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Cambodia-China Free Trade Agreement: A Cambodian Perspective

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China and Cambodia signed a free trade agreement (FTA) in Phnom Penh on 12 October 2020, with Cambodian Prime Minister Hun Sen and the then Chinese State Councilor and Foreign Minister Wang Yi attending the signing ceremony. Source: Modern China/Facebook.

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EXECUTIVE SUMMARY

- The Cambodia-China Free Trade Agreement (CCFTA), which came into force in January 2022, has provided Cambodia with renewed impetus to enhance trade facilitation and expand its trade portfolio. This is in line with the objectives of its Rectangular Strategy (2018-2023) and the economic diplomacy initiative that it launched in January 2021.
- Cambodia has been striving to mitigate economic and political risks stemming from the economic sanctions and pressures from the European Union and the United States by deepening its engagement with China.
- Cambodia stands to gain significantly in exporting its agricultural products to China under the CCFTA. The potential for growth in that area is massive. Cambodia's tariff reduction and elimination offer is 90%, while China's is 97.53%.
- To make the most of the opportunities provided by the CCFTA, Cambodia requires assistance in terms of improving sanitary and phytosanitary measures, conducting research and development to improve its export capacity and competitiveness, and establishing public-private partnerships to facilitate trade.

INTRODUCTION

The CCFTA, signed in October 2020 and effective since January 2022, was rapidly negotiated in just eight months amid the COVID-19 pandemic. Cambodia initiated the agreement with the aim of broadening its trade relations and export markets in China in response to the economic fallout caused by the pandemic, local flooding, and economic pressures and sanctions from the European Union and the United States. The year 2020 was a challenging period for the country.¹ Cambodia's economy contracted by 3.1% in 2020, before rebounding by 3.0% in 2021 and 5.1% in 2022. Economic growth is expected to reach 6.2% in 2023. This paper aims to shed light on the driving forces and key content of the CCFTA and its implications on Cambodia's economic diplomacy.

TRADE PRESSURES ON CAMBODIA

Cambodia's economic policies are relatively liberal for the region, and its investment and trade regimes remain attractive. However, being a small and open economy, Cambodia is susceptible to external changes and shocks. Global trade growth slowed in the second half of 2022 and further deceleration is projected for 2023. With the global growth outlook appearing gloomy, Cambodia's economy is facing various challenges. The manufacturing sector – particularly the garment industry – is heavily reliant on export markets, and the economic slowdown in Cambodia's two primary markets, the United States and Europe, has impacted it badly.²

As a country classified as a least developed country (LDC), Cambodia has received several Generalised System of Preferences (GSP) programmes that have provided benefits. Due to the duty-free market access that Cambodia has been granted to various export markets via different trade preference programmes,³ Cambodia's trade volume nearly doubled between 2017 and 2021, increasing from US\$25.44 billion to US\$48.01 billion. However, due to concerns over human rights and democracy issues in Cambodia, the European Union (EU) reduced approximately 20% of its "Everything but Arms" preferences for Cambodia in August 2020. The United States also suspended its GSP preferences, imposing various economic sanctions on Cambodia, including the "Cambodia Democracy Act" bill, the Magnitsky Act targeting several senior Cambodian leaders, and sanctions on the Union Development Group, a Chinese company operating in Cambodia. These sanctions and suspensions have negatively impacted Cambodia's trade with the world.

Furthermore, Cambodia's export potential to regional markets is limited. Only a small portion of total exports go to such markets, and the country's businesses are as yet not adequately integrated into regional value chains.⁴

Along with the reduction in GSP preferences by the US and EU, Cambodia's trade activities require optimisation and streamlining. According to the UN's evaluation in 2021, Cambodia received a score of 78.5% for its trade facilitation, with identified weaknesses being in paperless trade and cross-border paperless trade. Cambodia has not yet implemented an

authorised economic operator (AEO) system to streamline cross-border trade. Moreover, the statistics database management system of the General Department of Customs and Excise does not generate timely and precise statistics.⁵ Thus, under such dire conditions, the CCFTA is expected to stimulate increased diversification and facilitation of trade, as well as improve institutions and capacity-building for trade promotion and facilitation. From a geopolitical perspective, Cambodia apparently intends to use its relationship with China to mitigate the impact of the economic sanctions imposed by the EU and the US.⁶

