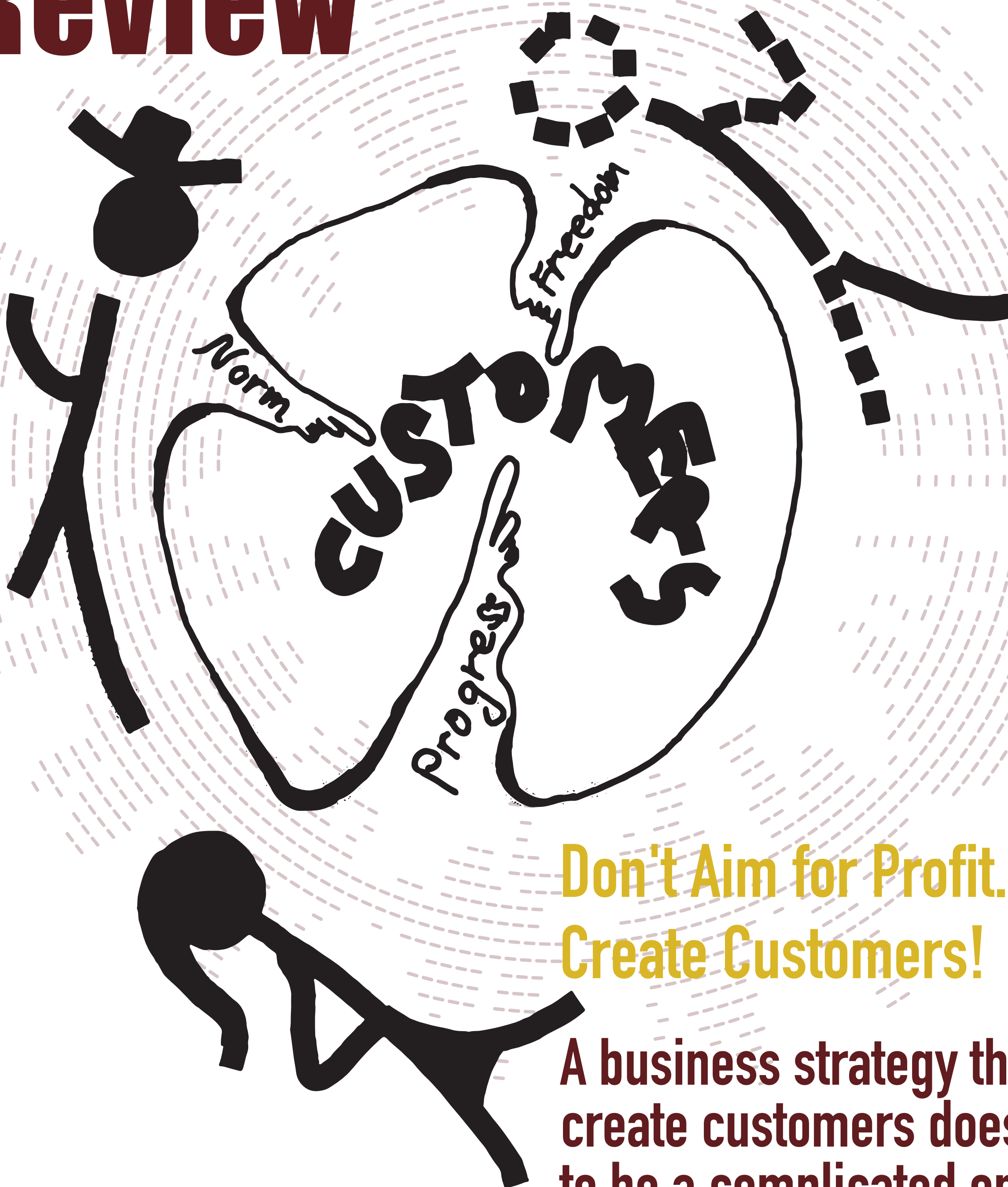
Inaugural Issue

CamEd Business School

CamEd Business Review



Don't Aim for Profit. Instead, Create Customers!

A business strategy that aims to create customers does not need to be a complicated one. Indeed, a simple 3-stage framework might just do the trick.

January- June 2024

A NOTE TO READERS

The views expressed in articles are solely the authors' own views.

Published by

CamEd Business Review (CB Review)
CamEd Business School
Phnom Penh, Cambodia
https://cam-ed.edu.kh/camed-business-review/

Welcome Message from Chairman

Welcome to our Inaugural Issue of CamEd Business Review!

Barely three months ago, I informed our faculty members that I would like for us to start publishing a business review which directly talks to CEOs, senior executives, practitioners and professionals in the business community. The responses were overwhelmingly supportive. Quickly, we began receiving manuscripts from our faculty representing various disciplines, to whom I wholeheartedly say Thank You Very Much. Your short articles on the following pages speak volume of your expertise and commitment. Moreover, I had reached out to non-academics whose opinion on important issues helps us see what it is like on the ground. We received manuscripts from the CEO, Partners and Country Director from a real estate company, a tax firm, a law firm and an international organization. Their insightful manuscripts clearly showcase our school's core value of embracing practicality. So, to you, I am deeply grateful and look forward to your continuous support. True to my own philosophy of always leading by examples, I volunteered to review all the manuscripts for this Inaugural Issue. I am hoping that you will tolerate my limited experience. But rest assured that we will keep improving as we embark on this journey together. Finally, my thanks go to our internal media team and the editor-in-chief who did everything possible in order to meet our deadline.

Have a good read through, and feel free to contact us at:
cbreview@cam-ed.com

Best wishes,

Dr. Virak Prum
Chairman & Professor, CamEd Business School

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January - June 2024

AI in the think tank World: My Personal Assistant, Not (Yet) My Friend

By Jason Chumtong
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Introduction

In 2019, I shifted my approach towards Artificial Intelligence (AI) from academia to the political sphere. I transitioned from studying the risk of AI for autonomous driving in Edinburgh to serving as a policy advisor on AI in Berlin. Although I was never a supporter of the Kurzweil-Narrative in The Singularity is Near (2005) regarding AI's evolution to surpass human intelligence, I remember that at that time, the consensus among the community was that AI would at least become ubiquitous in the following few years. Highlighting this point might seem almost redundant, considering that at least half of the readers of this text are likely wondering if ChatGPT played a role in its creation. However, it's important to note that discussing AI often feels like missing the forest for the trees. There are many AI applications out there that make life much easier. However, there are nearly as many problems associated with their use, demonstrating that AI is far from being a friend. Therefore, the text that follows shine upon aspect of the benefits AI provides as a digital tool akin to a personal assistant especially within the think tank world but also analyses ethical considerations and the state of technology that prevent it from being entirely reliable.

AI in the think tank word

Since I started focusing on AI in politics back in 2019, I've seen some truly interesting changes in how people view and use artificial intelligence. Initially, conversations around AI were dominated by its involvement in high-tech areas such as image recognition, robotics, and autonomous driving. As Mikey James illustrates in *The Evolution of Artificial Intelligence* (2023), these applications, complex and almost futuristic, showcase AI's potential in transforming industries and daily life. However, a significant shift has occurred over the years, steering the collective consciousness towards AI's role in writing and content creation. This change signifies a monumental leap. AI is no longer an elusive technology reserved for the few but a practical tool for the many, particularly for those daring enough to integrate it to their work bench. As Michelle Mitchel argues in his book *Artificial Intelligence* (2019), this democratization of AI is both intriguing and inspiring. It suggests that AI has breached the barriers of specialized domains, embedding itself into the fabric of everyday work. The implications are vast, not only in how we perform our tasks but also in our understanding and acceptance of AI as an integral part of our professional lives. But how does this apply to Thinks Tanks in particular?

When employing an expansive definition of think tank activities, one can identify five fundamental pillars: 1. Research, 2. Policy Development, 3. Advocacy, 4. Education, and 5. Networking. These pillars, particularly the first four and to a certain degree the fifth, are interconnected through a crucial skill—writing. Writing, essentially the art of translating thoughts onto paper, is pivotal across these domains. In this context, utilizing text generation tools like ChatGPT not only represents one of the most recognized applications in the current landscape but also stands out as a superior digital tool for integrating AI into professional workflows for two primary reasons:

1) Reduced Complexity: ChatGPT, or any other text creation AI, uses written text as the interface. As long as you can translate your desired goal into written text, ChatGPT will generate a corresponding output. This simplifies the interaction process, eliminating the need for complex interfaces or additional forms of communication. In a work environment where writing is one of the core exercises, this design allows for seamless integration of AI.

2) Open Sea Approach: Building upon its simple user interface, ChatGPT in particular aids in suggesting how to use its services, such as “write an email” or “create a concept note.” However, there are no further structural components that force the user into a specific set of steps to have text created. Whatever you type, there will be a response. It is up to your creativity to enhance the result. I call this method the “open sea approach,” because the general environment gives you a casual understanding of its functions and even supports your behaviour partially. But the exploration part is up to you and your curiosity. If done correctly, almost all parts of the pillars mentioned earlier can be translated into a written input for ChatGPT to respond to.

Together, these two elements elevate a text creation AI into an incredibly powerful personal assistant, provided you clearly define your objectives. For optimal use, the focus should shift from merely selecting prompts that improve your text to articulating the specific needs and gaps in detail that the AI assistant is intended to address. This becomes particularly critical when considering the potential risks.

AI: The Black Box and its Echos

As we delve into the integration of artificial intelligence within the think tank world, the call for well-defined ethical guidelines becomes increasingly apparent, particularly when assessing the associated risks. A key concern in employing AI-generated content lies in the realm of intellectual property rights. Adhering to academic integrity by avoiding to copy-paste AI-generated text is a commendable first step, but it does not tackle the real issue: the opacity of AI processes. The mechanisms through which AI systems generate text, especially regarding how extensively they rephrase existing content from expansive datasets, remain unclear. This lack of transparency, often referred to as the “black box”. In Christoph Molnars Interpretable Machine Learning (2019) we learn that this problem, poses a significant challenge in the ethical deployment of AI. And as further highlighted by Francesca Rossi in Building trust in artificial intelligence (2019), simple advisories against direct copying fall short of addressing these deeper concerns. They merely navigate the issue without providing thorough guidelines on the appropriate use of text-generating AI technologies.

This complexity is further heightened by another important issue: the echo chamber effect. This phenomenon occurs when individuals are consistently exposed to information and opinions that reinforce their pre-existing beliefs, thus endangering the inclusion of diverse perspectives in their opinion formation. In their article The echo chamber effect on social media (2021) qMatteo Cinelli et al. point out that the problem is starkly evident on social media and personalized news feeds, where extreme forms of echo chambers are prevalent. However, text-generating AI is not immune to this issue. It is notably more challenging to identify the influence of echo chambers in AI-generated content. Unlike on social media, where users might recognize that frequently engaging with specific content leads to the recurrence of similar themes, in text generation via AI, such mechanisms are obscure. When AI is tasked with tasks such as “make my text sound more professional” or “finalize my facts into a comprehensive argument,” it may inadvertently replicate frequently used text passages, risking the originality of your content. This problem is particularly acute when AI is prompted to provide specific background on political matters or to define technical terms. While such prompts are standard for search engines during online research, their implications for the use of text generation AI are profound and often misunderstood. However, as mentioned earlier, recognizing and understanding these issues is crucial. As Janna Anderson & Lee Rainie conclude in their chapter Closing thoughts on ChatGPT (2023), by clearly defining the objectives, the AI is meant to achieve, one can harness the same AI technologies that pose these problems to create viable ways to ones goal. In the end defining the problem can be 50% of the solution.

