of -2.7 and 2.8% respectively, does not bode well for the needs of a labour force expected to grow annually by around 250,000. The need for new employment opportunities challenges the government and the private sector to create jobs in rural areas.

3.3 Social developments

Low incomes alone do not explain poverty in Cambodia. A variety of conditions, ranging from malnutrition, illiteracy, gender discrimination, limited access to social services to weak social capital, contribute to the country's socio-economic inadequacies. Cambodia is ranked 130th out of 175 countries in the Human Development Index (HDI). Around 36% of its total population live on an income below 1 US\$ a day, whilst 40% of the rural population survive below the national poverty line (0.5 US\$ a day).

Adult illiteracy in Cambodia is 32.7%. Although gross and net primary enrolment ratios compare favourably with other Mekong countries, significantly lower gross secondary and tertiary enrolment ratios⁶ are of concern. Literacy among females aged between 15 and 24 years was 9% lower than the rate for males and the primary pupil-teacher ratio is much poorer than in Laos, Thailand and Vietnam.

While Cambodia is self-sufficient in rice production on a national level, factors such as poor infrastructure, varying soil quality, access to land, variable rainfall, drought and flood, result in an uneven distribution of the national staple. A lack of dietary diversification is one of the main causes of malnutrition, and micronutrient deficiencies in country. In addition, access to rural land continues to be impeded by the presence of landmines and unexploded ordnances (UXOs).

The health status of the Cambodian population is among the lowest in the Western Pacific region. The high cost and low quality of health care in Cambodia, estimated to consume about 11% of household income, cripples poor families and adds to the vicious cycle operating between ill health, malnutrition, poor social services and poverty. Death rates from preventable and controllable diseases are very high among both adults and children, with the main causes being respiratory infections, diarrhoea, malaria and tuberculosis. The poor in rural areas are particularly susceptible, due to a lack of access to safe water and sanitation.

⁶ standing at 18.7% and 2.8% respectively compared to 67.1% and 9.7% in Vietnam

3.4 Assessing the process of reform

Given the short period of time that has passed since the country experienced a return to democracy, the overall progress has been good. Strategies are in place at the national and sectoral levels to promote economic and social development and to address poverty.

Macroeconomic growth and fiscal stability have improved since the beginning of 1999 and were further strengthened under the Poverty Reduction and Growth Facility (PRGF). Tax revenues have increased but continue to suffer due to widespread smuggling and considerable exemptions from customs duty under the 1994 Law on Investment. Problems relating to collection have also affected income. The reform of the financial sector with respect to the re-structuring of the banking sector has been successful in so far that it has resulted in a banking system that is well capitalised and highly liquid. The RGC has started a complex reform of the trade sector, including streamlining custom administration.

The sectors where the reform process has been most dynamic are the social sectors, particularly education and health. The RGC is making steady progress in increasing funding for the social sectors and in improving the efficiency and effectiveness of spending on health and education. Despite this progress, disbursement rates in both the health and education sectors remain well below expectations due to chronic cash shortages and systemic and institutional constraints. This means that Cambodia's education and health expenditures as a percentage of GDP still lag behind the average for low-income countries, and compare poorly with the average levels of expenditure by countries in the region.

There is still a need for improvements as regards the implementation of reforms in public administration and in the legal and judicial sectors. The programme for the demobilisation of the military, agreed in 1999, has so far only been able to achieve a reduction in "ghost soldiers".

3.5 Main sectoral policies

Agriculture and natural resources

Cambodia is well-endowed with natural resources relative to the size of its population. Agricultural products have been identified as having a major potential for export led growth. The Government has acknowledged the need to modernise the agricultural sector whilst, at the same time, strengthening the capacities and resources of smallholder farming. Agricultural growth is to be achieved through increased private sector participation, improved infrastructure, private irrigation, crop diversification, and improved technologies. The RGC is now engaged in the promotion of private sector development, mainly among SMEs and a small number of international companies. The aim of private sector development is to link farmers to markets and recreate the delivery

mechanisms and retailer networks and associations that were destroyed during the years of war. Areas needing particular attention are access to information and capital.

The forestry sector remains problematic. Although a draft forestry law has been prepared, little thought has thus far been given to a practical sustainable forestry strategy. Unsustainable logging reportedly continues, and as a result the sector contributes very little to government revenue. Major problems also exist in the fisheries sector with the overexploitation of Cambodia's aquatic resources. Unsustainable fishing is taking place in many areas, notably in Tonle Sap, Cambodia's largest lake which supplies 40 percent of the country's fish protein and fish stocks are diminishing rapidly.

Trade development

A "pro-poor trade strategy" was endorsed by the Council of Ministers in 2001 and as a step to implement this strategy, a diagnostic trade integration and competitiveness study (DTIS) has been undertaken, outlining the links between trade development and poverty reduction, and the impact of trade reform on economic growth. With the support of the Integrated Framework, the Ministry of Commerce has developed an Action Plan containing a set of policy recommendations and priority capacity building needs to overcome the constraints identified. Trade policy priorities have been mainstreamed into the NPRS and a Technical Assistance Matrix has been developed. The RGC is presently revising the DTIS to include recent changes, primarily the need to comply with the terms of the accession protocol to the WTO. The revised DTIS will include an updated framework for Trade Related Technical Assistance (TRTA). It will make recommendations on how to improve policy dialogue and donor coordination, including a possible move towards a sector wide approach (SWAP).

The modernisation and simplification of import and export procedures and border controls is necessary to increase the competitiveness of Cambodian products on the world market. In particular, the garment sector would benefit enormously from such reforms. Restructuring of procedures needs to be accompanied by training for the customs services, and salaries/benefits of custom officials increased. In August 2004, the RGC presented a Trade Facilitation programme which includes also the setting up of a single window and a single administrative document for custom procedures. The WB will finance a programme for customs' automation.

Education

In recent years, the education sector has increasingly become a strong focus of the RGC's reforms, with the Ministry of Education Youth and Sport (MoEYS) launching a major overhaul of this sector. The MoEYS is fostering a sector approach and a policy-driven education reform programme aimed at implementing key reforms for equitable access, quality improvement and improved management and financing of education services at all levels.

In close cooperation with other stakeholders the MoEYS produced its first Education Strategic Plan (ESP) in 2001, which is supported by a rolling Education Support Sector Programme (ESSP). Priority Action Programmes (PAP) outline the key policy reforms of the MoEYS and are supported by financial management reforms in the Ministry of Economy and Finance. The ESP/ESSP medium-term programme is complemented by the long-term national Education for All (EFA) plan.