Despite the challenges posed by the pandemic, China and Cambodia managed to exceed their bilateral trade volume target by reaching \$11.1 billion in 2021, achieving the \$10 billion goal two years ahead of schedule. In 2022, China was Cambodia's largest export market, with exports totalling US\$1.24 billion, representing 5.5% of Cambodia's total exports. During the same period, Cambodia's imports from China amounted to US\$10.4 billion, accounting for roughly 34.1% of Cambodia's total imports. The main products that Cambodia exported to China included milled rice, bananas, mangos, cassava, fishery products, and apparel. Cambodia's imports from China mainly consisted of raw materials for the garment industry, machinery, vehicles, foodstuffs, electronics, and medicines.⁷

The negotiation of the China-Cambodia Free Trade Agreement (CCFTA) was completed relatively quickly, taking only eight months to finalise. The first round of negotiations took place in January 2020, with both sides engaging in significant discussions on trade in goods, customs procedures, trade facilitation, rules of origin, trade in services, transparency, economic and technical cooperation, cooperation under the Belt and Road Initiative, e-commerce, and related legal matters. The second round of negotiations took place virtually in April 2020, and both sides reached a broad consensus on the agreement's content, finalising consultations on cooperation in investment within the Belt and Road Initiative, e-commerce, economic and technological cooperation, and legal issues. The negotiations were concluded in July 2020, and the agreement was signed in October 2020 and went into effect in January 2022. Notably, 2020 marked the 10th anniversary of the signing of the Comprehensive Strategic Partnership between China and Cambodia, and this prompted both countries' leaders to direct their FTA negotiators to conclude the negotiations that year.

KEY CONTENTS OF THE AGREEMENT

The CCFTA encompasses 16 chapters that cover various aspects of trade and economic cooperation.⁸ The agreement is expected to bring benefits to Cambodia such as increased market access to China for agricultural products, improved efficiency in the application of rules of origin, strengthened customs and trade facilitation, and more investment opportunities.⁹

Cambodia and China have agreed to a tariff reduction and elimination scheme under the CCFTA. Cambodia will offer a 90% reduction and elimination of tariffs, while China will offer a 97.53% reduction and elimination of tariffs. Compared to the ASEAN-China FTA, China increased its tariff reduction and elimination rate by 3.16% under the CCFTA. The tariff reduction and elimination scheme are divided into four categories: Category A, which includes 8,328 tariff lines that enjoy zero tariffs; Category B, which will enjoy zero tariffs after five years; Category C, which will enjoy tariffs after 10 years; and Category D, which will enjoy

tariffs after 20 years. The products included in Category A are pepper, mango, banana, longan, dragon fruit, cashew nuts, fish, meat, processed meat, honey, vegetables, grains, processed foods, alcohol, beverages, vinegar, textiles, footwear, electronic parts, bicycles, cables, engines and electronic motors.

Transparency

The measures outlined in the CCFTA to promote transparency in customs procedures and trade policies will help to facilitate cross-border trade, and align Cambodia's trade facilitation measures with international best practices. The publication of laws, regulations, and administrative procedures relevant to trade-in goods and services, as well as the designation of enquiry points to address questions from interested persons, will also help to promote transparency and ensure that businesses have access to the information they need. This will be particularly important for small and medium-sized enterprises (SMEs), which may not have the resources to navigate complex trade regulations and procedures. Overall, the measures outlined in the CCFTA to promote transparency will help to create a more open, predictable, and efficient trading environment for businesses in Cambodia and China.

Sanitary and Phytosanitary

Low sanitary and phytosanitary standards (SPS) are the main barriers for Cambodia's export, especially of agricultural goods.¹⁰ The study by the United Nations Conference on Trade and Development (UNCTAD) in 2019 found that the main obstacles to entering the Chinese market are tariffs and SPS requirements. In the context of the World Trade Organisation (WTO), the SPS Committee was established to provide a forum for discussion and exchange of information.¹¹ Under the framework of CCFTA, Cambodia and China agree to explore further cooperation opportunities on sanitary and phytosanitary issues and facilitating bilateral trade. This is a positive development as sanitary and phytosanitary measures are critical in ensuring the safety and quality of agricultural products traded between countries. Cooperation in this area can help reduce trade barriers and increase market access for Cambodian agricultural products to China. The establishment of a committee on sanitary and phytosanitary measures shows the commitment of both countries to enhancing mutual understanding and technical cooperation on this issue. It also provides a mechanism for monitoring the implementation and operation of these measures.