Conclusion: Human creativity will prevail

In the dynamic interplay between AI and human creativity within the think tank realm, it’s clear that while AI can replicate certain aspects of human intelligence, the essence of creativity remains distinctly human. This creativity serves as a safeguard against the challenges posed by AI’s opaque processes and its tendency to create echo chambers. Recognizing that a general prompt yields a general result highlights the importance of individual reflection. This enables one to translate personal perspectives into creative expressions effectively. As stated in the beginning, for think tank professionals, the art of writing is familiar territory, which facilitates the integration of AI tools like writing assistants. However, the impact of a text—whether it's aimed at shaping policy, advocating for a specific set of facts, or outlining potential outcomes—does not solely rely on formal language, precise grammar, or thorough structuring. Rather, its effectiveness is derived from its narrative and the persuasive power of its content.We recognize this principle from the business world where it is equally critical. Here, AI shall not solely enhance efficiency and analyze data, but must also be used to understand market demands and reflect the changes of the respective environments in order to support decision-making. This approach provides businesses with a competitive edge by accelerating workflows and optimizing resource utilization to remain competitive. AI can expediently lay down a solid foundation for your arguments, much as spell-check tools help reduce typos in digital content. Yet, it cannot substitute for the unique creative flair that humans bring to their work. Therefore, as think tanks leverage AI technology, they must do so as an asset to enhance, not solely replace, repetitive and easy writing tasks. This approach ensures that AI acts as a conduit to a more informed, ethical, and human-centric future. Importantly, those who adopt this technology should not shy away from acknowledging its use. And yes, this text was enhanced through the use of ChatGPT.

Beyond the Numbers: How AI Empowers Accountants for Strategic Impact

by Edman Flores, MBA, CPA
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The Evolving Role of Accountants

Historically, the duties of accountants mainly involved maintaining financial records, reconciling accounts, and preparing financial reports. While these responsibilities remain critical, the role of accountants has evolved considerably. Nowadays, accountants are expected to provide strategic financial advice to businesses. They assist in establishing financial goals, crafting budgets, and developing growth strategies.

Accountants play an important role in organizational strategic planning and decision-making, extending their expertise beyond financial reporting to strategic management accounting (SMA). SMA takes a broader business perspective and informs strategic decision-making. The changing business environment and the introduction of new techniques have prompted management accountants to adopt a business orientation and strategic approach.

In addition, accountants actively participate in risk management efforts. They assess financial risks, identify vulnerabilities, and devise strategies to counter potential threats. Through this proactive approach, businesses can safeguard themselves from unforeseen financial crises. Accountants are also involved in financial forecasting, which helps businesses plan ahead. They use historical financial data and market analysis to forecast financial trends and recommend budget adjustments.

Furthermore, accountants play an increasingly important role in ensuring that businesses comply with tax laws and financial reporting regulations. They help businesses navigate complex tax laws, prepare accurate tax returns, and avoid legal issues. Given the ever-changing tax landscape, accountants are at the forefront of tax planning and strategy development. They assist businesses in identifying tax-saving opportunities, ensuring compliance, and optimizing their tax positions. Such a proactive approach results in significant savings and increased financial stability.

The emergence of digital transformation has transformed business operations, requiring accountants to adapt accordingly. Accountants today must be technologically proficient in order to optimize financial processes using accounting software, data analytics, and cloud-based systems.

AI is having a significant impact on the accountancy profession. One of the most significant changes is the ability of basic AI systems to automate repetitive tasks such as data entry and invoice processing. These previously time-consuming tasks can now be completed quickly and accurately by AI, freeing up accountants' time to focus on strategic functions. Automation can be used to standardize and simplify processes such as payables, receivables, general ledger, external reporting, and management accounting.

Beyond automation, AI offers benefits in various areas of accounting and finance. As highlighted in an article published by ACCA, machine learning (ML), a subset of AI, is already in use for financial planning and analysis, as well as audit tasks, and generative AI offers new possibilities. Generative AI can boost personal productivity by automating report generation, improving risk assessment, facilitating scenario modeling and predictive analytics, and providing more personalized services. However, responsible implementation and experimentation are required to fully grasp the potential and ensure ethical adoption of these technologies.

Limitations and Challenges of AI in Accounting

The integration of AI into accounting has sparked both excitement for its potential to improve efficiency and productivity, as well as concern about its limitations and associated challenges. One notable limitation is

AI's inability to completely replicate the complexity of human judgment in accounting tasks. For example, AI may struggle to accurately account for non-standard transactions such as complex lease agreements or asset impairment testing. While AI algorithms are extremely effective at processing large amounts of data and performing standard calculations, they lack the ability to make professional judgment that experienced human accountants possess. As a result, human oversight is necessary to ensure the effectiveness and reliability of AI's application in accounting.

Another limitation is the importance of professional skepticism in accounting and auditing practices. While AI has the ability to analyze large amounts of data, it may be unable to exercise skepticism in the same way that a human auditor can. Humans' ability to question and critically evaluate evidence is not easily replicated by AI. This skepticism is essential for detecting anomalies or irregularities that could indicate errors or fraud.

Moreover, AI falls short in the realm of ethical judgment. Accounting professionals frequently face ethical issues that require a thorough understanding of context, professional standards, and the potential consequences of decisions for various stakeholders. For example, an accounting firm is engaged in auditing a large multinational corporation in the technology sector. During the audit process, the audit team discovered potential irregularities that could significantly impact the client company's reported revenues and expenses. The audit team's ethical judgment in determining the appropriate course of action necessitated a holistic assessment of the impacts on stakeholders, including investors, employees, and regulatory authorities. Making such intricate ethical decisions is an area where AI proves inadequate due to its inability to effectively balance competing interests, analyze nuanced scenarios, and comprehend the broader ramifications of its recommendations. Ethical dilemmas in auditing often demand human judgment that considers not only the black-and-white rules but also the grey areas that require empathy, critical thinking, and a deep understanding of the ethical responsibilities of accountants.

The Importance of the Human Element in Accounting

The accountancy profession places a strong emphasis on effective communication and strong interpersonal skills for several compelling reasons. Firstly, effective communication is paramount for accountants who regularly interact with a diverse range of clients. Secondly, the accountancy profession has evolved beyond a mere focus on number-crunching and now involves actively engaging with clients. This shift has resulted in a greater demand for accountants with strong interpersonal and personal skills. Employers place a high value on the ability to collaborate effectively, present ideas persuasively, and maintain a positive attitude, as evidenced by their frequent mention in job advertisements.

Additionally, accountants possess commendable adaptability and problem-solving skills, enabling them to effectively address emerging challenges, regulatory changes, and unforeseen issues that arise. The ability to swiftly evaluate situations, identify appropriate solutions, and implement strategies in order to overcome obstacles necessitates intellectual creativity and critical thinking that go beyond the capabilities of AI systems.

Adapting and Upskilling in the Age of AI

To successfully integrate AI into accounting practices, it is crucial for accountants to enhance their skills in areas that require human judgment, such as financial data interpretation, strategic planning, and specialized business advice. Additionally, a strong focus should be placed on data management, including data cleansing and correcting inaccurate or incomplete data.

As AI technology becomes more prevalent, accounting professionals must recognize that their role will undergo significant changes, allowing them to shift their focus towards managerial decision-making. With AI's ability to handle large volumes of data, accountants can dedicate their attention to analyzing this information. However, effective analysis requires a deep understanding of business contexts and strategic implications.

It is crucial for accountants to acquire a comprehensive understanding of AI, encompassing its capabilities, limitations, and potential applications in their specific areas of expertise. This necessitates employers to implement training programs and educational initiatives that equip accountants with the necessary knowledge and skills to effectively use and interpret AI tools, such as robotic process automation for automating repetitive accounting tasks, ML algorithms for financial forecasting and risk analysis, and natural language processing for automated data extraction and report generation. Regular upskilling programs are vital to keep accountants informed about the evolving technologies and best practices in AI, creating an environment that supports innovation and responsible AI implementation. Moreover, fostering strong collaboration between professional accountants and experts in data science and AI is essential to encourage interdisciplinary cooperation and ensure the responsible and effective utilization of AI.

Conclusion

The rise of AI has brought about significant changes in the field of accounting and finance, prompting the need for accountants to adapt and embrace AI as a powerful tool that can empower them for strategic impact. While concerns exist about the potential replacement of accountants by AI, it is important to recognize that AI automation has the potential to enhance accountants' efficiency, accuracy, and decision-making abilities. By automating repetitive tasks, AI allows accountants to focus on higher-value activities that require human judgment, directing their skills towards strategic decision-making. To adapt to AI-driven transformations, accountants must upskill in areas that require human expertise, such as business and tax advisory, data analytics and interpretation, and strategic planning. By leveraging AI's potential and embracing technological advancements, accountants can position themselves as valuable strategic advisors and maintain their relevance in the accounting and finance landscape.

DON'T AIM FOR PROFIT. INSTEAD, CREATE CUSTOMERS!

by Virak Prum, PhD
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Purpose of any business

It is well known that the purpose of a business is to create customers. Nothing else should matter as much. Peter Drucker, the well-regarded creator of management study as a distinct discipline, announced his wisdom early on when he published his *The Practice of Management* in 1954. There is, he wrote then, "only one valid definition of business purpose: to create a customer." (p.37) Yet, it is not uncommon to find managers and economists so focused on profit maximization which leads them to prioritize on quick wins, neglecting the need for a more comprehensive strategy. True, business environment in the 1950s might have been quite different to what we are facing presently. Globalization and technological advancements have brought about new challenges and changing realities into the market, a phenomenon which could make long-term strategies less certain. But, even so, half a century after his famous book first appeared, in the revised edition of *Management* published in 2008, the assertion remained unchanged: "to maximize profits…is not only false, it is irrelevant." (p.97)

If not profit, aim for what?

Granted, most books on corporate finance and financial management readily follow the same concept: maximization of profits for shareholders. "The success of a corporation depends on how…to increase value," write Richard Brealey et al. (*Principles of Corporate Finance*, 2nd ed, 2011, p.1). And they are not wrong in claiming so, because that is what finance managers are hired to do. But they are exactly that: managers, rather than strategists. Managers are different from strategic leaders in that managers are obsessed with planning and costing whereas leaders believe in a vision and devise a strategy after evaluating various options. Planning is not strategy. In any sizeable firm, plans generally exist everywhere. If you care enough to bring all the plans from all the divisions and view them altogether, they usually fail to form a big coherent whole. It will not be a surprise to find out that some plans are even counterproductive to each other. Lafley and Martin, in their best-selling 2013 book called *Playing to Win: How Strategy Really Works*, do not directly talk about profit maximization in their famous 5-question strategic framework.

