



MEETING THE COSTS AND MAXIMIZING THE IMPACT OF SOCIAL PROTECTION IN CAMBODIA

EXECUTIVE SUMMARY

FINDINGS AND RECOMMENDATIONS

Cambodia's engagement in Public Finance Management reform has led to significant progress in resource mobilization and budget execution and resulted in the restoration of budget balance. In 2018, the public budget surplus was equivalent to approximately USD 150 million. This amount is sufficient to substantially close the poverty gap, if used to cover the costs of social safety nets. **This report estimates that the current surplus, before the pandemic, represents more than double the amount required to bring the share of Cambodians living in poverty below 3%.**

Analysis of household livelihoods presented here finds that:

- For National Social Protection Policy Framework (NSPPF) schemes to allow for sizeable poverty reduction, a transfer size equivalent to 20% of the poverty line would be needed.**
- Categorical transfers require higher budgets for poverty reduction rates that are equivalent to safety net programmes that would deliver a basic *social protection floor*. **The most economically efficient use of public funds would therefore be a safety net scheme that accounts for household size, or a scheme that complements these transfers with categorical allowances.**
- While categorical transfers offer some targeting advantages over safety net schemes, they risk leaving segments of the poor without financial support. **Graduation-based interventions, which involve the transfer of assets and skills as opposed to cash alone to poor working-age households, would effectively serve these populations not targeted by NSPPF policies.**

- Graduation programmes are designed to enable extremely poor households to generate their own income streams by addressing the root causes of their economic exclusion. This report finds that the potential socio-economic impacts for the targeted groups are substantial.
- Regardless of the modalities of Cambodia's social assistance system, **the report estimates that it will cost approximately USD 80 million to reduce the incidence of poverty by half. This requires an increase in public expenditures of just below 0.5% of GDP**, bringing total social spending to 1.4% of GDP, a proportion which is still below the global average.

General equilibrium analysis presented in this report, confirms these findings and shows the wider economic benefits of social protection interventions. It also illustrates the potential benefits of skills and productive asset transfers. **Combining social transfer policies with graduation-based interventions can stimulate the local economy and boost employment.** Given the productivity and multiplier effects, income generation from graduation interventions compensate for the lower level of transfers received by some in the programme. Our macroeconomic **results show that these social protection policies, irrespective of their modalities, would not weaken economic growth processes, even if fully tax-funded.**

This set of **findings indicates that Cambodia has sufficient fiscal space to create a comprehensive system of social safety nets.** Moreover, it confirms Cambodia's ability to engage in effective redistributive policies without compromising budget balance or economic growth.

A *COVID-19 Update*, which follows, further accounts for the added complexity of the COVID-19 crisis on social protection policy progress in Cambodia and addresses how the report's findings can help address these new challenges. First, the emergency cash transfer programme follows the most economically efficient social protection modalities outlined in this

report. This suggests the increased relevance of the report's findings and allows for its use beyond policy recommendations to support the evaluation of policy effectiveness. Second, the emergency cash transfer programme provides safety nets above the 20% threshold of the national poverty line identified in this report. Thus, even if temporary, this programme promises to achieve significant poverty reduction in both rural and urban settings. **For as long as it lasts, the new emergency social protection scheme in response to COVID-19, could lift over one million Cambodians out of poverty and improve the livelihoods of many more.** This represents an unprecedented political stance and institutional progress towards more permanent and ambitious programmes, including towards the establishment of a social protection floor.

Building a modern and comprehensive social protection system requires long-term vision and strong political commitment. It necessitates a willingness to promote social cohesion, reduce inequality and guarantee every citizen a decent living condition. This study provides empirical evidence that these aspirations are within reach of the Royal Government of Cambodia and demonstrates the affordability and efficiency of tailored social assistance interventions, should they be met with political will.

CONTEXT

Cambodia has achieved impressive rates of economic growth over the past 15 years and kept income inequality in check. As a result, poverty has fallen dramatically. While half of the population was living in poverty in 2007, this figure is estimated to have fallen below 10% by 2016. **Vulnerability to shocks, however, has risen, and harder to reach pockets of poverty have also emerged. The development of social assistance has been slow and there is no effective Social Protection Floor¹ for Cambodians living in poverty.**

The NSPPF was approved by the Council of Ministers in March 2017 in response to these pressing needs. The proposed social assistance component of the framework consists of categorical transfers to the poor with a focus on select vulnerable groups: the elderly, people living with severe disabilities, expectant mothers and those with young children, and primary and secondary school students. The Framework demonstrates foresight and clear political commitment.