In the end of 2003, a comprehensive revision of the ESP was started to consolidate current achievements and to extend and deepen the range of policy and strategic reforms. The purpose of the ESP revision is also to enable a more immediate implementation of the RGC's broader development agenda, which includes: the realisation of NPRS poverty reduction targets through improved pro-poor access to education opportunities at all levels; the enhancement of Cambodia's economic competitiveness within the WTO framework, by improving the market responsiveness of education and training systems; the acceleration of economic growth and the advancement of social well-being through the deepening and diversification of Cambodia's human resource base and the achievement of agreed Millennium Development Goals (MDGs).

Health

Produced in 2002, the Government's first Health Sector Strategic Plan (HSP) provides guidance to the Ministry of Health (MoH) and international partners for the development of the health sector. The strategy is "to enhance health sector development in order to improve the health of the people of Cambodia, especially mothers and children, thereby contributing to poverty alleviation and socio-economic development". The HSP marks a major shift from a strategy based on health facilities coverage to one based on outputs and outcomes.

The HSP defines the priority areas of work and strategies to follow in order to reach its expected outcomes, which include: reduced maternal, infant and child morbidity and mortality rates, improved nutritional status among children and women, reduced total fertility rate, reduced household health expenditure especially among the poor, and a more effective and efficient health system. The MoH has developed a "Sector Wide Management" approach, which facilitates the implementation and monitoring of the strategic plan in close consultation and collaboration with all stakeholders.

Governance

The current Governance Action Plan covers several cross-cutting areas, including civil service reform, decentralisation and deconcentration, judicial and legal reform, public finance, anti-corruption, and gender equity.

The overall policy for **civil service reform** is in place, but there are important challenges for this long-term reform process. It will be crucial that the long awaited sustainable pay reform is clearly defined in consultation with all stakeholders, and implemented. The definition of a policy for human resource development and management is also critical

for efficient services delivery. The legal framework of the **decentralisation** process and its relationship with the deconcentration process is not fully in place. Progress has been made since the election of the Commune Councillors, with a legal framework allowing them to plan, develop and manage the communes' development plans and budgets. However, it has yet to be ensured that the communes have adequate human resources for socio-economic planning and development at the local level. The RGC has established a RGC/donor Working Group for the development of a joint long-term Strategic Framework on decentralisation and deconcentration.

While the legal framework has been expanded, the problem of weak enforcement remains unsolved. In 2003 the RGC adopted a Strategy on **Legal and Judicial Reform**, and a subsequent action plan, setting out short-term to long-term priority activities for implementation. A draft anti-corruption law has been adopted by the Council of Ministers, but has not yet been approved by the National Assembly. The implementation of the **military demobilisation** programme agreed in 2001 has stalled and there is presently no clear policy direction from the RGC. Large numbers of soldiers with arms contribute to violent crime and personal insecurity among the general population. To reverse this situation, the Government is actively promoting the registration and/or collection of small arms and weapons by the public, the armed forces, and the police.

3.6 External Environment

Both exports and imports increased significantly between 1999 and 2003. Exports increased by 20% per annum during the period, enhanced by an impressive growth in the garment and tourism sectors. The share of garment exports totalled 85% of total exports in 2002. Industries such as rubber, logs and sawn timber lag behind at 3.4% and 2.2% of total exports respectively (according to official figures), reflecting a general lack of will on forestry reform.

Cambodia's membership of the Association of Southeast Asian Nations (ASEAN) in 1999 and thus automatic accession to the ASEAN Free Trade Area (AFTA) has impacted on trade flows. Exports to ASEAN countries decreased from 42% to 6% of total between 1998 and 2001, whilst imports from the ASEAN region increased from 26% to 72% of total during the same period. To support its commitments under AFTA and its own development goals, the RGC has reformed the tariff regime to boost investment. It agreed to reduce tariffs on imported goods from ASEAN members to 0-5% by 2010. Negotiations are on-going for signing FTAs with USA, Australia, India, China.

Cambodia's trade will continue to be shaped by key WTO rules and regional arrangements. The share of exports to the US has continued to increase and reached 68% in 2003, thanks to the quotas granted to Cambodia by the US on garment products under the US-Cambodia textile agreement. With garments and textiles accounting for 99% of exports to the US, the phasing out of quotas in 2005 under the WTO Agreement on Clothing and Textiles will challenge the industry's ability to increase its competitiveness and prevent investors from re-locating their factories outside the country.

Cambodia's accession to the WTO was approved by WTO ministers on 11 September 2003, and the agreed terms were ratified by Cambodia's National Assembly in August 2004. Stated commitments within the WTO framework include the implementation of stringent criteria with regard to privatisation, the elimination of quantitative import restrictions, abstention from dumping, withdrawal of subsidies for favoured investors, export restrictions and other sub-areas.

EU-Cambodia Trade Relations

EU Imports from Cambodia totalled **€419 million** in 2003. Main products were knitted clothing and woven clothing. Main importing countries were Germany, U.K. and France. Exports from the EU countries totalled **€ 79 million** in 2003. Main products were electrical machinery, equipment and parts, pharmaceutical products and mechanical machinery. Main exporting countries were France, Germany and Austria.

In 1999 the EC initialled a “**Textile Trade Agreement with the Royal Government of Cambodia**”. This agreement provides Cambodia with unlimited access to the EU market for Cambodian textiles exports and assures the Cambodian origin of the exported products through a system of agreement and triple-checking for such trade. With Cambodia's entry into ASEAN, the EU has granted to Cambodia the “Regional Cumulation” and Derogation benefits offered by the EU Preferential Rules of Origin. The derogation has been prolonged until the end of 2006. Moreover, since early 2001, Cambodia benefits from the **Everything But Arms** (EBA) initiative, which grants duty-free and quota-free access for all exports (except arms) originating from Cambodia.

3.7 Sustainability of current policies

One of the main challenges for the sustainability of current policies will be to ensure the **continued implementation of structural economic reforms**. Although the Government has declared its commitment to further economic reform measures and strict macro-economic management, there is a risk that the pace of implementation of reforms will be hampered by the lack of institutional capacity, pervasive corruption and the strong links between political and business interests. Discussions regarding a new IMF Poverty Reduction Growth Facility Programme are due to commence with the formation of a new government, which will put pressure on the Government to continue the stabilisation programme.