Thinkers who do not treat profit maximization as a guiding purpose might not be always right. But profit, as any reasonable person can tell you, ultimately should be the likely result anyway if you have a right strategy and faithfully carry it out in an innovative manner. This is why two respected strategic thinkers painstakingly studied and tested their theory and bet everything on what they have famously called Blue Ocean Strategy, which powerfully recognizes "value innovation" as the cornerstone (Kim and Mauborgne, 2005). Maximization isn't the same as innovation. Simply put, value innovation focuses on "making the competition irrelevant by creating a leap in value for buyers and your company, thereby opening up new and uncontested market space." (p.12) As such, the recommended business strategy is one that must aim to create new market and find new pools of customers.

Any observable trend?

A quick search on mission statements or similar statements adopted by purposeful companies in various industries—social media, food and beverages, hospitality, banking and manufacturing—tends to reflect the power of a customer-centered business model, a trend that is self-reinforcing.

Industry	*Statements on mission, purpose or similar aspirations*	*Source*
Meta (Facebook)	Giving people the power to build community and bring the world closer together.	https://about.meta.com/company-info/
Brown Coffee and Bakery	The BROWN family is committed to excellence and to providing friendly and welcoming service.	https://www.browncoffee.com.kh/page/Our_Company
Airbnb	Every day, hosts offer unique stays and experiences that make it possible for guests to connect with communities in a more authentic way.	https://news.airbnb.com/about-us/
ABA Bank	Our mission is to help Cambodia, Cambodian businesses and people to build a bigger and brighter future…	https://www.ababank.com/en/about-us/vision-mission-values/
Toyota USA	We create vehicles by listening and responding to you. Why? Because it's our belief that our cars should do more than help you go places on the road, they should also help you go places in life.	https://www.toyota.com/usa/our-story#philosophy-practice

How many times are these words You, People, Community used in the above statements? If you are a coffee lover like I am, you have certainly tasted the world's most recognizable brand: Starbucks coffee. Instead of settling for an uninteresting drink, Starbucks strategy is to allow customers to have coffee tailored to their personalized liking with various options to choose, from the level of sweetness to the amount of caffein (or decaf) to the type of milk to the amount of ice or heat and many more varieties. Obviously, Starbucks company strives to create and nurture returning customers who are made to feel as if the brand belonged to them wherever they may be, globally. When the world was hit by the Global Financial Crisis in the years 2007-2009, Starbucks registered a 21% decline in earnings but, after introducing several bold moves, the company subsequently turned things around. One such recognizable move was to "ignite the emotional attachment with our customers" (*Leading the Starbucks Way*, Joseph A. Michelli, p.3-4, 2014). This is the reason why, "to inspire and nurture the human spirit—one person, one cup and one neighborhood at a time" is the mission statement of Starbucks Coffee Company (https://www.starbucks.com.kh/about-us/company-information/mission-statement). It does not require a rigorous training to be able to predict that Starbucks coffee shall remain a successful business (and therefore profitable) in the foreseeable future because they, clearly, have embraced Drucker's advice that the purpose of a business is to create a base of inspired clientele, first and foremost.

Any alternative?

Maybe. Of course, people don't like the idea of a one-size-fits-all prescription. They aspire to believe what they choose to believe. But for all the technological breakthroughs and for all the knowledge we have acquired concerning the mysterious universe, nobody can yet claim with certainty whether our human species had evolved à la Darwinism or were created by God. Uncertainty is the rule when it comes to big things. And in a big field such as economics, there often are numerous uncontrollable factors at play that can affect the fate of a particular industry at a particular time. For instance, if in a given country, the government suddenly decides to heavily subsidize local products so much that foreign imports simply become totally uncompetitive, imports would decrease unless the importers succeed in re-inventing a new value proposition based on some uniqueness that makes pricing an irrelevant factor for customers. For example, for those who readily pay $4 dollars for a cup of coffee, price does not seem to be a problem. In Phnom Penh, with all the promotional discounts that are now offered regularly, loyalty and stickiness are hardly breakable. The existence of an expanding business ecosystem adds more value quickly, which helps to create and retain customers. And if yours is already a powerful and dignified brand, it can, with some localized tweaks, carry itself far and wide. For instance, faced with an initially strong resistance from

Vietnamese consumers, observers were quick to suggest that Starbucks would pull out of this coffee cultured Asian country. But the last time I checked, by September 2023, Starbucks had just opened its 100th store in Vietnam (https://en.vietnamplus.vn/starbucks-opens-100th-store-in-10-year-journey-in-vietnam-post268156.vnp).

So, how can we do it strategically?

Complexity belongs in a fool's toolkit. Resolving complex matters in simple ways is a habit of a genius. I am sure this statement sounds familiar. I recently gave a speech at CamEd Graduation Ceremony 2024 in which I asked graduates to simply ponder over three things: norm, progress and freedom. It would be great if strategy may be thought of this way:

Stage 1: Strategy as Norm. For example, formulate something to this effect: I am going to try to convince ten couples a week, come what may. Stick with this norm, you and your team. Commit to do as you say without second-guessing. Make it a law that you don't break unless warranted by absolutely necessary circumstances.

Stage 2: Strategy as Progress. This is when all the identified suitable and feasible resources are brought into action. All acceptable changes that must happen have to happen. No nonsense nay sayers; no reactive excuses. Keep going, keep doing, keep progressing until the desired norm has become a routine. Watch out for resistance and handle it tactfully. If necessary, do the unexpected.

Stage 3: Strategy as Freedom. If your normative strategy involved creating more excitement so that customers would want to stay a night longer (Sunday night) on top of their usual Saturday night stay, it should be clear by now what tactics/resources were used effectively, which led to progress. For things that worked, continue to execute them with tweaks as may be necessary. Those that did not work must be freely dropped, so as to give you needed space to maneuver. Also, don't forget to freely take lessons to heart and freely evaluate progress and pitfalls.

Quite often even well-versed normative strategies fail to achieve results because they are not progressively executed and become quickly unrecognizable, making the whole team lose confidence. So, execution, execution, and progressing. If, after executing it faithfully, it somehow creates effects not as intended, you must feel free to revise, rectify, drop and try new ways. A strategy that offers no such freedom can become outdated or even harmful. Creating customers is not easy but not impossible. No strategy can bring you customers unless you act. Along the way, learn to appreciate progress and celebrate even small gains. Take to heart The Power of Small Wins (Amabile and Kramer, HBR, 2011).

Great, but will it work?

Have some faith. Let me draw a parallel from something bigger than ourselves, the fabric of our democratic society. If you read political or constitutional law materials sometimes, you would notice the idea that there should be three branches of government, three stages of governing: legislative stage, executive stage, and judicial stage. If legislators and ministers are inherently faithful and wise, a good law should carry itself at ease at these two stages since the intended effect was clearly identified from the get-go. Likewise, an effective strategy should manifest itself at the normative and the executive stages. Otherwise, just as a badly worded law would give ministers and judges headache and confusion, a poorly articulated strategy renders execution unnecessarily hard and, worse, it won't accommodate freedom that the evolving market space requires every so often. True, even without a good strategy, pure luck might still bring about some success sometimes. But if you do not grasp the challenge and do not assess what the challenge means for the future, less customers guaranteed.

How to Measure Creating Shared Value

By Kenneth Paul Charman, PhD
Professor, CamEd Business School

Creating Shared Value and Sustainability

The concept of creating shared value (CSV) was put forward by Professor Michael Porter and Mark Kramer in 2011 to identify company strategies which directly address a social need for profit through the business model rather than addressing the same social needs through redistribution of profits already made. Many companies, including large corporations have adopted CSV principles to govern and guide their business strategies. CSV represents a further progression in rethinking the role of the firm from the more narrowly defined responsibility of providing shareholder value, to the wider perspectives of addressing the impact of the firm on its stakeholders through corporate social responsibility (CSR). The principles of corporate governance are well established to oversee the activities of firms, and sustainability reporting is common today, and which now extend to frameworks and guidelines for reporting. Responsible Business Conduct (RBC), put forward by the OECD has provided a framework to incorporate due diligence to guide actions to reduce or alleviate the negative impact of a firm on its stakeholders. More recently the growth of ESG accounting has provided metrics for measurement of the impact of the firm on the economy, social factors and its environment, creating huge steps towards sustainability accounting.

Each of these frameworks has its niche. Collectively each contributes to a fuller understanding of the role of a firm vis-à-vis society and are providing guidance to move towards better practice. In addition to practical guidance, each of these frameworks also provides a beacon of light on corporate purpose, giving a sense of direction, that a company has a social purpose beyond that of its own shareholders. CSV sits withing this broad categorization of sustainability measures, with a niche of win-win for the firm and for social needs.

The evolution of metrics through ESG accounting and the due diligence process of RBC has brought the sustainability frameworks to a new level where there is responsibility not only for a company to recognize its social responsibilities but to actively take steps to reduce negative impact on stakeholders and to report on its social impact. The guidance and manuals created under ESG and RBC, are providing a basis for CSR reporting, now commonplace amongst corporations and smaller firms. Similar scope for measurement and verification should be a priority for CSV.

It is this progression to measurement and operationalization which creates an opportunity. Creating shared value has proponents, who consider that CSV represents a new purpose and way of thinking for businesses wishing to make a positive impact on social needs. But shared value also has critics, who claim that CSV is nothing new, covering nothing more than what has already been covered by CSR and other sustainability frameworks. Verification would establish the CSV contribution.

Measuring Shared Value

Creating shared value (CSV) has a distinct niche, that a company can address social needs through its business, with no need to redistribute profits because social needs are benefitting through the business itself. If there is commercial purpose in addressing a social need, then purchasing the company's products or services directly provides both a commercial and a social benefit. If this can be measured and verified, CSV can claim its niche, and can contribute directly to the growing body of sustainability reporting.

An effective way to measure CSV can also provide a roadmap for companies adopting the CSV path. Knowing what results and impact they can make, both commercially and for social needs, gives company's large and small a target to achieve, and resources and capabilities can be guided over time to reach a multiple purpose of achieving both commercial success and social impact.

Value Created: Private Sector Return

So how might we measure CSV? Firstly, the scope of shared value was taken from the original principles put forward by Porter and Kramer, that the benefits of creating shared value are likely come to a firm in three areas; through the customer needs served and the products and services created, through improvements in the value chain from raw material or concept through to the customer, and the value to the industry itself, the cluster, and the industry spin-offs which can occur from a shared value initiative. For each of these components, likely categories of value added were set out. For example, products and services aimed at CSV often involve innovation, new ways of addressing social needs, and new business models. New attributes create value for customers. These create value for the firm through creating a platform for future business and spin-offs. New methods of processing can improve the value chain, creating less waste, more innovation in processing, new techniques of manufacture. At the industry level, these can result in more collaboration and industry spin-offs. This broad categorization of value added allows for the assumption that value can come from many different sources, and the categories are broad enough and inclusive enough to be able to include any specific measure of value added that the firm can identify.