Cooperation on the Belt and Road Initiative

This is a special cooperation agreement under the framework of FTA. Cambodia has embraced the China-proposed Belt and Road Initiative since its inception.¹² Under the CCFTA, Cambodia and China agree to strengthen the role of the Belt and Road Initiative as an important instrument and further strengthen high-quality Belt and Road cooperation by promoting policy coordination, facility connectivity, unimpeded trade, financial integration and people-to-people bond.

Technical Cooperation

The CCFTA also includes provisions for technical cooperation and capacity building, particularly in agriculture. This will help Cambodia improve its export capacity and competitiveness in the Chinese market, while also promoting sustainable development in its agriculture sector. Personnel exchanges between research institutions will also build stronger links between the two countries and foster innovation in agriculture. The establishment of platforms for agricultural enterprises will further facilitate trade and investment in this sector, and streamline import-export procedures. Overall, these measures will strengthen economic ties and support the long-term growth and development of both countries.

Furthermore, the private sector plays a crucial role in promoting the quality of Cambodia's agricultural goods. In late 2021, the China Firm for Global Business (CFGB) built a working relationship with Cambodian government agencies in research and development to promote Cambodia's export of agricultural goods to the Chinese market.¹³ Both sides will enhance planning and interconnection in industrial cooperation, and develop and implement potential projects and industrial development policy. They will also provide support to enterprises in the areas of start-ups incubation, innovation development of SMEs and the establishment and operation of industrial parks to enable them to leapfrog towards Industry 4.0.

In relation to electronic commerce, both sides will cooperate in the areas of joint studies, legal framework establishment and enforcement, experience sharing in policy making and government management of e-commerce as well as capacity enhancement for suppliers to directly access to the marketplace. Concerning transport and logistics, the agreement will simply harmonise cross-border transport and trade regulations, improving physical infrastructure and the quality of logistics services, and supporting the Greater Mekong Subregion Cross-Border Transport Agreement (CBTA).

IMPLICATIONS FOR CAMBODIA'S ECONOMIC DIPLOMACY

The government's Rectangular Strategy Phase IV (2018–2023) recognises the global economic shift to East Asia as a 'golden opportunity' for Cambodia¹⁴ to develop and modernise its manufacturing industries and services. Integrating Cambodia's production network with the region, developing infrastructure connectivity and facilitating the cross-border flow of goods, services, capital and data are crucial foreign economic policy instruments. Indeed, ASEAN, China, Japan and South Korea are Cambodia's key economic partners.

In January 2021 the Ministry of Foreign Affairs and International Cooperation introduced 'economic diplomacy' to promote trade, investment, tourism and develop Cambodian cultural identity. The economic diplomacy strategy of 2021–2023 is instrumental in enhancing Cambodia's international integration, diversifying its economic partners, expanding its export markets, and attracting foreign investors and tourists.

Under the pillar of international trade, the strategy stresses advancing and diversifying exports and export markets, identifying and capitalising on new opportunities for Cambodian products

and services, and strengthening international economic cooperation and partnership with a focus on bilateral and multilateral FTAs. The conclusion of the Cambodia–China Free Trade Agreement in late 2020, as well as the Cambodia–South Korea Free Trade Agreement in early 2021 and being part of the Regional Comprehensive Economic Partnership (RCEP) demonstrate Cambodia’s economic diversification strategy at play. Particularly, CCFTA will boost the export of Cambodia’s agriculture products to China.

The Cambodia Diagnostic Trade Integration Study 2019-2023 posits that China cannot replace the European Union and United States as markets of destination for garments, bicycles and shoes. However, China could be a potential market for agricultural products and processed foodstuffs.¹⁵ The CCFTA can lead to productivity gains while offering Cambodia new export opportunities, especially in agricultural goods and products.