The success of Cambodia's efforts to alleviate poverty in the rural areas will depend on its ability to **ensure sustained growth** through increased domestic demand, continued export growth and increased foreign investments. The performance of the agricultural sector, which accounts for 40% of GDP will be particularly important as it will influence the consumption capacity of Cambodia's largely rural population. At the same time, sustainable management and use of natural resources remains a challenge for the development of the rural areas.

Cambodia still has one of the worst AIDS epidemics in Asia, even if infection rates are declining. Cambodia has an estimated 169,000 people living with **HIV/AIDS** and there

are already an estimated 49,000 children under 15 years of age orphaned by HIV/AIDS. Factors contributing to the epidemic in Cambodia include poverty, high prevalence of other sexually transmitted diseases, commercial sex, international and domestic migrations and the low social and economic status of women. The AIDS epidemic could potentially de-stabilize current development gains, overloading already stretched health and community services and diminishing national productivity.

The **trafficking of women and girls** is a major problem with an estimated 40,000⁷ trafficked Cambodian women in Thailand alone. The Ministry of Women and Veteran Affairs and the Ministry of Interior are collaborating to promote public awareness, while the role of the police is being strengthened in cross-border operations. Regional initiatives within ASEAN are also being developed. The sustainability of Cambodia's efforts in this field will depend on the success of Cambodia's efforts to alleviate poverty, particularly in the rural areas, as well as continued efforts to improve the legal framework and the judicial system.

The Government is sharing intelligence on **terrorism** with other countries and some donors are providing training to the police and customs authorities. The Government has said that its first priority will be dialogue with the religious sects and indicated intelligence sharing and training as possible areas of collaboration with the EU and other international donors.

3.8 Medium term challenges

Cambodia's development challenges can be grouped under three main themes: reducing the high incidence of poverty, particularly in the rural areas; increasing exports through continued reform of the economic sector; and addressing governance and democratisation.

Poverty and inequity challenges

80% of the poor in Cambodia rely on agriculture related activities for their primary source of income. In addition, the country is presently experiencing the impact of a demographic skew in its population – the baby boom of the mid eighties - that is now producing around 250,000 unemployed youth each year, mainly in rural areas. Therefore, **rural development remains a key issue for addressing poverty in Cambodia.**

It will be necessary to modernise the agricultural sector with appropriate technologies while, at the same time, strengthening the capacities and resources of smallholder farming. Better access and ownership to land, water, and other agricultural inputs need to be achieved. The scale of development required to achieve the economic and social development targets suggests that significant private sector involvement will be needed for rural development, especially with regard to the expansion of agricultural production and agro-processing. Considering the number of areas that need to be addressed, the Government must prepare an integrated framework to guide the direction of

⁷ Ministry of Women and Veteran Affairs Cambodia

rural/agricultural development and reflect more seriously upon the allocation of resources within this framework. An initiative to establish a technical working group in the agricultural sector, involving donors and government, aims to address some of these issues, including better targeting of pro-poor agricultural development.

According to the Participatory Poverty Assessment Report of 2001, most of the poor have low educational attainment. The annual ESSP reviews and other studies highlight that a number of major challenges for **education development** remain. In particular, high drop-out rates in basic education, inequities in access for girls and remote areas and the uncertain quality and standards of education services need to be addressed. The problem of the lack of schools in rural areas is further compounded by teacher shortages in those areas. The increase in enrolment rates have not been matched by a concurrent increase in the number of skilled teachers.

In addition to the focus on achieving the completion of a nine year basic education for all, equitable access to relevant post-basic education and life skills training must be ensured to meet the needs of new labour markets and to improve economic rates of return. While a number of policy measures to implement pro-poor policies have been undertaken, further strengthening of public finance management is needed in terms of the planning, timing and predictability of financial disbursement. In addition, the share of teaching salaries as a proportion of education expenditure has dropped to unsustainably low levels, indicating the urgency of pay reform.

Although considerable effort and progress has been made, the **health** status of the Cambodian population remains one of the lowest in the region. The current incidence of diseases has high economic costs for the country, since it increases the burden on the health care system while reducing the current and future productivity of the population. Given the RGC's relatively low expenditure on the sector, health care is one of the main causes of household indebtedness and impoverishment. Access to services remains low and uneven, with significant provincial variations, resulting in serious health problems for women and children. Substantial physical and financial barriers remain for access to services by the poor. As in the education sector, the wage share of expenditure is too low to be sustainable, and the low level of salaries has been recognised in several studies as one of the most critical factors limiting the effective delivery of health services. Much more attention to behavioural change is required to improve the household health practices of consumers and carers with regards to nutrition, the use of preventive measures and healthy lifestyles.

Economic challenges

Cambodia will face significant challenges in sustaining economic growth at rates exceeding six percent annually and ensuring fiscal sustainability over the medium term. Despite significant progress since 1999, further improvements in **fiscal performance** will be needed over the medium term. In order to improve revenue performance through the collection of tax arrears, the Government will need to ensure that no counter-productive tax exemptions or preferential treatments are given to specific sectors or selected

taxpayers. Contracts with the private sector should be made more transparent and the provisions of contracts need to be properly enforced to ensure that appropriate revenues can be transferred to the state budget. Cash management procedures need to be strengthened through improved cooperation between relevant agencies in order to enable timely and complete disbursements to line Ministries.

Despite impressive efforts in the **trade sector** in preparation for Cambodia's accession to the WTO, a substantial amount of challenges remain. With the expiry of the Multi-Fibre Arrangement for WTO members in 2005, the expected increase in global demand in the garment sector risks being offset by increased competition, particularly from Chinese producers. Customs administration remains an area of serious concern. Porous borders, extensive informal trade resulting in a lack of government revenue and unfair competition with formal traders, low civil service salaries all contribute to the enormous task ahead. In order to attract FDI, the RGC must improve the business environment by ensuring that the trade regime is not anti-export biased, reducing official and un-official tariffs, improving the efficiency of the customs regimes and lowering cross frontier transaction costs.

The programme of reforms prepared by the Government to implement the commitments undertaken to accede to the WTO will provide the first steps towards improving the environment for FDI and trade development. However, the Government will be required to demonstrate a strong political commitment to implement and enforce these new regulations. Vested interests and weak capacity in the Cambodian administration are important obstacles to the success of the trade reform.