Value Created: Social Needs

The same process was carried out to measure of how a firm's business directly impacts social needs. A broad categorization of social needs comprises five categories. Firstly, quality economic activity, which can include good quality employment, startups, infrastructure, and can extend to local price, civic pride. Secondly education, including affordable schools for children of all ages, access to higher education, public awareness, technological awareness. Thirdly, health and safety, which could include a firm's contribution to healthcare directly, or to improving safety standards, or health awareness amongst the population, each of these can be measured and assessed. A fourth category is social progress, measuring such factors as basic human needs, housing, shelter, access to clean water and sanitation, opportunity and inclusivity. The final category is the environment, the impact of the company's activities on the urban and rural landscape, and which can also extend to broader impact such as preservation of historical sites.

Not all value added can be directly measured. Employment and startups are straightforward to measure, but happiness, community engagement, and civic pride can also be measured, even if only indirectly through interviewing people. So, it is suggested that a suitable measure is chosen for each component where the company can claim to be adding value. An indicator, a corresponding means of verification and an expected or actual result are all that is required.

Using this framework, any business can develop a template of how and where it is creating shared value. Indicators can be added amended over time as the business model evolves. Some indicators, such as increasing employment can be directly measured, increasing the quality of jobs is more subjective, and improving civic pride is wholly dependent of people's views. But the purpose is to recognize where value is created.

Measuring Shared Value Impact

Also included is the facility for the measurement of impact using a simple framework which assesses impact at three levels. Firstly, marginal impact, where value is created for the firm or for a social need and can demonstrate a profit, or some measurable benefit which, whether large of small in size could form a valuable platform for future business. Secondly, sustainable impact, where a firm can be seen to have created a sustainable, self-supporting or revenue generating business activity which benefits both the firm and provides a lasting social need. Thirdly, at a game-changer level, where a new way of delivering a social need is shown to provide superior profits and benefits and as a result, supersedes the previous ways of delivering the social need. Such new ideas often form the basis for a new business model with noticeable improvement to both the firm and to social needs delivery.

Measuring Shared Value: Contribution

The categories, value added, indicators, results and assessment of impact can be easily compiled into a table, and used to assess shared value created, either at a heuristic (rule of thumb) level or in more detail. The table below provides some examples of how to demonstrate that a business undertaken by a company has led directly to creating value for the firm and the industy and also for social needs.

Providing a measure of shared value needs a straightforward and pragmatic approach. Developing ways to measure shared value based on appropriate indicators brings us forward to answering the question of actual and expected shared value, where, how much, and the potential impact that creating shared value will have on the firm and on addressing social needs.

Equally importantly, the process of developing measures can help us find common ground between the more established areas such as ESG, RBC and CSR, where we are likely be measuring the same or similar impact. The intention is to contribute to the building of measures of sustainability, and thereby helping progress the debate on the role of business in society, and in particular demonstrating the contribution of creating shared value.

Measuring the Impact of Your Business's Shared Value Created

Your Shared Value Initiative			
Likely Benefit / Value Added	**Indicator of Value**	**Expected Results/Verification**	**Impact**
PRIVATE SECTOR VALUE			
New Needs, Products, Customers	Market size; profitability Innovation level Reputation platform	Sales and market share New product /service New business spin-off	New products, services, New delivery of social need Reputation leads to business
Value Chain	Reducing cost & waste Building resources Developing competences	Company technical report New infrastructure New innovative skills	Greater efficiency Improved infrastructure More skilled workforce
Cluster Development	Cluster building Industry collaboration Spill-over potential	New cluster activities New partners & suppliers Greater output & exports	New industry activity New local skills New sectors and trade
SOCIAL NEEDS VALUE			
Quality Economic Activity	Flourishing local economy Local Infrastructure Community Engagement	Economic activity/employment Affordable infrastructure More community involvement	Widespread Local Prosperity Greater wealth spread Strengthened communities
Education and Skills	Affordable schools & education Higher education provision Workforce & technology skills	Number & quality of schools Enrolment at university/STEM No. trained in vocational skills	More educated population Higher & professional skills Skills based population
Health and Safety	Public health improvement Fit & Active Population Higher Safety Standards	Lower disease incidence Improved activity levels Improved work/transport safety	Low obesity/chronic disease Fitter & active population Reduced work/road accidents
Social Progress	Fulfilling basic needs Improving population wellbeing Opportunities and inclusiveness	Less people below poverty line Less anxiety / less stress Creation of opportunities	Better wealth distribution Healthier, happier population Diversity of opportunities
Environment	Urban and rural environment Air, coast, marine environment Energy and water efficiency	Reduced urban / rural pollution Less polluted coast, sea & air Reduced fossil fuel use	Cleaner lives & environment Vibrant coastal environment Sustainable energy future

Lessons in Cambodia's Real Estate: Raw Opinion of a Practitioner

By Kevin Lim
Chairman, Key Real Estate Co., Ltd

Why investing in Cambodia's real-estate

With political stability, Cambodia has opened to the world and has become one of the fastest growing-economies in Asia, with strong record of sustained GDP growth of over 7% in the past two decades prior to the COVID-19 pandemic in 2020, driven largely by export-oriented manufacturing, tourism and real estate developments.

Geographically, Cambodia is located at a very strategic location within ASEAN. It is the central hub and gateway to ASEAN member nations. So, investing in Cambodia is to target the overall ASEAN market with 670 million populations. Cambodia also joined RCEP. Such regional integration laid a good foundation for Cambodia to boost its exports further through multilateral and liberalized trading system. Investors may also benefit from the bilateral Free Trade Agreements established between Cambodia and China and other ASEAN/RECEP member nations.

Cambodia is agricultural-based economy. With its young and inexpensive vibrant work force and huge vacant agricultural lands across the country the country presents a great opportunity for investment in agro-industrial sectors for domestic consumption and exports to regional and global markets.

Cambodia is largely a dollar-based economy. Foreign investors can conveniently transact their business within the country in U.S dollars and repatriate their business profits with ease. Favorable investment climate for Foreign Direct Investment (FDI). Freehold foreign property ownership and 100% ownership of business are allowed. No restriction or control on foreign exchanges and international money transfer.

Cambodia remains a sought-after paradise for tourists and retirees, attributed to the low-cost of living, untapped natural resources, absence of major natural disaster, political stability, urbanization and on-going infrastructure development.

Opportunities in real estate investment

As a newly emerging market, Cambodia presents a golden investment opportunity in real estate, which is an important pillar contributing to the country's economic growth. In the last two decades, affordable housings and plot lands were rapidly developed in urban centers and suburban areas respectively in response to the migration of young Cambodians from rural to urban areas in search for job or in pursuit of further education. Further, millions of young Cambodians, who are working overseas, have been sending money back to Cambodia members to invest in residential properties for investment or residential purpose.

The changing lifestyle among the younger generations is a key contributing factor to development of mid-range and high-end residential properties including gated communities ("Borey") and condominium in the urban centers. The older generation Cambodians chose to live with big family under one roof either for economic or cultural reasons. The younger-generation Cambodians, in contrast, are more educated and economic independent. They are either professional or entrepreneurs, who largely represent the rising middle class with exposure to overseas and contemporary lifestyle.

The influx of tourists has driven the development of hospitality industry, building of guest houses and hotels of all levels, which indirectly drives the price of real estate up in major urban areas including Phnom Penh, Siem Reap, and Sihanoukville.

The Cambodian government has ambitious urban expansion and infrastructure development plans to cope with anticipating demographic and economic growth.

Due to limited public transportation and increasing traffic congestion, Condo has become more and more appealing to young educated and professional Cambodians working in Phnom Penh and major cities. However, condo-living is still not attracting Cambodians at large. Most Cambodians still prefer landed properties, Villa or Town House, to Condo. The main contributing factors to such negative attitude include Condo's strict rules and regulations, relatively high management fee, limited parking, and no empty space for hobby gardening, many Cambodians suffer from acrophobia.

Cambodia's real estate boom was largely driven by home lending products made available by banks and Microfinance Institutions (MFI). In the last two decades, commercial and specialized banks began to offer attractive home loans to middle-high income earners with long loan tenor and flexible payment options. While MFIs have offered micro-loans to low-income earners with social mission. These, in turn, have driven remarkable sales growth in the residential housing business.

With constant economic growth and ever-changing lifestyle, younger generation Cambodians become more active in their employment, career, business, and less time for their parents or grandparents at home. Such challenges trigger the needs for quality nursing homes for elderly that have been growing in number.

The most potential areas for investment in real estate include Phnom Penh, Siem Reap and Sihanoukville. Phnom Penh is home of over two million residents. It is the center for tourism, foreign investments, commercial activities, and government. Rapid real estate development has been witnessed in recent years with hotels, skyscrapers, shopping malls, and gated communities being developed by both domestic and foreign investors. The norther part of Phnom Penh, along the national road 6A leading to Siem Reap is ideal for high-end residential properties given it's newly developed areas along the 2 rivers: Mekong and Tonle Sap. Siem Reap is the gateway to Angkor Wat, the Eighth Wonder of the world. It established itself as a cultural hub for tourists and therefore driving demand for accommodation and real estate development. The completion of the 38-road expansion project, with total length of over 106 km and cost around USD149 Millions added significant value. Sihanouk Ville is, once-tranquil beach town, vibrant commercial town characterized by the white sand beaches, busy commercial port, special economic zone, and high real estate prices. The Highway connected from Phnom Penh adds additional commercial value to the development. The influx of Chinese investments in hotels, apartment towers, restaurants, and casinos prior to the pandemic made Sihanoukville the fastest growing real estate development.

The Chinese investors withdrew after the ban of online gaming business followed by the pandemic, leaving behind with unfinished buildings that can be turned into a great investment opportunity for those developer/ investors who have funds and the right expertise as they can pick and choose the right location and negotiate for the best price using their best bargaining power.

Challengs and Risks

While Cambodia represents great investment opportunities in real estate, one must emphasize that challenges and risks are present and need cautious investment decisions.

Things you need to know including the type of land ownership, property developer's background and reputation, property location, and infrastructure, flooding in the area.

Proof of land ownership in Cambodia was not available after the Khmer Rouge Regime, in which private ownership of landed properties was abolished and land title records were destroyed. Cambodia began its private ownership re-establishment process from scratch with Land law being promulgated in 1992 followed by amendment in 2001 whereby a land registry system was created enabling land title issuance.

Several types of title deeds are available in Cambodia including LMAP, Hard Title, Soft Title, Strata Title. LMAP and Hard Title are both recognized at the national level and are the strongest form of land ownership. Initiated by World Bank, LMAP is different from Hard Title in that it has GPS coordinates that clearly identify the property boundaries. Soft Title are the most common form of land ownership recognized at the district and commune level. Strata Title is a hard title designed for co-ownership property. It is strongly recommended to have the ownership verified with the Ministry of Land Management to ensure it is legitimate, genuine, and encumbrance-free. Land ownership option should be decided based on investor's actual investment purpose and risk appetite. Advice from experts should be sought to mitigate investment risks.