¹ *Social protection floors* are nationally defined sets of basic social security guarantees that should ensure, as a minimum that, over the life cycle, all in need have access to essential health care and to basic income security which together secure effective access to goods and services defined as necessary at the national level (adopted at the General Conference of the International Labour Organization 2012).

However, it does not plan for the development of a national *social protection floor* or to ensure coverage of a sizeable share of the working age poor.

This prompts a series of questions, which this study seeks to answer. Does the Framework allow for adequate provision of social safety nets if fully implemented? What would be their benefit adequacy, given Cambodia's current income distribution? Could alternative measures be implemented to complement these programmes? And what are the potential costs of extending policies that improve coverage of the population living in poverty?

These questions are intrinsically linked to the programme affordability and the allocation of public resources required to support the Framework. This study, therefore, focuses on the fiscal space needed to deliver a social protection system capable of tackling poverty and protecting the vulnerable.

It also analyses the economic benefits that would come from such investments. To do so, it compares the financial costs and economic impacts of the Framework's social assistance programmes both from a household perspective and from a wider economic angle. It further examines alternative pathways that may be considered as the NSPPF is rolled out.

COVID-19 UPDATE

NEW CONTEXT

We started this study at a time that was promising for social protection development in Cambodia. Government revenues were such that they could cover the cost of a social safety net for a large majority of the Cambodian poor. The Royal Government's adoption of the NSPPF as well as the rapid development of the IDPoor identification system opened the way for large scale safety nets implementation. Poverty incidence has fallen dramatically (this study estimated poverty was below 10% before the crisis), access to social services was rapidly progressing and economic growth was one of the fastest in the world, so much so that Cambodia became a lower-middle income country in 2015.

Over the past months however, the COVID-19 pandemic spread rapidly affecting virtually every country in the world, compromising the health of more than 10 million people and claiming more than half a million lives to date. Economies contracted at unprecedented scale, and in many places, lockdown measures have affected both production and employment, household demand collapsing for many services and goods, while trade and supply chains were disrupted. The livelihoods of millions are nowadays afflicted by unemployment and income loss soaring to record high levels.

In Cambodia, the health crisis did not take the proportion feared at the beginning of the pandemic and the mortality incidence remains among the lowest in the world, with 272 recorded cases and zero deaths (13th August 2020). Nonetheless, the socioeconomic dislocations, driven by very dramatic external demand shocks due to the collapse in export markets were large. Key production sectors driving growth, were substantially hit, causing income loss at

an unprecedented level. Tourism, construction, and manufacturing exports which have been the largest components and main drivers of economic growth for decades are nowadays the main recipient of the pandemic economic impact. These sectors account for over 70% of Cambodia's gross domestic product, 80% of its exports and generate the largest source of fiscal revenue. The collapse of external demand for these export goods and services as well as the slowdown in investment that affects the construction sector, have worsened employment and the income distribution, and threaten Cambodia steady progress on poverty reduction.

These sectors employ nearly 2 million workers, over 20% of Cambodia's labour force, a large share of which are low skilled and on low wages. Income loss resulting from the contraction of these sectors therefore threatens the livelihood of a significant number of already vulnerable households. Spill-overs and multiplier effects from this economic shock could dramatically affect the incidence of households unable to meet their subsistence needs.

In this context, the need for emergency interventions and policy packages that mitigate economic recession and bring back the country on the path of recovery is substantial and unprecedented.

Globally, governments responded to the sudden economic recession with rescue packages for both private sector support and social protection. In many countries, these interventions include labour and income protection schemes both for transition period when employment is compromised and for those who lose their livelihood. Similarly, Cambodia engaged in a recovery plan that aims at tackling both symptoms

of the crisis. Its first component aims at restoring growth and mitigating the impact on the private sector, through investment and infrastructure development as well as support for structural change in key production sectors. The other consists of the protection of the most vulnerable and most affected Cambodians by

maintaining all existing social protection programmes and introducing the *Cash Transfer Programme for Poor and Vulnerable Households during COVID-19* based on the IDPoor identification system, including the *On Demand IDPoor* identification fast track update.