An improvement in the implementation and enforcement of **private sector**-related regulations is crucial to Cambodia's ability to attract investments in the private sector. The Government's commitment to increased education and skills training, trade liberalisation and improvements in regional transportation routes could provide new opportunities for agro-processing if efforts are made to ensure the provision of credit to SMEs in rural areas.

Governance and democratisation challenges

Reform of the legal and judicial sector remains one of Cambodia's major policy challenges as it has an impact on all major policy areas. The development of skilled judicial professionals represents a major challenge, as well as appropriate functioning of the courts. **Impunity**, in particular for people in positions of political and economic influence, remains a problem and the majority of Cambodian citizens are neither confident in the judicial system nor can they afford legal representation. Corruption remains widespread, undermining socio-economic development and hampering the development of the private sector. **Juvenile justice** is a real problem, characterised inter alia by the absence of prisons for minors, who are imprisoned with adults, and a lack of rehabilitation centres. Street children are often gathered up by authorities and taken to temporary detention centres.

The Commune Councillors' elections held in 2002 throughout the country were an important step forward in the **decentralisation** process. The participation of the population in the identification of local development needs and relevant responses will lead to more sustainable poverty reduction if a clear and comprehensive legal framework defining the roles, powers and functions of different levels of the decentralised system can be developed. The strengthening of human resources capacity at the commune, provincial and district levels will be crucial in this regard. While decentralisation is a long-term process and concrete local development results will prove significant in the coming years, proper performance monitoring mechanisms are necessary to define improvements, based on lessons learned, and to improve the impact of local development projects on poverty reduction.

4. OVERVIEW OF PAST AND ONGOING EC COOPERATION

4.1 Overview of past and on-going EC co-operation

The European Union has played an integral role in the development of Cambodia since the peace accords were signed in Paris in October 1991. Between 1991 and 1999 some 262 million Euros was provided in EC assistance to Cambodia, while EU Member States have funded bilateral cooperation programmes worth another 590 million Euros. Initial EC assistance programmes sought to facilitate the reintegration of 375,000 former refugees and were mainly implemented through NGOs and international organisations. Following the elections in 1993, the 88 million Euros Rehabilitation Programme for Cambodia (PERC) was initiated. This was a long-term programme that ran from 1994 to 1999, and included several important sub-programmes, including PRASAC I (Programme de Réhabilitation et d'Appui au Secteur Agricole du Cambodge) for rural development, PASEC I (Programme d'Appui au Secteur Education du Cambodge) for primary education, together with institutional support and human rights projects.

Despite the political instability of 1997, the Commission supported the continued implementation of programmes that were having an impact on the local populations – particularly those pertaining to rural development, education, de-mining and humanitarian aid. This unsettled period came to an end with the national elections in July 1998. On 1 November 1999 the EC-Cambodia Cooperation Agreement entered into force, reaffirming both parties' long-term commitment to cooperation. The Agreement focuses on trade, economic and development cooperation, while recognising the 'essential elements' of democratic principles and human rights.

The first EC-Cambodia Country Strategy Paper (CSP), covering the years 2000-2003, established poverty reduction as the overriding focus of EC aid interventions. Priority areas of intervention included rural support, primary education and training, health, humanitarian actions, mine clearance, support to the reform of the public administration and military as well as activities in support of human rights and consolidation of democracy. The possibility of an EC intervention in the environment sector was also examined but did not materialise in the end.

The first National Indicative Programme (NIP), for 2002-2004, identified actions in the sectors of rural development, the social sector - education and health - and trade. Governance and democratisation were identified as cross-cutting themes. Issues such as human resource development, gender and environment have since been mainstreamed into all EC development programmes.

4.2 Degree of implementation of the NIP 2002-2004

From the NIP 2002-2004 three main activities, amounting to approximately €40 million, remain to be committed in 2004. Progress of the actions under implementation (notably support to basic education and WTO support) has been positive, however, it is too early to draw any conclusions for other actions implemented from the NIP 2002-2004.

Area of co-operation	2002	2003	2004	TOTAL 2002-2004
	€M	€M	€M	€M
1: Support to Rural Development				30
ECOSORN			25	
Support to the livestock sector		5		
2: Support to the Social Sector				25
Support to the Basic Education Sector	20			
Health			5	
3: Trade Sector Development				3
EC support to Cambodia's WTO accession	2			
Participation in the EC/ASEAN IPR programme		0,5		
EC-Cambodia Project on Standards, Quality and Conformity Assessment			0,5	
Cross Cutting Issue: Governance		0,9		10,7
Support to the decentralisation process			9,8	
Total				68,7

It is anticipated that all funds under the NIP 2002-2004 will be committed by the end of 2004 with implementation commencing late 2004 or early 2005.

4.3 Lessons learned from previous EC programmes in Cambodia

Based on evaluation reports of individual projects/programmes and the Government response, some general conclusions can be drawn on the implementation of EC-funded projects in Cambodia. The projects are perceived as fully relevant to the country situation and to the existing Cooperation Agreement. Ongoing projects are considered to be making good progress, taking account of the realities of Cambodia's situation as a country in transition. With improved national ownership of the development agenda and improved donor co-ordination, sector-wide co-operation has increased, particularly in the social sectors.

The main EC programmes in *rural development* have clearly demonstrated a positive and significant impact. Agricultural extension activities that include new growing methods, integrated pest management, crop diversification, support to livestock and support to the development of producer association have demonstrated positive and sustainable benefits to the local population. Rural water supply and sanitation continue to be a priority in all

provinces of Cambodia and has been targeted successfully both in humanitarian as well as rural development programmes. However, experience has shown that constraints to access to land due to UXO and landmine contamination is better addressed from a rural development perspective, rather than a purely humanitarian response as they can be major obstacles to the implementation of rural development programmes.

Large-scale infrastructure is needed for the development of rural Cambodia. However, issues of ownership and maintenance dictate that primary and secondary rural roads and large-scale irrigation are better constructed by the government under loan agreements rather than using grant aid which could be more directly targeted for poverty alleviation.

Lessons have been learnt regarding the formation of future intervention strategies. As the situation in many parts of Cambodia has moved from emergency relief and food security towards sustainable development, a major problem emerging in rural areas is the lack of both on and off-farm employment opportunities. Future interventions should work towards the development of employment opportunities in agribusiness, including fisheries, livestock, and forestry.

Commission support to the *education* sector has covered areas such as support to primary education, construction and rehabilitation of primary schools, development of life skills training at basic education levels and vocational training. Later Commission programmes have been instrumental in supporting MoEYS reforms, in particular the planning and implementation of the Priority Action Programmes, capacity building in budget management at provincial/district/schools levels, and the new MoEYS approach to school governance.