The Cambodian law prohibits foreigners from land ownership in the Kingdom. The Strata Title introduced in 2009 allowed foreigners to own private units above the ground floor of co-owned residential or commercial building in Cambodia provided that the co-owned building is owned minimum 30% by the local Cambodians.

There are several options available for foreigners to invest in landed properties in Cambodia. The most secured option is to acquire a Cambodian citizenship. Other options include renewable long-term lease, engaging a trust company, setting up a property-holding company with 49%-51% shareholding structures, or using the nominee structure through which a Cambodian citizen is nominated as a legal owner.

In the last two decades, plot land development has become a popular investment opportunity among domestic developers in response to growing demand of low-income earners seeking to invest in landed properties for capital gain and/or residential purposes. However, in the recent years, such opportunities have been eroded due largely to unethical activities of some developers and the loss of incomes among low-income Cambodians.

Real estate business is less regulated. The general practice of real estate transactions is conducted in a traditional manner with thumbprints of the buyer and seller placed on the deposit form/agreement established with or without witness/lawyer. Brokerage service is available but not mandatory. Bank's Escrow account service is not widely used. Commercial banks have imposed lending restrictions to real estate sector in their lending portfolio.

Property valuation remains a challenge for buyers, sellers, and banks. Property valuation is a combination of arts and science. As science, it requires formula, theory and technical skills. As art, it needs human judgement and analysis. Good judgement needs practical experience, in-depth industry knowledge and data. It is therefore advisable that licensed independent real estate valuation firms should be sought to conduct professional and independent valuation services and minimize potential fraud.

Correction/Adjustment of real estate sector

Cambodian real estate will take a long and painful adjustment and correction to reach a new equilibrium.

The country has been facing challenges with an oversupply of gated communities, condos, and commercial buildings in the urban centers. This has placed downward pressure on occupancy and rental rate. Pricing strategy and structure must be corrected to fit the current real estate market. Developers need to reposition themselves in the market. Some of the existing unfinished construction projects, especially in Sihanoukville, need to be repurposed despite the challenges of the sophisticated local regulations and the costly conversion of building design, layout and MEP conditions.

Property developers must now focus on quality rather than quantity. Careful consideration will be placed on project branding and positioning, product design and concept, and sight selection for project development. Before any development projects take off, serious study must be conducted on the market to identify consumer behavior and attitude as well as the market trend. Investment in landed properties for short term capital gains and speculation is the thing of the past. Investor must have clear residential or commercial purposes for investment decision. No borrowing for investing on properties under construction for speculation purposes.

Outlook of real estate in 2024 and beyond

Emerging from stagflation, Cambodia's real estate market is heading on gradual and positive recovery trajectory. I hold an optimistic view that 2024 is a year of slow but strong economic recovery for Cambodia despite the spillover effects of China's real estate crisis, Russian-Ukraine war, Middle East crisis, and the escalating US-China geopolitical tension. According to ADB, the forecast GDP growth for Cambodia is expected to be 5.8% and 6.0% in 2024 and 2025 respectively due largely to rebounding tourism and influx of FDIs. Cambodia has experienced a significant upswing in visitor numbers with over five million of foreign tourists in 2023. According to CDC's (Council for Development of Cambodia) 2023 report, there were 268 major projects worth up to USD4.9 billion of total investment capital have been approved in 2023. Most of these approved projects are expected to be operational in 2024 and the subsequent years.

FDIs is the key driver. With its current limited capital funds Cambodia needs external capital to re-invigorate its economy. Capital funds injected in various sectors by FDIs will create jobs and stimulate the economy, thereby positively influencing the real estate business in Cambodia, directly and indirectly, since the economic performance is intricately linked to real estate sector. The pro-active and dynamic Cambodian government has ramp up its efforts in bringing FDIs into the country. It does so by introducing different measures and actively reaching out to international business communities. While China remains a major investor, Cambodia opens its door to FDIs from all countries that are interested in investing in Cambodia.

Opportunities and Challenges in Intellectual Property Rights Protection and Enforcement in Cambodia

by Ly Tayseng & Sophorn Pouvchannita
Managing partner and partner at HBS LAW

I. Legal and Regulatory Framework for IPR

Cambodia's IP framework has undergone significant development in recent years to align with international standards and facilitate innovation-driven growth. Cambodia is a signatory to various international treaties and agreements, including the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). At the time of Cambodia's accession to the World Intellectual Property Organization (WIPO) in 1995 and the Paris Convention for the Protection of Industrial Property in 1998, the regulatory framework to protect IP in Cambodia was weak. After the accession, the Cambodian Government has enacted numerous laws and regulations to strengthen the protection of IP rights in order to attract foreign direct investment. Those laws include the Law Concerning Marks, Trade Names and Acts of Unfair Competition; Law on Copyrights and Related Rights; Law on the Patent, Utility Model Certificates and Industrial Designs; Law on Geographical Indications; Law on the Management of Quality and Safety of Products and Services; Law on Seed Management and Breeder Rights.

II. Registration and Protection of Intellectual Property

The IP rights cover a wide range of areas, including patents, marks, copyrights, industrial designs, geographical indication and plant variety. While the laws governing these IP rights were adopted, the enforcement mechanisms and procedures are still evolving and each type of IP rights present different opportunities and challenges. The following are type of IP rights which can be registered in Cambodia:

- **Patents**

Patents protect inventions and innovations, granting exclusive rights to the inventor for a specified period. Cambodia's Patent Law, enacted in 2003, provides protection for inventions that are new, involve an inventive step, and are capable of industrial application. However, the process of obtaining and enforcing patents in Cambodia is complex and lengthy. There is lack of sufficient expertise and human resources to carry out the patent examination at the relevant ministry.

- **Marks**

Trademark and service marks are defined as any visible sign capable of distinguishing the goods (trademark) or services (service mark) of an enterprise. According to this definition, non-visible marks, such as smell, sound, or taste, shall not be registrable. Even though the law is silent, three-dimensional trademarks can also be registered as long as they meet the statutory requirements of "distinctiveness." With the rise of e-commerce and cross-border trade, protecting marks has become crucial for businesses seeking to enter Cambodia's market.

- **Copyrights**

Copyright protection extends to literary, artistic, and scientific works, including software, music, literature, and architectural designs but exclude all laws, regulations, government circulars, court decisions, and their translations, as well as any idea, formality, method of operation, concept, principle, discovery or mere data, even if expressed, described, explained or embodied in a work. The Cambodia's Copyright Law safeguards the rights of creators and encourages creativity and innovation. However, the enforcement of copyright law remains a challenge, particularly in the digital sphere, where piracy and unauthorized use are prevalent. The relevant ministries should increase their resources, expertise and efforts to strengthen the protection of copyright and related rights as well as to combat infringing acts.

- **Industrial designs**

An industrial design may be any composition of lines or colours, or any three-dimensional form, or any material, so long as it gives a special appearance to a product of industry or handicraft. This special appearance must be judged visually; hence non-visual characteristics – such as the smell or touch of a material – are not protected. Like other areas of IP, Industrial design also faces its own challenges. The main challenge is regarding the limited resources, including personnel and expertise within enforcement agencies.

- **Geographical indication**

In Cambodia, Geographical Indication (GI) refers to the name, sign, and/or other distinctive symbols used to designate or represent the geographical origin of goods. These indicators serve to identify products originating from a specific geographical area where the quality, reputation, or other characteristics of the goods are linked to that origin. Although Cambodia may have laws and regulations in place to protect geographical indication, the effectiveness of these instruments in practice may vary, and there could be gaps or inconsistencies in the legal framework.

- **Plant variety**

The Law on Seed Management and Breeder Rights, which came into force in 2008, enables Cambodia to protect newly developed plant varieties. A new plant variety is defined as one recently discovered and developed by plant breeders, and it can be broadly protected for a specific period. However, due to the lack of awareness among plant breeders, farmers, and relevant authorities, this posted as a challenge about the importance and benefits of protecting the plant variety rights.

III. Challenges and Opportunities

Notwithstanding the notable progress regarding the enact of new IP laws and regulations in Cambodia, we can still see several challenges in practice. Most of the challenges include the lack of resources and capacity for effective enforcement, public awareness, active involvement from the government, and the unstoppable flow of counterfeit goods and piracy.

However, amidst these challenges, opportunities abound for businesses operating in Cambodia's dynamic market. The country's young and increasingly affluent population presents a growing consumer base hungry for innovative products and services. By strategically leveraging intellectual property rights, businesses can differentiate themselves in the market, build brand equity, and secure a competitive advantage.

IV. Moving forwards

As Cambodia continues its journey towards economic development and integration into the global economy, the protection of IP rights will play a pivotal role in driving innovation, attracting investment, and fostering sustainable growth. While challenges persist, proactive engagement and collaboration between stakeholders can pave the way for a more robust and effective IP regime in Cambodia. Technology integration could also play an important role and act as a powerful tool to overcome challenges.

Investing in digital solutions such as automation, data analytics and remote collaboration tools can enhance efficiency and resilience. Moreover, collaboration across departments and sectors can also lead to innovative solution and shared resources between the government institutions to tackle issues effectively. By embracing best practices and seizing opportunities, businesses can harness the full potential of IP to thrive in Cambodia's dynamic business environment.

Sihanoukville's recovery and tax incentives – treating the disease and not the patient?

By Clint O'Connell
Tax Partner, DFDL Cambodia

"The good physician treats the disease; the great physician treats the patient who has the disease."

Sir William Osler[1]

Twenty-five years before he was elected president, a certain D.J. Trump appeared at Capitol Hill to complain that Congress had closed too many tax loopholes for the real estate industry[2] ;

"Real estate really means so many jobs… you create so many other things. They buy carpet. They buy furniture. They buy refrigerators. They buy other things that fuel the economy."

Trump of course famously benefited from a 40-year negotiated property tax abatement when building the Grand Hyatt in New York which at the time was recovering from a painful fiscal crisis. The Trump abatement cost New York City over USD$400 million[3] in forgiven, or uncollected, taxes, on a property that cost only USD$120 million to build in 1980.

Cut to Sihanoukville, located in Preah Sihanouk Province Cambodia, in 2024 and we find ourselves in familiar territory. A province and city experiencing difficult fiscal times following a recent surge of primarily Chinese led investment in real estate driven by the legalization of the gambling sector that resulted in a short-lived boom period for the construction of casinos and hotels. This all came to a crashing halt with the ban of online gaming in 2019 quickly followed by the outbreak of Covid-19 leaving buildings half-finished and an exodus of Chinese businesses.

1 https://guides.library.uab.edu/Osler
2 https://www.nytimes.com/2020/10/30/business/trump-taxes-real-estate.html
3 https://www.nytimes.com/2016/09/18/nyregion/donald-trump-tax-breaks-real-estate.html

Conservative estimates put the current number of unfinished buildings in Sihanoukville at around 360[4] requiring over USD$1 billion to complete.