RELEVANCE OF REPORT OBJECTIVES AND METHODS

This report aims at providing evidence for efficient design and implementation of such social safety nets. It explores avenues to expand the current Cambodian social protection system. To do so, it evaluates and compares policy options through the review of several potential schemes providing social transfers and protecting livelihood for Cambodia's poor.

Using recent national household surveys and national account data, this study is based on the analysis of the demographic and the socio-economic characteristics of the Cambodian population, living costs and consumption patterns. We estimate the adequacy of the social transfers given these elements and evaluate the cost of a range of social protection interventions, both expanding the current system and developing new complementing strategies. We also review public financing options for these policies. We then adopt a macroeconomic perspective on the impact that these

interventions are likely to have on the local and wider economy, considering their effects on both economic growth and income distribution.

The relevance of this report was primarily grounded on the need for safety nets for a part of the Cambodian population that was not benefitting from fast economic growth as well as for population groups that were highly vulnerable to financial shocks and stresses. The new economic context resulting from the COVID-19 crisis makes this type of analysis even more pertinent and valuable as it amplifies both the need for such policies and the challenges to implement them. The report provides analytical tools and evidence to design and implement country-specific programmes which have been made even more necessary by the new socio-economic context and that are at the centre of the government rescue packages and recovery objectives.

RELEVANCE OF OUR FINDING TO TACKLE THE NEW CHALLENGES

A sudden increase in population needing social protection represents a challenge both in terms of targeting and identification of beneficiaries. It also requires an increase in financial resources which can be particularly challenging to mobilise swiftly even in non-crisis circumstances. The COVID-19 crisis is adding more complexity to such emergency policy process since government revenue is expected to fall by about 30% this year as the result of the contraction

of the economy. The simultaneous increase in funding needs and contraction of government revenue constitute a substantial policy challenge, which also makes the efficient use of public funding even more imperious.

To which extent can the report's findings help address these new challenges?

FINDINGS ON SOCIAL TRANSFERS

Initial reports on sector contraction and employment decline, even though difficult to precisely estimate at this stage, point to a significant deterioration of income and livelihood in Cambodia. In this report, we use the most recent household socio-economic surveys to analyse income distribution, as presented in Graph 1 in Section 1. Given the concentration of household just above the poverty line, this shows that a small income loss for households at the bottom half

of the distribution would lead to a surge in poverty incidence.

Households who have lost their income and became poor as the result of the COVID-19 crisis might not have been enrolled in the IDPoor registry. The national poverty lines used in our methodology is based on caloric anchor. This allows us to estimate transfer adequacy independently from enrolment in the pre-



existing IDPoor database. Therefore, even for larger number of poor households, the adequacy analysis of social transfers, which is a key element of policy design and efficiency, remain valid and could be used to tailor new poverty schemes.

Since April, the Royal Government of Cambodia has engaged in a substantial expansion of its poverty targeted cash transfers. The social protection programmes we analyse in this report include schemes identical to the ones currently implemented in response of COVID-19 crisis. The present report therefore analyses the potential impact of these specific interventions and show their effectiveness at tackling poverty.

Two of our findings are particularly relevant to the current policy context. First, we find that one of the most economically efficient use of public funds consists of a social protection programme that accounts for household size, as well as schemes that complement lump sum transfers with categorical allowances. The emergency cash transfer programme follows this precise strategy, making our findings even

more relevant and our estimates more accurate than foreseen. Initially used for policy recommendations, our analysis could now also be used for effectiveness evaluation.

Second, we find that a transfer size of at least 20 per cent of the national poverty line is needed for the Framework's schemes to efficiently allow beneficiaries to meet their subsistence needs. Again, the emergency cash transfer programme provides safety nets above this threshold for most beneficiary households. Even if temporary, this programme promises to achieve significant poverty reduction and improve the livelihood of over 1.5 million Cambodian poor.

For as long as it lasts, the new emergency social protection scheme could, given its size and transfer modalities, lift over a million of Cambodian out of poverty. This represents an unprecedented political stance and institutional progress towards the establishment of a social protection floor. The key questions, however, are can and will this be sustained after the COVID-19 crisis has abated.