The principal lessons learned from the EC's past support to the education sector underscore the importance of (1) ensuring a close alignment with government policy; (2) nation-wide support, covering reforms and capacity building, and (3) dispersing support in a manner such that it strengthens provinces, districts and communes as well as the central level.

In response to the MoEYS sector-wide and policy-driven reforms and to financial reforms in the Ministry of Economy and Finance (MoEF), the EC designed a new programme in 2002 to support MoEYS's priority policies and action programmes in the Education Strategic Plan/Education Sector Support Programme. These sought to promote equitable access to, and completion of, quality basic education and non-formal education, with special attention to girls and the most vulnerable. The current EC programme consists of a sectoral budget support combined with institutional support and technical assistance to strengthen policy planning and management in education and to support the development of financial and accounting management and audit systems in education. Results have so far been positive and first EC Independent Technical Monitoring Mission recommended that the EC consider broadening its support to other Priority Action Programmes which have a direct impact on the quality and efficiency of basic education.

EC support to the *health* sector has focussed on support in the field of malaria control, sexually transmitted diseases and reproductive health. In addition, the Commission has supported a substantial number of NGO projects in the health sector. Previous evaluations of EC-supported activities in the health sector noted that although considerable sums had been spent, limited sustainable impact was noted. In the absence of a national framework for the health sector, the large number of projects with different implementation, monitoring and evaluation procedures also created an obstacle to the development of local capacity. As recognised by the Health Sector Strategic Plan, the vertical approach of many disease control programmes has not spread benefits throughout the system. Focusing on a single health problem has resulted in missed opportunities for addressing health problems of a similar nature within the same target group.

A programming mission reviewing EC support to the health sector undertaken in 2001 concluded that, while continued support to the MoH's development of a comprehensive national policy could serve as a basis for a sector-wide approach, a complementary EC action targeting disease prevention and health education would have a critical and sustainable impact on the health status of the population. Implementation of this action, identified in the NIP 2002-2004, will commence in 2005.

In the field of *governance and democratisation*, the EC has funded projects promoting human rights awareness and empowerment of civil society, the legal protection of children through the European Initiative for Democracy and Human Rights (EIDHR), as well as institutional support and capacity building programmes aimed at the development of sustainable democratic structures. The EC is in particular, but not exclusively, supporting the decentralisation and deconcentration process to improve local democratic participatory mechanisms and local governance, and to enhance the service providers' function of the Commune Councils for appropriate local development activities. A €10 million programme in support of the decentralisation process, identified in the NIP 2002-2004, is to be committed in 2004.

The Commission has supported electoral processes in Cambodia since the holding of the National Assembly elections in 1998. EC assistance has included support to the organisation of the elections, voter education activities, media access, and the deployment of Election Observation Missions. Since the costs for the organisation of the elections have increasingly been borne by the Cambodian authorities, the Commission has shifted to providing targeted technical assistance to the National Election Committee, following recommendations from the EU Election Observation Missions.

The assessment of the electoral processes by EU Election Observation Missions in 1998, 2002 and 2003 showed an increase in the technical capacity of the national institutions responsible for the electoral process. The atmosphere during the election period was less tense and the number of violent incidents declined. It is clear that the presence of international observers, the majority of whom are from the EU, has contributed to this development.

The question of the **Commission's capacity to implement programmes** in an efficient manner is crucial. Project development, management and implementation has improved in recent years with the creation of the new EuropeAid Cooperation Office, the opening of the Delegation of the European Commission in Phnom Penh, and with the deconcentration of the external service. The devolution of project management to the EC Delegation has improved financial management as well as management of project implementation as an increased number of implementation decisions can be taken locally, thereby reducing risk of delays.

Experiences from the implementation of previous EC assistance has shown that progress often has been hampered due to the lack of a sector programme, prepared by the government and agreed with donors. In addition, best results have been noted in sectors where both the government and donors have been committed to allocate human resources/capacity to follow up on the sector programmes through discussions on policy and implementation issues in the sectoral working groups. The EC strategy proposed herewith will therefore concentrate on fewer priority sectors (and within these sectors a limited number of programmes) to increase EC expertise and know-how in focal sectors, leading to higher quality and better coordinated projects. Additional EC Technical Assistance in support of the development and implementation of sectoral programmes will be considered, if needed.

Difficulties in preparation of new projects/programmes have been experienced due to changes introduced with the new Financial Regulation, resulting in delays in the finalisation of some project proposals. Delays have also been experienced as regards the agreement on additional posts to the Phnom Penh Delegation, resulting in an imbalance between workload and human resources. These problems have now largely been addressed.

4.4 Programmes of EU Member States and other donors

According to OECD-DAC, in the year 2001, total ODA disbursements to Cambodia from the Commission and EU Member States amounted to US\$ 112.5 million, which represented close to 28% of the total ODA (grants and loans) during that year. In terms of total EU aid disbursements, the EU is the second largest donor in Cambodia, after Japan (with US\$ 120 million in 2001).⁸

4.4.1 EU Member State programmes

EU Member States active in Cambodia include Belgium, Denmark, France, Germany, Sweden and the UK. They support programmes in the areas of education, health, rural development, decentralisation and deconcentration, legal and judicial reform, trade and private sector development.

⁸ Details of aid disbursements and commitments to Cambodia, according to the OECD/DAC classifications, can be found in annex 9.

Belgium supports basic education, teacher training and the provision of health services in three provinces. In addition, it funds rural development projects targeting rural livelihoods. **Denmark** is funding NGO projects on human rights and it supports the Danish Institute for Human Rights in its activities to develop the Legal and Judicial Reform Strategy. **France** is a donor for HIV/AIDS projects, supports higher education institutions and is involved in institutional strengthening and development programmes in the legal, health and administrative sectors. It is also active in the field of rural development and trade sector reform. In addition, France funds NGO projects on human rights. **Germany** is also a donor to a large variety of projects. In the educational field, it supports vocational and small enterprise-type training. In the health sector, Germany's focus is on health sector reform and reproductive health. Administrative and trade sector reform, as well as rural development and SME promotion are other areas of attention. **Sweden** is mainly supporting the UNICEF Expanded Basic Education Programme, decentralisation of government and NGO projects on human rights. The **UK** firstly co-funds education and health sector projects of the World Bank and the ADB. Secondly, institutional development and safe motherhood are being supported. The UK also supports a government programme on decentralised governance and some activities targeting rural livelihoods. Another focus is NGO projects on human rights, and a last area of attention is trade sector reform.