Targeted Tax Incentives

In January 2024 the recently elected Royal Government of Cambodia introduced a special program[5] to promote investment in Preah Sihanouk Province ("the Program"). The Program traces its origin to the ambitious Pentagonal Strategy-Phase I[6] that is the policy centerpiece of Prime Minister Hun Manet the Vice-President of the ruling CPP party. One of the stated goals of the Pentagonal Strategy is the concept of developing a specific region into an engine-room for economic growth for the whole country.

Preah Sihanouk Province with its deep-sea port, expressway, airports, and natural resources has been prioritized under the Pentagonal Strategy with the objective of accelerating the multi-purpose special economic zone ambitions that have been laid out for the province.

The Program provides targeted tax incentives for three (3) categories of investment projects or business activities located in Preah Sihanouk Province as follows:

(1) Investment projects/business activities relating to unfinished buildings re-starting in 2024.

(2) Investment projects/business activities not related to unfinished buildings starting in 2024.

(3) Expansion of existing investment projects/business activities starting in 2024 based on specific criteria.

With respect to category one, above, the tax incentives comprise of:

4 https://www.khmertimeskh.com/501378991/a-city-transformed-over-1000-high-rise-buildings-built-or-in-progress-in-sihanoukville/
5 https://www.phnompenhpost.com/business/special-incentives-revitalising-p-sihanouk/
6 https://www.mfaic.gov.kh/files/uploads/1XK1LW4MCTK9/EN%20PENTAGONAL%20STRATEGY%20-%20PHASE%20I.pdf

- An additional three (3) years of corporate tax exemption for existing Qualified Investment Projects (QIP) and tax registered SME's.
- An exemption of corporate tax for three (3) years for registered taxpayers that do not qualify as QIP.
- An exemption of Value-Added Tax on local supplies.
- An exemption of withholding tax on rental property for five (5) years.
- An exemption for unpaid Immovable Property Tax and associated penalties for the period 2016-2025.

Tangible Benefits?

A deep dive into the tangible benefits of the tax incentives provided under category one above provides more questions than answers. The QIP's that currently exist in Preah Sihanouk Province would have predominately registered under the previous Law on Investment and its implementing Sub-Decree under which casino activities, real estate development, hotels classified below three (3) stars did not qualify for QIP incentives[7] . Given that Sihanoukville wants long-term investors who will need to be in the Cambodian market for some time a three-year corporate tax exemption may not be enough to whet the appetite of cautious investors given the current market conditions.

The exemption of Value-Added Tax on the purchase of products from local supplies echo's the new incentive provided under the 2021 Law on Investment[8] which already exists for QIP's in Preah Sihanouk Province and provides practically just a timing benefit for construction entities who may have upfront cashflow issues. Ironically the VAT incentive provided under the new Law on Investment and the Program should not even need to be in place if Cambodia already had a robust and functional VAT refund mechanism.

The exemption of withholding tax on rental for five (5) years does not practically help developers. Most developers, or building operators, who would complete unfinished buildings in Preah Sihanouk Province would, or should, be tax registered meaning that when they issue tax invoices for rent to tax registered tenants there would be no applicable withholding tax.

For those unregistered property owners dealing with tax registered tenants the practice has been for some time to pass the cost of the withholding tax, incorrectly, to the tax registered tenant. For example, a lease agreement structured on a net basis for USD100 per month would require the tax registered lessee to pay USD100 to the lessor in addition to paying a non-deductible USD10 withholding tax to the tax authority. Practically it is the tenant who may benefit from the withholding tax on rental exemption not the actual property owner/lessor that it was designed for.

For a comparative analysis on immovable property taxes, it should be noted that when D.J Trump was negotiating his tax abatement in New York in the 1970's that city's annual property tax rate was in the region of USD$8-$9 per USD$100[9] of assessed value. The current annual rate of immovable property tax in Cambodia is 0.1% or USD0.10 per USD100 of assessed value.

The Goldilocks Doctrine

In medical terms treating the patient rather than the disease means considering what's important to the individual patient and keeping that in mind when deciding how to proceed. Arguably the current tax incentives provided for unfinished buildings in Preah Sihanouk Province provide a short-term mask for the symptoms but not actually addressing the underlying needs of the patient.

Investors require long-term certainty with respect to tax particularly if they are investing heavily in brick and mortar in a foreign jurisdiction. The basic premise for policy makers as per the frequently touted goldilocks doctrine is to get the mix just right – not too hot and not too cold. A too liberal approach by policy makers on tax could result in a D.J Trump scenario whereby the government loses out on millions of dollars of revenue. A too restrictive policy may end up scaring off would-be investors from returning.

Alternative options for consideration to the current tax incentives on offer could include pre-negotiated taxes for a long-term period, advance tax rulings (a concept used particularly in transfer pricing for related party transactions), exemptions of taxes on profit repatriation

7 Annex I of Sub-Decree No. 111 ANK/BK dated 27 September 2005 on the Implementation of the Amendment to the Law on Investment of the Kingdom of Cambodia

8 Article 27(1) of the Law on Investment, promulgated under Royal Kram No. NS/ RKM/1021/14, dated 15 October 2021

9 https://www.nyc.gov/site/finance/property/property-tax-rates.page

and comprehensive tax incentives on financing costs. Pre-negotiated taxes and rulings would remove the need for tax audits, and the inherent problems of uncertainty that they bring, while still ensuring that the Royal Cambodian government receives fixed tax revenues to go towards its annual budget needs.

Comparatively the current incentives on offer in Sihanoukville, whilst arguably fair, could be more attractive when compared to those historically provided by East African[10] , Pacific[11] or Middle Eastern[12] countries where investment in infrastructure and construction of commercial buildings has also been a necessity at times.

Compromises and solutions.

There is no doubt that Preah Sihanouk Province is on the right track to becoming an engine-room for economic growth in Cambodia. The focus and implementation on drafting a master plan to develop the province into a 'Model Multi-Purpose SEZ (Special Economic Zone) and develop Cambodia's coastal provinces into a multi-purpose and comprehensive economic corridor' will bear fruit in the foreseeable future.

In the current environment, with global economic uncertainty and fiscal restraint, to what extent will the current tax incentives on offer for unfinished construction encourage existing investors to restart their projects in Preah Sihanouk Province or for new investors to take over?

Constructing high-rise buildings in a foreign country is not something that investors take lightly and rather than looking at short-term tax benefits that may be at play most would be looking at the long game with a view to being present in-country for decades and not necessarily a few years.

While the incentives on offer in Sihanoukville are good start they don't seem to address the more pressing tax issues that face would-be investors coming to Cambodia. These issues include unpredictable tax audits, the omission of a truly independent tax tribunal and the lack of uncertainty regarding the interpretation and application of Cambodia's fast evolving tax regulations.

These issues will need to be addressed to make or break investors decisions on re-entering or entering the Sihanoukville market - not so much tax incentives that may mask the symptoms but may not provide a holistic look at assisting the patient.

10 https://actionaid.org/publications/2016/still-racing-toward-bottom-corporate-tax-incentives-east-africa

11 https://www.adb.org/sites/default/files/publication/939871/governance-brief-054-tax-incentives-investment.pdf

12 https://www.arab-reform.net/publication/which-tax-policies-for-lebanon-lessons-from-the-past-for-a-challenging-future/

Green, Social, and Sustainability Bonds in Cambodia: Status and Prospects in Q1 2024

by Varabott Ho
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Introduction

The Royal Government of Cambodia (RGC) is deeply committed to combating climate change and fulfilling its obligations under the Paris Agreement and the Sustainable Development Goals (SDGs). As the nation aims at significant climate adaptation and mitigation, financial strategies including Green Bonds are considered pivotal. Despite their potential, only a limited number of bonds have been issued, with none qualifying as Green Bonds, highlighting a major opportunity for growth and impact. The adoption of the Paris Agreement in 2015 marked a global consensus on reducing climate change effects, focusing on low-carbon initiatives such as Green Bonds. These bonds are part of a broader category known as Thematic Bonds, which fund projects with explicit environmental and social benefits. Despite their growing popularity, challenges such as high issuance costs and complex regulatory frameworks are notable, especially in emerging markets like Cambodia.

The International Capital Market Association (ICMA)[1] sets guidelines and standards for issuing bonds to achieve social and environmental objectives. In addition to the Green Bond Principles (GBP), which are designed for bonds financing environmentally friendly projects, ICMA has developed additional frameworks:

1. Green Bond Principles (GBP)[2] : a set of voluntary guidelines to promote transparency and integrity in the green bond market. These guidelines are designed to assist issuers, investors, and other market participants in ensuring that green bonds truly finance environmentally beneficial projects. Green bonds finance a wide range of environmentally friendly projects, with some of the key sectors being: Renewable Energy (solar, wind, geothermal, etc.), Energy Efficiency (building retrofits, efficient appliances), Sustainable Waste Management (recycling, waste-to-energy), Clean Transportation (electric vehicles, public transport), Sustainable Water Management (water efficiency, treatment), Land Use & Forestry (conservation, sustainable practices), Climate Change Adaptation (resilient infrastructure)
2. Social Bonds Principles (SBP)[3]: These principles guide the issuance of bonds specifically intended to finance projects with positive social outcomes, such as affordable housing, education, and healthcare.
3. Sustainability Bonds Guidelines (SBG)[4] : These guidelines assist issuers who want to raise capital through bonds that finance a combination of both green and social projects, thus supporting overall sustainability goals.
4. Sustainability-Linked Bonds Principles (SLBP)[5] : This set of principles is for bonds that are linked to the achievement of sustainability objectives that the issuer commits to meet. Unlike green or social bonds, which finance specific projects, sustainability-linked bonds are tied to the issuer's overall performance on sustainability targets.

The Current State of Green Bonds in Cambodia

While Green Bonds are a global phenomenon, Cambodia's market is still in its infancy. This is partly due to excessive issuance costs, lengthy approval processes,

1 International Capital Market Association (ICMA) https://www.icmagroup.org/ (ICMA, 2024)
2 https://www.icmagroup.org/sustainable-finance/the-principles-guidelines-and-handbooks/green-bond-principles-gbp/ (ICMA, 2022)
3 https://sustainable-infrastructure-tools.org/tools/social-bonds-principles-sbp/ (ICMA 2023)
4 https://sustainable-infrastructure-tools.org/tools/sustainability-bond-guidelines/ (ICMA,2021)
5 https://www.icmagroup.org/assets/documents/Sustainable-finance/2023-updates/Sustainability-Linked-Bond-Principles-June-2023-220623.pdf (ICMA, 2023)

and a nascent regulatory environment. However, these challenges are not insurmountable. Enhanced policy frameworks, alignment with international standards, and active collaboration among market participants could significantly improve the situation.

Green bonds and sustainability bonds are gaining traction in Cambodia as part of the broader effort to develop a sustainable finance market within the country. The Cambodian government and various organizations have initiated programs to support the issuance of these bonds, addressing both environmental and social projects.