RELEVANCE OF GRADUATION PACKAGES

In addition to analysing conventional cash transfer schemes, we investigate the potential of multifaceted social protection tools called “graduation programmes”. They are designed to enable poor individuals to generate their own streams of income, addressing the causes of economic exclusion. These support programmes combine safety nets with the transfer of productive assets and the development of skills. Over 14 million individuals currently benefit from these livelihood improvement packages in Asia, Latin America and America and more than 34 governments are nowadays integrating these programmes into their social protection frameworks.

There are several reasons why these programmes could offer a potentially relevant complement to the current recovery strategy from the COVID-19 crisis. They aim at supporting local supply and demand

simultaneously, where trade or supply chains have been interrupted, for food staples but potentially also for a range of goods and services that could be produced locally. That would be particularly valuable to answer any supply restriction due to border closures and limit on internal movements. They also create new prospects for the integration of the poor into their local socio-economic fabric, enabling them to generate new income streams. A growing body of evidence shows their effectiveness to build resilience to financial shocks and stresses. In this study, we find substantial economic benefits not only at the household level, but also from a wider economic perspective as all economic indicators improved due to their multiplier effects. Those include agricultural production, household consumption, and growth, with long lasting effects beyond the duration of the programme.

MEETING THE COSTS OF SOCIAL PROTECTION

The second Section of the report analyses the affordability of social protection schemes, based on the findings from the costing evaluation. It shows that extensive progress on revenue collection and management generated a budget surplus sufficient to cover the costs of ambitious large-scale programmes before the COVID-19 crisis. However, government tax receipts are expected to decline by approximately 30% this year due to the contraction of sectors that are major contributors to the fiscal revenues. Therefore, the fiscal space for such policies has now changed and with it their affordability under the current year budget.

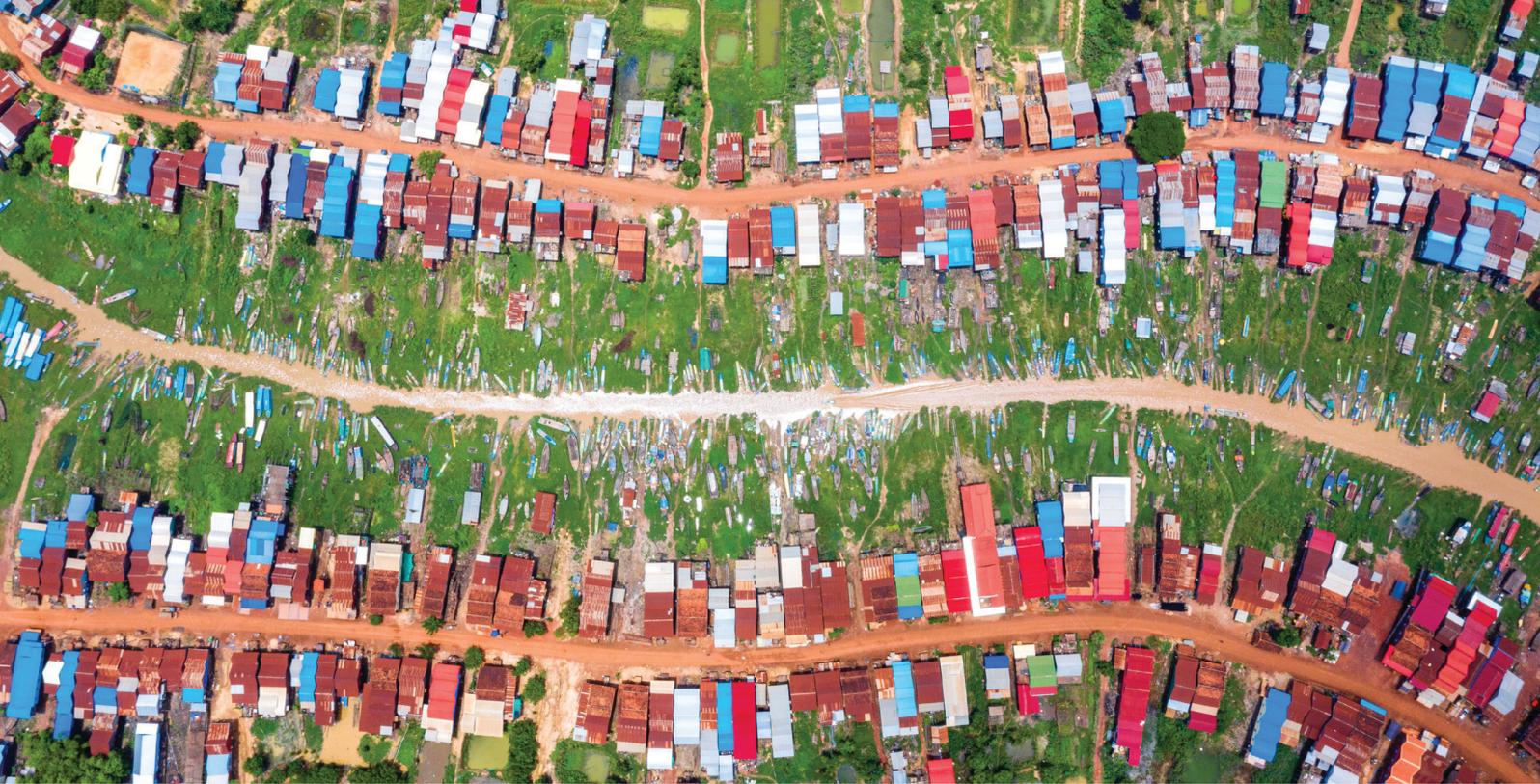
Nonetheless, two elements need to be considered. First, there are options that this report review to fund these policies on other sources than the current