4.4.2 Other donors

Japan is by far the most important bilateral donor to Cambodia. Its priority areas include good governance (administrative, financial and judicial reforms), economic promotion, infrastructure improvement, enhanced food and agricultural production, education and human resource development, health and natural resource management. Another significant bilateral donor is **Australia**. The Australians currently support demining, governance, research and development, and legal and judicial reform. They also intend to assist in the field of WTO capacity, SPS and economic governance, and to provide assistance in linking agriculture to trade. Projects funded by **Canada** include demining, support for legislative and administrative reform, and assistance with the drafting of the Commercial Court law and regulations and the setting up of a Commercial Arbitration Centre. **New Zealand** and **Norway** are small but active donors. In the trade sector, New Zealand provides assistance in SPS, legal metrology and custom evaluation, and Norway channels funds through UNIDO in the areas of market access, trade facilitation and standards. Relating to private sector development, New Zealand is preparing a small intervention in agricultural diversification and technology.

The leading international organisations working in Cambodia are the UN agencies (UNDP, UNFPA, UNICEF, UNIDO and UNCTAD), the World Bank, ADB, IMF and IFC.

UNDP's activities for the period 2001-2005 concentrate on the strengthening of governing institutions, poverty reduction and monitoring and the management of natural resources. UNDP also supports demining and is involved in trade and investment facilitation. UNDP has earmarked close to US\$ 45.5 million in its Country Cooperation

Framework for 2001-2005. Of the other UN agencies, **UNESCO** supports the education and health sectors, **UNIDO** works in the areas of market access, trade facilitation and standards, and **UNCTAD** is providing assistance on WTO accession and training on multilateral trade negotiations, as well as completing a programme on E-business for SMEs.

The **World Bank** prioritises five types of activities in Cambodia: supporting good governance (1), building physical infrastructure (2), rebuilding human capital (3), facilitating private sector development (4), and demobilising and reintegrating soldiers (5). Some of its core projects/activities at present include support to the forestry sector, governance, legal and judicial reform, demining, trade facilitation and implementation of WTO requirements, and assistance with the development of the RGC's Private Sector Growth Strategy. Over the years the Cambodian government has borrowed a total of US\$ 657.20 million and has received more than US\$ 15 million in grants from the World Bank.

The **Asian Development Bank's** strategy for Cambodia has two prime foci: economic growth and poverty reduction. ADB's activities firstly support broad-based rural development through the promotion of water resource management, decentralisation, natural resource management, and agriculture sector reform. ADB also assists human and social development, via sector-wide initiatives in education and health and complementary support in water supply. A third area of activities is private sector development, mainly through the development of a national road network. Furthermore, gender and governance in economic planning, public finance and legal reform receive continuous attention. Cumulative ADB lending to Cambodia as of 31 December 2003 was US\$775.3 million. 112 technical assistance projects (grant) have been approved with a total value of \$72.9 million as of 31 December 2003.

IMF and **ITC** have supporting roles in the areas of trade and private sector development.

4.4.3 Donor coordination

Cambodia is highly dependent on donor aid, (with external financing reportedly accounting for 49% of expenditures in 2001). Following recent events in Afghanistan and Iraq, donors have been under pressure to reduce commitments to Cambodia. Under these circumstances, there is a need for the Government to achieve agreed benchmarks, for more effective donor-government dialogue and for better coordination between donors. The RGC at the June 2002 Consultative Group meeting proposed the formation of a Government–Donor Partnership Working Group under the CG mechanism to build more effective development mechanisms with Cambodia's external partners. The Working Group and three sub-Working Groups are presently monitoring the preparation of three studies, and the findings will be presented to the next CG Meeting (2004).

Under discussion are the creation of:

- at policy level, "Government-Donor Coordination Committee" (GDCC) to be chaired or co-chaired by Government and whose membership will include key

Senior Ministers and Ministers and the heads of mission of diplomatic and multilateral institutions of Cambodia's development partners.

- at operational level, 17 "Joint Government-Donor Technical Working Groups" whose members will include senior sectoral professional/technical staff of concerned Government institutions, and bilateral and multilateral partners.

Several EU Member States have bilateral co-operation programmes with Cambodia. Co-ordination between the EC and Member States is ensured via the ALA Committee, via the EC Delegation in Phnom Penh and through the donor co-ordination working groups. The EC Country Strategy and the National Indicative Programme, as well as individual projects/programmes, are discussed with EU Member States and other donors during their preparation. The Commission is also participating in the working groups established under the CG mechanism and specific working groups following the implementation of sector-wide programmes. The Commission has been particularly pro-active in the working group on the implementation of the education sector programme, lending its support to the move towards a sector-wide approach. Based on the positive experiences in the education sector, it is foreseen that the Commission will take a similar pro-active approach in the other focal areas for support, health and pro-poor economic development (including both rural development and trade).

5. RESPONSE STRATEGY

5.1 Principles and objectives for co-operation

Co-operation with Cambodia follows the broad objectives of Community Development co-operation policy, defined in the Commission's Communication of April 2000 and the Declaration of the Development Council of November 2000. These documents affirm that the strategic areas for EC action are sustainable development, the social sectors, integration into the world economy, fight against poverty, democracy, human rights and the rule of law.

Account must also be taken of the various mechanisms available to the Commission for this response including the European Union's external policy actions (CFSP, conflict prevention, ECHO humanitarian aid operations, and NGO funded activities including food security and targeted health and education initiatives).

The principles and objectives outlined in this CSP are in full accordance with EU policy guidelines and remain largely unchanged from the previous CSP and NIP.

5.2 Priorities for co-operation

The priorities for co-operation have been jointly defined on the basis of the following criteria:

- Response to the medium term challenges facing Cambodia;

- Relevance to the overarching goal of poverty reduction;
- Convergence with the key priorities of the RGC, expressed in the SEDPII and NPRS;
- Complementarity with other donors and with EU Member States in particular;
- Lessons learned and acquired know-how in specific sectors, based on experience from previous EC co-operation programmes;
- EC and RGC capacity to manage and monitor programmes;
- Level of commitment to structured sector policy dialogue and capacity within relevant line Ministries;
- Existence of agreed sector plans and commitment to move to a sector-wide approach.