In recent developments, two Cambodian private companies were the first for green and sustainability bond issuance in 2022[6] and 2023[7] .

- Golden Tree Co. Ltd[8] ., a real estate company in Cambodia, was supported in issuing its first green bond of USD $2.5 million. The proceeds from this bond are specifically aimed at green building development. The bond, which comes with a seven-year maturity and a fixed coupon rate of 7% per annum
- CAMGSM PLC[9] , also known as Cellcard, a leading telecommunications operator in Cambodia, issued the country's first-ever sustainability bond of USD $20 million on November 24, 2023. The proceeds from this sustainability bond are designated for improving Cellcard's network and infrastructure, particularly focusing on renewable energy projects and expanding connectivity to underserved communities. The bond, which comes with a ten-year maturity and a coupon rate that is higher of SOFR plus 3% or 5.5% per annum, was fully subscribed by major institutional investors like Manulife and Prudential, with a 100% guarantee from GuarantCo.

Moreover, the Cambodia Sustainable Bond Accelerator Program[10] was launched to expand the green and sustainable bond market. This initiative is backed by partnerships with international bodies like the United Nations Economic and Social Commission for Asia and the Pacific (UNESCAP) and the Global Green Growth Institute (GGGI), CGIF or Credit Guarantee & Investment Facility (ADB), and GuarantCo (part of the Private Infrastructure Development Group or PIDG).

The Securities and Exchange Regulator of Cambodia (SERC)[11] plays a significant role in promoting and regulating the issuance of these bonds. Guidelines and frameworks have been set up to ensure transparency and integrity in the issuance process, which includes clearly defining the use of proceeds, assessing, and selecting projects, managing proceeds, and mandatory reporting on the impacts and outcomes of the funded projects. These efforts are complemented by tax incentives for issuers and a push to attract national and international investors to participate in Cambodia's burgeoning green and sustainable bond markets.

The Role of Universities

Universities are uniquely well positioned to contribute towards the development of the Green Bond market in Cambodia. They can provide research support, professional training, and certification programs that are crucial for capacity building. This involves not only academic curriculum development but also partnerships with financial institutions and government bodies to ensure that the educational offerings are practical and relevant. For instance, CICERO[12] , was an independent research center founded in 1990 by the Norwegian government, focusing on interdisciplinary climate research and environmental studies in Norway. Affiliated with the University of Oslo, CICERO tackles climate challenges and climate finance through research and collaboration with the public and private sectors. They have been actively involved with the IPCC since 1992 and their "Shades of Green" business was acquired by S&P Global Ratings in 2022[13] . Through this acquisition, S&P ambitions to further expand its expertise as second-party opinions (SPOs) for the GSS+ Bonds.

The primary challenges include limited understanding and recognition of Green Bonds, a need for standardized procedures, and a lack of technical expertise (Ho, 2023)[14]

6 https://www.khmertimeskh.com/501222765/golden-tree-announces-first-green-bond-official-listing-on-csx/ (KT, 2022)

7 https://www.khmertimeskh.com/501384050/cambodias-capital-market-promotes-sustainable-financing/ (KT,2023)

8 http://csx.com.kh/company/announce/viewPost.do?MNCD=5040&postId=1491 (CSX, 2022)

9 http://www.csx.com.kh/news/notice/viewPost.do?MNCD=8020&postId=577 (CSX 2023)

10 https://gggi.org/gggi-unescap-and-serc-sign-moa-and-launch-the-cambodia-sustainable-bond-accelerator-program/ (GGGI, 2023)

11 https://www.adb.org/sites/default/files/publication/827631/green-bond-market-survey-cambodia.pdf (ADB, 2022)

12 https://cicero.oslo.no/en (CICERO, 2024)

13 https://www.spglobal.com/ratings/en/products-benefits/products/shades-of-green (S&P, 2022)

14 https://cam-ed.edu.kh/capacity-building-in-green-bonds-in-cambodia/.

. On the other hand, opportunities lie in leveraging academic institutions as hubs for innovation and knowledge dissemination, which can play a transformative role in the finance sector, especially in emerging markets.

Recommendations

1. Policy Enhancement: Develop a clear and consistent policy framework for Green Bonds, aligning it with international practices to enhance credibility and attract global investors.
2. University Involvement: Integrate sustainable finance into university curricula and establish specialized training programs to equip stakeholders with the necessary skills.
3. Public-Private Partnerships: Encourage collaborations between universities, government, and the private sector to foster innovation and practical learning.
4. Awareness and Advocacy: Universities should actively participate in public awareness campaigns to highlight the benefits of Green Bonds and sustainable investments.
5. Research and Development: Continuous research is needed to monitor Green Bonds' impact and innovate new financial instruments that support sustainable development.

Conclusion

While Cambodia's green bond market is young, it's showing positive signs. The recent issuances by Golden Tree and CAMGSM demonstrate a growing interest in financing environmentally and socially sustainable projects. The Cambodia Sustainable Bond Accelerator Program, along with clear regulatory frameworks from SERC, is contributing to a more supportive environment for future issuances.

However, challenges remain. Limited public awareness, standardized procedures, and technical expertise need to be addressed. Universities can play a pivotal role by providing research, training, and knowledge dissemination to bridge these gaps.

Overall, Cambodia's green social, sustainability (GSS) bond market holds significant promise for achieving sustainability targets and fostering sustainable economic growth. Through continued policy improvements, university involvement, and public awareness efforts, Cambodia can unlock the full potential of GSS bonds.

The potential of GSS+ Bonds in Cambodia is immense but underutilized both in the private and public sectors. For example, according to the Ministry of Environment (MoE), and National Council for Sustainable Development (NCSD) on Cambodia's Nationally Determined Contribution (NDCs[15]), the total funding requirement for climate mitigation is approximately US$ 5.8 billion (forestry, land use, waste, and energy) and total funding required for adaptation actions is over US$ 2 billion (infrastructure, water, and agriculture). The NCSD also stated that without investment in adaptation, climate change could cost Cambodia 1% of GDP every year by 2030, and all economic growth could be wiped out entirely due to climate change impacts by 2050[16].

With strategic policy adjustments and the active involvement of academic institutions in capacity building, Cambodia can pave the way for a robust Sustainability Bond market. This will not only help in achieving environmental targets but also in fostering economic growth through sustainable investment and enriching the sustainability ecosystem.

DOI: https://doi.org/10.62458/CamEd/OAR/ACBSP/73-86 (CamEd, 2023)

15 https://ncsd.moe.gov.kh/resources/document/Cambodia_NDC_Updated (MOE, 2020)

16 https://www.khmertimeskh.com/37807/cambodia-needs-to-seize-the-opportunities-in-climate-finance/ (KT, 2016)

The Growing Scope of Central Bank Mandates - Lessons for Cambodia

By Pat Beck
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Raison d’être - Public Finance

Throughout history, central bank mandates have evolved. Generally, these adaptations involve an increase in the scope of the aegis of the institution evinced through the refinement and addition of tools central banks possess. However, the arguments for the creation of central banks began with a need to help facilitate the funding and marketing of sovereign debt. Public debt management remains a central tenet of central banks today. In this early period, central banks were also tasked with issuing currency. Yet, over time, the banks began to be issued a wider range of responsibilities. (Redish, 2012)

Financial Stability

In 1793, a series of bank runs in England commenced as liquidity was tight during England’s war with France. It was then that Sir Francis Baring began calls for the central bank to act as a lender of last resort by assuming liabilities of retail banks in order to promote financial stability in tumultuous times. The concept that a central bank is the lender of last resort has persisted to this day. (Jones, 2023) In 1873, Walter Bagehot, the famed journalist and editor of The Economist, called for central banks to impose high rates - known as penalty or discount rates - against quality assets commercial banks held should they avail themselves of the assistance of the lender of last resort. (Le Maux, 2011) This was an attempt to incentivize banks to explore alternative funding options in private markets before appealing to the central bank for assistance by charging a rate that was higher than the prevailing private market rates between banks.

Bagehot’s ideas would act to limit moral hazard as penalty-free lending rates would cause banks to be inclined to take excessive risks knowing that a central bank would bail them out from a position of insolvency due to liquidity mismatches and market panics when private market actors would be unwilling to do so.

And then there was gold - Stable currencies

Another series of banking crises beginning in the 1870s created a demand for central banks to maintain the stability of national currencies which beget a long period known as the gold standard. Central bankers were tasked with maintaining the convertibility of their nation’s paper-based money to a fixed amount of gold. Furthermore, this required central banks to actively attempt to manage their currency’s exchange rate with other nations. This system, however, produced contractionary policies and fueled deflation as central bankers were forced to contract the money supply to keep the value of their currency on par with a limited supply of gold. The system resulted in instability again as inherent flaws that limited both liquidity and thereby economic growth proved ineffective when large spending and deficits took place in the lead up to World War I. Further, politicized central banks began to limit or halt the conversion of foreign money within their country and suspended the export of bullion to neighboring states that attempted to exchange their holdings of foreign currency. Central banks also engaged in rounds of currency devaluations in attempts to boost the attractiveness of their exports. Many nations experienced wild exchange rate fluctuations and inflation and the discount rate was revisited as a tool to try to stall rampant inflationary pressures of the time. Towards the end of World War II it became clear that currency stability was not enough to produce systemic stability.

Macro stability and policy:

International commerce became too risky as large exchange rate fluctuations, price changes, and the inconvertibility of foreign currencies made predicting trade gains or losses based on future dates uncertain and undercut one of money's main roles which is to act as a medium of exchange. Additionally, pressures to devalue one's own currency damaged the role of money as a store of value and made holding foreign reserves risky. To help restore macro stability of the monetary system and confidence in the banking system, the Bretton Woods Conference was held in 1944 where the US dollar was fixed to the price of gold at $35/ounce and member countries' central banks agreed to hold the value of their home currency to a pegged rate with

the dollar. It was at this time that maintaining a fixed exchange rate became paramount for central bankers and inflation was kept in check by tying the US dollar to a fixed amount of gold. Eventually, this became an unsustainable position with the number of US dollars exceeded first, the value of the total holdings of gold by the US and then eventually the value of gold on Earth.

Therefore, in 1971 President Nixon suspended the convertibility of US dollars into gold at $35/ounce and signified the end of both the Gold Standard and Bretton Woods Era.