China has emerged as the world’s biggest importer of Cambodian milled rice, now accounting for more than half the market share – versus just 3% a decade ago – and is expected to further strengthen its dominance going forward. Insiders point out that traders who ship to Chinese shores pay relatively large sums for the grains. In the first half of 2022, China bought 168,280 tonnes or 51.4% of Cambodia’s total milled-rice exports of 327,200 tonnes. Milled-rice sales to China have reached about 200,000 tonnes year-to-date, or the equivalent of half the official annual tariff-free quota allowance of 400,000 tonnes for Cambodian milled rice.¹⁶

In 2019, Chinese authorities granted import permission to Cambodian bananas, making them the first Cambodian fresh fruit to receive market access to China. The growth has been driven by more Chinese companies investing in plantations and in the banana production and export infrastructure in Cambodia. In the first half of 2022, reportedly all of Cambodia’s banana exports were sent to China.¹⁷

In early 2022, China completed the risk assessment of Cambodian Pra fish, sweet corn, and longan in addition to banana and mango. These products can now be shipped directly to China. Currently, 74 longan plantations and eight longan packing plants have been registered and recognised by the Ministry’s General Department of Agriculture and the General Administration of Customs of China.¹⁸ So far, Cambodia has exported 27 kinds of agricultural products to China.

The National Policy on Cassava 2020-2025 is a significant step towards developing Cambodia’s cassava industry and expanding its export market. Cambodia has already made progress in exporting cassava, with Vietnam and Thailand as the top buyers, and China’s emergence as a key export market for Cambodian cassava is a positive development. The new agreement between Cambodia and the Guangxi Zhuang Autonomous Region to export 400,000 tonnes of dried cassava from March 2022 to March 2023 has been a good opportunity for Cambodia to further increase its cassava exports to China.¹⁹ However, it is important for Cambodia to continue developing its cassava industry and addressing any challenges that may arise, such as ensuring quality standards and improving productivity and efficiency in the process.

Peppercorn is another key Cambodian agricultural product. In 2021, the country exported over 28,074 tonnes of the item. The total land area of pepper cultivation is about 6,000 hectares

nationwide. In November 2022, The General Administration of Customs of China (GACC) gave the green light for Cambodian peppercorn exports to China after the Protocol of Phytosanitary Requirements for Export of Peppercorns from Cambodia to China was signed by the Cambodia's Ministry of Agriculture, Forestry and Fisheries and the General Administration of Customs of China. The direct exports to China would effectively end Cambodia's reliance on Vietnam or other neighbouring countries acting as middlemen in China's import of Cambodian peppercorn.²⁰ Cambodia has been exporting peppercorn to markets such as Vietnam, Europe, the US, South Korea, Japan, Chinese Taipei, and the Middle East, and it has been affirmed that some of the product shipped to Vietnam end up in China.²¹

To fully utilise the benefits of CCFTA, there is a crucial need to promote strengthen public-private partnerships. By working closely with the government and related authorities, firms, businesses and export companies can ensure that they understand and comply with the preferential access and rules under the agreement. This will enhance their export competitiveness and capacity. In addition, the setup of a team of experts at the Department of Export-Import to assist Cambodian exporters on rules of origin and Certificate of Origin is a positive step towards facilitating trade. The simplification and automation of rules of origin can reduce export costs, which will make Cambodian products more competitive in the Chinese market.

Notably, the law on rules of origin, once passed by the National Assembly, will provide a more solid legal framework for determining the origin of goods and promoting compliance with the rules of origin under CCFTA. This will further enhance the transparency and predictability of trade between Cambodia and China, making it easier for businesses to take advantage of the preferential treatment offered under the agreement.

CONCLUSION

The CCFTA can provide Cambodia with an opportunity to deepen economic ties with China. However, to fully benefit from the agreement, Cambodia needs to address some of its trade barriers, particularly in the area of sanitary and phytosanitary measures. Technical support from China and other partners can help Cambodia improve its institutional capacity and automate and digitalise trade facilitation. In addition, public-private partnerships can enhance Cambodia's export capacity and competitiveness.

The CCFTA reflects the present trend in South-South trade, offering new growth opportunities for developing countries such as Cambodia. To promote industrialisation and export diversification, developing countries need to adopt an integrated industrial-trade-investment strategy. China, as a global trading power, can play a significant role in this process.

ENDNOTES

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