Based on the above-mentioned criteria, and with the aim of focusing on a limited amount of priority sectors, several sectors which could merit EC support, one notable example is the legal sector where the EC has very limited previous experience in Cambodia, have not been included among the focal sectors.

Taking these aspects into account, the overarching goal of EC-Cambodia co-operation is to target poverty reduction in rural areas. **Pro-poor economic development**, taking into account relevant economic sectors that have a bearing on rural areas, including trade, will thus remain the first focal area for EC support. As outlined in previous sections, poverty alleviation in the rural areas is closely linked with development in the **social sectors**, health and education, making this the second focal area for EC support.

Crosscutting and complementary themes to the focal sectors are related governance and democratisation issues.

Human resource development will form an integral part of all EC development programmes, as will environment and gender issues. In addition to the pre-requisite to undertake Environmental Impact Assessments, particular attention will be given to ensuring that environment-friendly practises are promoted in rural development and rural enterprise development activities. Participation of women in all EC programmes will also be actively promoted. As regards gender issues, women and children also form a particular focus for Cambodia under the EIDHR (see 5.2.3)

The implementation of EC cooperation activities in Cambodia will be complemented by an increased focus on policy dialogue with the government and other key donors through the sectoral working groups established by the government and through regular meetings between Commission representatives, from EC headquarters and the EC Delegation, and different Ministries. Such a dialogue will facilitate the establishment of jointly agreed goals and assessment indicators, resulting in better targeted assistance programmes. As is already the case in the education sector, the Commission will continue to liaise with other donors in order to support the RGC's move towards SWAPs in identified focal sectors.

5.2.1 Pro-poor economic development

The Commission is one of the main actors supporting rural development in Cambodia. Whereas previous EC support focused heavily on the agricultural sector, as the situation in Cambodia has moved from rehabilitation to sustainable development, the lack of on and off-farm employment opportunity in rural areas has been identified as a major problem. Based on its long experience in the sector, the Commission is well placed to take a leading role, together with main actors such as the ADB and the World Bank, in pushing for greater coordination between line ministries involved in the rural development sector as well as among donors in general. The Commission is also well placed to provide trade related technical assistance, thereby linking trade possibilities to development issues.

- The EC-Cambodia Pro-poor Economic Development strategy focuses on rural livelihoods. While development of agriculture is emphasised - particularly as regards small-scale irrigation, crop diversification and improved technologies - attention will also be given to the development of local SMEs.

This is fully in line with the priorities in the NPRS, which defines the agricultural sector as the engine of growth for the country, both for exports and for consumption internally, and highlights the need for diversification of the agricultural production and value added opportunity through the development of agro-business. The SEDP II plans to foster broad based economic growth with equity, with the private sector playing the lead role.

- Trade policy priorities have been incorporated into the NPRS and the Government is currently undertaking a revision of the diagnostic trade integration and competitiveness study (DTIS), prepared under the Integrated Framework. The revision will update the framework for Trade Related Technical Assistance (TRTA) and it will also assess the possibility to use a SWAP approach for delivering TRTA.
- In addition to targeted support to activities identified in the DTIS, the Commission is implementing a trade action plan with Southeast Asia, the Trans-Regional EU-ASEAN Trade Initiative (TREATI), comprising dialogue and joint activities with the goal of facilitating trade and investment flows. Indicated priority areas include customs co-operation, technical barriers to trade, investment and SPS matters.
- The EC pro-poor economic development response strategy will be complementary to the activities of other donors. The EC will involve other donors in the identification and design of its cooperation programmes and will actively promote the setting up of more effective coordination mechanisms between donors and Government Ministries involved in both agriculture and trade reform/private sector development.

5.2.2 Social sector response strategy

The added value of EC support to the social sectors is represented by the solid EC experience both as regards support to health and education programmes in general, as well as its particular experience in education and health sectors in Cambodia. In addition, recently established sector plans provide a good basis for move towards a sector-wide approach, with increased attention to policy discussions between the RGC and donors, which is fully in line with EC priorities. The continued EC support to the sectors will give an additional support to the social ministries in achieving these aims.

Education

As highlighted in the National Poverty Reduction Strategy, education is one of the key determinants of Cambodian society's future economic and social development. Over the last years, the Royal Government of Cambodia (RGC) has shown an increasingly genuine commitment to pro-poor reforms in social sectors. The Ministry of Education, Youth and Sports (MoEYS) has been selected as a pilot Ministry, together with the Ministry of Health, for implementing the Government budget reforms and to develop new partnerships with donors. In close consultation with donors and the civil society, MoEYS has developed its own sector policy encompassing key reforms to assure equitable access, quality improvement, management and financing of education at all levels, with particular attention to pro-poor and gender responsive policies.

- MoEYS sector-wide and policy-driven reforms have led to significant progress in sector performance, including improved access to basic education and improved effectiveness of education resource management. The EC is one of the lead donors in the field of basic education and is playing a key role in the move towards a Sector Wide Approach. The performance-based mechanism established for the release of the EC budget support is already encouraging the Government to pursue the reforms that are essential for switching to modern sector-based management of education.
- The EC response strategy is therefore to continue and enhance its support to the MoEYS for implementing ESP/ESSP strategies and producing desired policy outcomes, within the long-term objectives of the EFA plan.
- This will be done, depending on progress, through increased support to Priority Action Programmes having a direct impact on the quality and efficiency of basic education, including those strategies which address continuous teacher development and education service efficiency, scholarships and incentives for equitable access and sustainable provision of core instructional materials.

Health

Poor health is the major cause of impoverishment and other forms of social deprivation, such as loss of educational and employment opportunities, and seriously undermines the

country's economic and social development. To respond to these challenges and support the National Poverty Reduction Strategy and the Millennium Development Goals, the Ministry of Health has designed, in collaboration with all stakeholders, the Health Sector Strategic Plan 2003-2007, which for the first time provides an agreed sector-wide strategic framework to guide the use of domestic and external resources to the sector. The MoH has also developed a Sector Wide Management (SWiM) approach, which facilitates a coordinated implementation and monitoring of the strategic plan.