Following the demise of Bretton Woods, the world has experienced a series of banking and financial crises with some of the more notable being the Mexican Peso/Latin American Debt crisis, the US Savings and Loan crisis, the collapse of the Japanese asset bubble, the Asian Financial Crisis, the Russian, Turkish, and Argentine crises, the Global Financial Crisis, and the European Sovereign Debt Crisis. (Reinhart & Rogoff, 2009) This period of time witnessed new effects of a more globalized and interconnected banking system. Culminating with the Global Financial Crises, central banks began to coordinate policy across borders and expand their toolbox further. (Goodheart, 2011)

Things get unconventional:

To respond to these challenges, central banks began acting in new ways known as unconventional monetary policy. The Bank of Japan began experimenting with quantitative easing and direct asset purchases, the European Central Bank followed suit and extended the duration of bond issuances, collectivized sovereign debt financing, and expanded supervisory powers. The US FED established currency swaps, Repo agreements, directly bailed out financial institutions, provided foreign guidance, purchased assets and so on. (Bordo, 2022)

Most recently, central banks are contending with large debt burdens and rising interest rates and have responded by transforming into the de facto provider of liquidity of first resort. This can be seen most readily by US FED actions following the Silicon Valley Bank and First Republic panics and by the People's Bank of China signaling that it will engage in open market operations for Treasury Bonds and for pushing for more swap lines. Further still, the European Central Bank has made this shift explicit by adopting a new "Operational Framework" in March of 2024 that explicitly focuses on providing liquidity. In other words, although monetary policy is still the role of central banks, providing market liquidity has presently taken center stage for central banks. This appears to be the most important role for central banks now due to high levels of volatility in global markets, recent and impending bank failures, rising geopolitical uncertainty, financial sanctions, frozen foreign reserves, US-China decoupling, and rising holdings of gold reserves.

Lessons for Cambodia:

The National Bank of Cambodia's mission "to determine and direct monetary policy aimed at maintaining price stability to foster economic development" is broad enough in scope to be able to navigate these times. To ensure adequate resources to respond to the liquidity needs of the real economy, the NBC should direct banks and MFIs to create a self-financed bank deposit insurance scheme to avert market panics and to facilitate larger interbank swap lines at pre-negotiated overnight rates. This will create a more robust market with less need for intervention which reduces the implicit liabilities of the NBC. The latter point should prove to be incredibly important as quantitative tightening and rising interest rates limit heavily-indebted central banks' abilities to pursue unconventional policies.

Meanwhile, the supervisory powers of the NBC must be maintained to stave off any potential solvency issues before they arise. Forestalling de-dollarization will keep a larger pool of liquidity available to local markets during these tumultuous times and reduce the need for intervention. It is certain that the mandate of central banks will continue to evolve. Presently, the NBC should continue to be forward looking by remaining abreast on emerging trends to include green development objectives into central bank mandates, and to include any such duties within the current mandate set by the Royal government of Cambodia.

The Infant Formula Crisis in the United States: A Cautionary Tale of Regulatory Capture

By Alexander Franco, PhD
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In October of 2021, an infant formula plant in the state of Michigan in the United States was shut down by Abbott Nutrition after allegations that contamination in its products had caused the deaths of two children. As a result, Abbott also voluntarily recalled several of its infant formula products from the market. At the time, the company was producing approximately 40% of all infant formula in the country. This occurred as the nation was experiencing skyrocketing national out-of-stock rates in many sectors of the economy due to the COVID-19 pandemic. By June of the following year, about a fifth of the U.S. was witnessing out-of-stock rates of baby formula that exceeded 90%. Acute shortages would remain for all of 2022 and into early 2023. Panic buying and hoarding, with parents driving from supermarket to pharmacy, caused large-chain retail operations like Walmart, CVS, Target, and Walgreens to establish draconian purchase limits for customers.

The baby formula industry in the U.S. operates under a cumbersome matrix of governmental agencies that maintain tight regulations beyond the norm in the general food industry. The federal government's Food and Drug Administration (FDA) establishes rules and regulatory review on how formula is produced, stored, packaged, and labelled. This is complicated by the fact that baby formula is not generic but, rather, is especially produced to consider for food allergies, respiratory reactions, and other health considerations. The federal government's U.S. Department of Agriculture (USDA) oversees the Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) which operates through single-supplier rebate contracts for infant formula. In essence, this federal program is administered by state-level agencies throughout the fifty states to provide vouchers for low-income individuals to purchase a predetermined brand of infant formula. Beginning with only 100,000 enrollees in 1974, like most federal government programs, it grew to over six million enrollees by 2024, accounting for more than half of all the infant formula sold in the country on an annual basis.

The USDA provides federal money to the fifty states who then individually contract with one manufacturer each with the exclusive right to provide formula to WIC participants in that state. This created a blatant nexus of corporatism whereby the largest and most powerful of the formula makers, with powerful lobbyists and political action committees with campaign contributions, were able to obtain exclusivity arrangements that granted them monopoly status on a state basis. As a result, just three companies – Abbott, Nestlé/Gerber, and Reckitt/Mead Johnson, all with a total of only seven formula producing factories- came to hold all WIC contracts within the fifty states and to dominate the formula market. Abbott alone received exclusivity contracts for thirty-two of the fifty states.

This created a market concentration with serious vulnerabilities to economic shock and which resulted in adverse pricing at the retail level. With only seven factories among the three companies, the disruption of only one, as was the case with the closure of Abbott's plant in Michigan, could and did create an adverse wide-spread effect on production and consequential accessibility of the product to WIC and non-WIC consumers alike. The federal government granted monopoly status on a state-to-state basis to the three companies regarding WIC consumers (half of the market) who were only allowed use the government vouchers to make purchases from the designed company even if the sole company's brand was out of stock. In addition, WIC recipients could not make on-line purchases.

Ample and prime shelf space in retail outlets, coupled with the prestige and credibility of having their brand chosen by the government, allowed the monopoly-status companies to boost their sales to non-WIC consumers with marked-up pricing, thereby compensating for lower revenue from WIC voucher purchases. However, retailers came to experience that WIC reacted to increases in the general retail price of formula by increasing the face value of the vouchers. Over time, this also allowed wholesale prices to creep upward. Top administrators at the USDA accommodated price increases beyond inflation due to pressure from politicians rewarded by lobbyists. Others collaborated to seek eventual transition of employment in the companies they were regulating.

The dysfunctional regulatory structure of the WIC program extended to tariff barriers regarding the importation of foreign infant formula. The federal government imposed a base tariff of about 15% to 17.5% on imported formula which was also subjected to tariff-base quotas operationalized within a complex system based on quantity thresholds. As a result of this protectionism, approximately 98% of all infant formula consumed in the United States has been domestically produced. During the COVID-19 pandemic, the federal government was slow to distinguish the infant formula shortage from shortages of other products as a result of disrupted supply chains. However, media outlets widely reported that parents in the United States were crossing the U.S-Mexico border to purchase formula in municipalities on the Mexican side, such as Tijuana, Cuidad Juárez, and Matamoros, where inventories of infant formula were in ample supply due to more liberal policies on importation, particularly from Europe.

Despite its trade restriction policy, in May 2022, under pressure to act, the Biden Administration invoked the Defense Production Act (a relic of the Cold War period) to be able to utilize military aircraft and to commandeer civilian aircraft to conduct *Operation Fly Formula*" which imported over 100 million bottles of foreign-made infant formula (about the same amount that is typically sold over two days in the U.S.), mostly from Europe and Australia. In addition, in July of 2022, the U.S. Congress, under heavy public pressure and with much fanfare, suspended tariffs on imports of certain foreign formula and, later, on formula base powder. However, the tariff liberalization legislation was short-lived, quietly expiring on December 31 of 2022 with WIC reverting back to the status quo of maintaining an oligopolistic market structure.

The lack of competition within the infant formula industry, due to government-sanctioned monopolies at the state level, was exacerbated by highly restrictive non-tariff barriers with a protectionist orientation. The federal government's Food and Drug Administration (FDA) imposed strict regulations pertaining to the manufacture (including nutrient content), labelling, and distribution of formula, as well as standards for quality control in production facilities. This significantly discouraged new entries into the U.S. formula market from potential domestic and foreign competitors due to the high costs caused by excessive regulations. Under FDA dictates, infant formula from the European Union (EU) cannot be imported into the U.S. for commercial use and is only allowed to be imported through third-party delivery services for the intent of personal use, not sale. This is despite the fact that scrutiny on the production and distribution of infant formula in the EU is equal to standards in the U.S. and that the EU's infant mortality rate has consistently recorded tendencies of being lower than that of the U.S.

What Should be Learned From the Infant Formula Crisis?

In March of 2024, the federal government's Federal Trade Commission (FTC) issued a report on the infant formula industry, suggesting liberalization in certain aspects of existing government regulation but did not recommend any liberalization as to existing tariff policies. In addition, the FTC report also discussed the possibility of creating a new office within the FDA exclusively for specific oversight of the infant formula industry. However, any of these reforms can only take place through legislative action by both chambers of the U.S. congress and, before that, such reforms would have to survive a long gauntlet of congressional hearings being conducted by lawmakers under the heavy influence of corporate lobbyists and their ties to political campaign contributions.

Lost in the limited public scrutiny of the infant formula crisis was any revelation of the actual culprit: regulatory capture through corporatism. Regulatory capture was best articulated by Nobel laureate economist George Stigler who noted that, though their collective wealth, large corporations are able to control the regulatory agencies created to oversee their industries by influencing legislators who pass laws that create and fund the regulatory review frameworks. The process of capturing is conducted through well-financed lobbyists and political campaign contributions given to these politicians. Influence is also exerted over the agencies themselves by way of offering top administrators, with the specialized and insider knowledge they acquire, to accept lucrative employment in the government affairs office or other employment within the incumbent corporations. As a result, the captured agencies then focus on benefitting those they are supposed to regulate.

Corporatism, as a macroeconomic phenomenon, is a form of statism and is not capitalism or even a variant of capitalism. It is an amalgam of elite corporations and government where political means within regulatory cartelization are utilized to benefit those corporations with taxpayer bailouts, infrastructure subsidies, state-enforced restrictions on competitive entry, and the socialization of an array of corporate costs (e.g., state subsidization of research and development, international marketing, physical protection of assets abroad, and the externalizing of other operating expenses).

In its limited coverage of the infant formula crisis, the fourth estate in the U.S. failed to focus an urgently needed spotlight on corporatism and its consequences. Instead, the legacy media characterized the infant formula industry as yet another sector of the market victimized by disrupted supply chains and crippled distribution channels brought on by the COVID-19 pandemic. It was mostly the independent (non-corporate) media that pointed out that the trade-restricted infant formula crisis seemed deeper and more prolonged than the distortions in other market sectors dealing with more freely traded products. The legacy media's focus was driven by two main factors: Firstly, it is largely populated by egalitarians who could not risk drawing criticism or scrutiny of a government program supposedly catering to vulnerable low-income families with infants – the ideal recipients for those advocating a robust welfare state. Secondly, with a dwindling viewership as more news seekers turn to a splintering nexus of often ideologically tribalized outlets in social media, the legacy media has become increasingly hesitate to confront any large corporation (but especially in Big Pharma) for fear of losing already declining advertising revenue.

The infant formula industry remains today as fragile as before the COVID-19 crisis. A single disruption can again have an industry-wide effect. The state-facilitated cartelization of the industry has concentrated decision-making to an elite few where price fixing has replaced price determination by the spontaneous order of the market. The continued interventionist measures applied through corporatism will preserve an inability to enact rapid response to future economic shocks and to guarantee open, fair, and robust competition in the infant formula industry.

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Illustrative drawing on the front cover by Dr. Virak Prum

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