



Media Release

RAM Ratings revises outlook on Cambodia to negative from stable, reaffirms ${}_{\text{g}}\text{B}_1(\text{pi})$ rating

RAM Ratings has revised to negative from stable the outlook on Cambodia's respective ${}_{\text{g}}\text{B}_1(\text{pi})$ and ${}_{\text{sea}}\text{BB}_3(\text{pi})$ ratings on the global and ASEAN scales, to reflect the potential withdrawal of preferential trade access to the EU and US markets and heightened macrofinancial risks. The ratings have been reaffirmed on the basis of commendable economic growth as well as FDIs and official loans which continue to support the country's external financing needs.

Cambodia's exports, particularly garments, face severe challenges amid rising protectionism and sluggish global growth. Preferential trade privileges reserved for least developed countries currently offer Cambodia duty-free and quota-free access. However, criticism of Cambodia's human rights abuses and disregard for democracy had led to a review of these privileges, with the EU presently evaluating the country's efforts to address the issues. A decision on the suspension of some or all aspects of Cambodia's special trade status is expected by 1H 2020. Additionally, the US has introduced the Cambodian Trade Act 2019 to reassess preferential trade treatment accorded to the country.

Considering Cambodia's reliance on the EU and US markets (which account for 61.3% of its exports in 2017) and its narrow range of exports, 78% of which are garments and footwear, the potential revocation of special privileges could significantly affect the growth trajectory of the country. "Cambodia's exports accounted for more than 100% of GDP in 2017. Any imposition of tariffs, in addition to a rising minimum wage, will undermine the country's export competitiveness and in turn affect the economy," notes Esther Lai, RAM's Head of Sovereign Ratings.

Macrofinancial risks have been amplified by rapid growth in credit, primarily extended to the construction and real estate sectors. Oversupply in certain real estate segments, unregulated lending by property developers and a potentially slower pace of Chinese FDI inflows compound the risks. Given that total loans reached USD4.85 billion as at end 1H 2018 or 22% of GDP (2017: USD3.9 billion; 17.6% of GDP), microfinance institutions with more relaxed underwriting standards pose a rising systemic risk. Cambodia's substantial exposure to contingent liabilities related to public-private partnerships may erode future fiscal flexibility.

Cambodia's GDP grew at around 7% in 2017 and 2018, backed by construction, manufacturing exports and tourism activity. Expansionary fiscal policies had also contributed to the commendable growth. The government is targeting a budget deficit of 3.7% of GDP this year (2018: 4.8%) in view of higher property tax revenues. Nevertheless, GDP growth is expected to moderate in 2019 amid challenging external conditions. Cambodia receives large capital inflows in the form of FDIs and official loans from multilateral and bilateral development partners. These inflows help finance its persistently wide current account deficits and boost foreign exchange reserves. Official loans are the government's key source of affordable funding. These rating strengths have not been affected by the potential withdrawal of trade privileges.

A downgrade of Cambodia's ratings may be warranted should the loss of special trade status cause worsening economic conditions and a deterioration in fiscal metrics. Distortive developments in the property market and increased financial vulnerabilities will also exert pressure on the ratings.

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