- The programming mission undertaken in 2001 concluded that in the absence of an agreed sector-wide plan for the health sector, EC support should be directed towards supporting the SWiM process, but to develop an interim programme focused on capacity-building in a key sub-sector. Although the Health Sector Strategic Plan has been agreed in the meantime, discussions with the MoH and other donors active in the sector have led to the conclusion that this strategy remains valid.
- The EC therefore identified, in the NIP 2002-2004, a five-year project that will specifically support MoH in implementing its strategies for Behavioural Change Communication identified as one of the priority areas of the Health Sector Strategic Plan. Under a joint co-financing arrangement with UNICEF, the project will improve the capacity of health providers nationwide to deliver effective behavioural change communication for better health-seeking behaviour and healthier lifestyles. This initiative is consistent with, and supports, the Sector-Wide Management (SWiM) approach adopted by the MoH.
- By supporting implementation of a key component of the Health Sector Strategic Plan and by following closely broader health reforms addressed through the multi-donor Health Sector Support Project, the EC will be able to encourage the MoH in its move towards a Sector Wide Approach.

5.2.3 Coherence and complementarity with EU policies

Coherence with EC/EU policies

A key objective of EC action in Cambodia is to support the country's move from a state of conflict to sustained peace through reconstruction and stabilisation activities, using all budgetary instruments available. The anchoring of democracy in Cambodia through assistance to elections, decentralisation and conflict resolution should thus continue to be a priority. Food security is another area of concern, and activities under the thematic budget line will be complemented by programmed actions aimed at removing obstacles to food production and trade through the strengthening of institutional and legal frameworks.⁹

⁹ On-going and planned activities include support to the decentralisation process, conflict resolution activities under the European Initiative for Democracy and Human Rights and the EU Joint Action on Small Arms, actions addressing trade infrastructure, customs procedures and regulations, tariff and non-tariff barriers and support to the development of NGO's in the agro-business.

Governance and democratisation issues

The Joint Declaration of the Council and the Commission on the Community's development policy (November 2000), identifies the sustainable establishment and functioning of democratic institutions, ruled by good governance principles, including the rule of law, as a major area of concentration for Community action. To reduce the fiduciary risk to public funds and to facilitate the use of budget support, the EC will support priority reforms aimed at improving the country's public expenditure and financial management systems.

Social sector support

In their Joint Statement of November 2000, the Commission and the Council affirmed that equitable access to social services, i.e. health and education services, is a vital dimension of poverty reduction. EU policies also state that a SWAP should be pursued and promoted in health and education as foreseen in the CSP.

The Education Sector Programme, supported by the EC is fully in accordance with EC commitments made in the Dakar Forum in April 2000 and the Millennium Development Goals (MDG) for education. EC support to the health sector is also in line with the MDG for health and with EC policies on health, AIDS and population.

Rural development

The response strategy in this sector is in line with the objective of the EC rural development policy to achieve a sustainable reduction in rural poverty. With a focus on the agricultural sector, including support to the development of the agro-business and market links, the EC strategy is coherent with the EU policies for both rural development and private sector development.

Complementarity with other EC budgetary instruments

Cambodia is a focus country under the European Initiative for Democracy and Human Rights (EIDHR) 2002-2004. Areas identified for EC actions include: 1) **promotion of human rights**; 2) **conflict prevention and resolution**, aimed at developing early warning, mediation, reconciliation and confidence-building mechanisms at local level; 3) **strengthening the legal system**, with the aim of improving possibilities for victims of human rights abuses and other vulnerable groups to receive support through the provision of legal or para-legal assistance, protection and facilitating rehabilitation of victims of serious human rights abuses (trafficking in human beings, land grabbing, labour rights) and of **vulnerable groups (women, children, prisoners)**. These areas are coherent with EU policies and in line with the areas of concern established in the CSP, such as the shortcomings of the judicial system and trafficking in human beings.

Support for the Khmer Rouge Tribunal is also considered under applicable budgetary instruments.

In 2000, **ECHO** launched a global plan, intending to phase out of areas where humanitarian needs were already met. However pockets of extreme vulnerability persist, obliging ECHO to adopt a differentiated approach so that extreme humanitarian situations would still be addressed as needed. ECHO's interim report on the global plan 2000, the ECOSORN report of RELEX as well as ECHO's field assessments describe some areas where ECHO intervention is still justified such as the north-west provinces of Oddar Meanchey, Prey Vohar and Banteay Meanchey and the north-east provinces of RatanaKiri, MondulKiri, and Stung Treng. Interventions in 2003 have mainly been in the areas of basic health, water supply and hygiene.

The EC is one of the main contributors to the Global Fund to Fight AIDS, TB and Malaria. Implementation of programmes in Cambodia in all three areas of intervention is on-going.

Under the CSP 2004-2006, in accordance with applicable procedures and subject to availability of funds, Cambodia is also eligible for support under other EC horizontal budget lines, including in particular the following:

- 21 02: Food aid/Food security and support operations
- B7-210: ECHO
- 21 02 05: Environment in the developing countries and tropical forests
- 19 02 04: Community participation in action concerning anti-personnel mines
- 21 02 03: Co-financing with European NGOs, operations in developing countries
- 21 02 13: Decentralised co-operation
- 21 02 07 02: Aid for poverty-related diseases (HIV/AIDS, malaria and tuberculosis) in developing countries
- 21 02 07 03: Aid for population and reproductive health care
- 19 04 03: European Initiative for Democracy and Human Rights
- 19 04 04: Support for activities of the International Criminal Tribunals and setting up of the ICC

Complementarity with EU Member States Programmes

As has been illustrated in previous sections of the CSP, the focal sectors for EC cooperation with Cambodia are complementary to the strategies of EU Member States. Consultations with EU Member States confirm that rural development, with a particular focus on the creation of market opportunities, is viewed as a key area to be addressed by the EC and EU Member States. Education and health have also been identified as focal sectors and there is a strong wish, among several EU Member States active in these sectors, to support the RGC's move towards SWAPs in those sectors, possibly through pooled funding, or budget support.

Coordination between the Commission and EU Member States ahead of Consultative Groups meetings, to enable joint statements and pledges, will be increased. The Commission also intends to look at additional “harmonisation activities” such as those successfully undertaken in, for example, Vietnam.

Complementarity with other donors

Donors and NGOs have been consulted during the preparation of the EC-Cambodia CSP. The EC response strategy is fully in line with the RGC sectoral development plans identified in the NPRS and endorsed by donors. Depending on the progress in the focal sectors, EC interventions will be coordinated in the sectoral donor-government working groups or with a few key donors. Supporting the EC aim to move towards a sector wide approach where appropriate conditions exist, technical assistance will be considered to assist the RGC with the preparation of sectoral frameworks or plans.