year fiscal revenues. We present successful country experiences to develop such space in support of social protection programmes, which could inform alternative strategies relevant to the economic recovery period. Second, given that the economic crisis is mainly due to an external demand shock as well as the contraction of the construction sector, partly due to a decline in foreign direct investment, the Cambodian economy could bounce back as rapidly as external demand, especially with the support of the government rescue package. So the current and possibly next fiscal year could remain exceptional in compromising affordability. Cambodia’s experience in tax collection and revenue management should allow for effective budget restoring as the economy recovers from the COVID-19 crisis.

A MACROECONOMIC PERSPECTIVE

We use a general equilibrium model to analyse the impact of social protection schemes on the wider economy, looking at transmission channels and multiplier effects as well as measuring the effect on macro aggregates such as the GDP, trade, agricultural production, investment. We find that regardless of their modalities, the social protection programmes defined in the report would not compromise economic growth, even if fully tax-funded. These estimates are especially useful in the current context as they provide a benchmark for scaling up existing schemes.

Since the poor in Cambodia mainly consume domestic goods and services, their transfer-funded consumption is likely to stimulate their local economies and if scaled up to promote wider economic growth. In the current context of where demand is binding growth, this kind of direct support to households with this pattern of consumption is likely to help the Cambodian economy to recover and bounce back towards its pre-crisis growth path.



INEQUALITY AND SOCIAL COHESION

The COVID-19 crisis has demonstrated the importance of ambitious and adequate policies and effective governance. Countries where support policy packages have been swiftly adopted and support measures adequately designed to respond to the needs in a tailored way have been the ones that best mitigated the impact of the pandemic on their populations. While this was particularly evident for the safeguard of population health, it is now also well established for support to firms and private sector as well as social protection for affected populations be it in the form of income protection and safety nets, cash transfers and food vouchers for school pupils.

Countries that put in place efficient and generous income support are more likely to engage in a rapid recovery path because such policies support and restore distorted demand more swiftly, stimulating and boosting economic growth. The ones with the least generous social protection, wage protection schemes and unemployment insurance, appear more prone to delay economic recovery. Even when lockdown ends and social distancing eases - allowing domestic production to recover- depressed demand is likely to continue hindering economic prospects. In the case of Cambodia where the COVID-19 crisis is mainly caused by a demand shock, these emergency interventions have an especially strong potential for economic growth promotion.

The present report provides evidence that social protection policies do not have to come at the

expense of economic growth – on the contrary, holistic approach to social protection with a range of complementary schemes can promote economic progress and development. The more complex and multiple the causes of poverty, as they emerge from the current crisis, the more relevant multifaceted tools become. This report shows avenues for ambitious and innovative policy response, increasing the flexibility of schemes that are even more needed in the current context.

The COVID-19 crisis revealed how fragile economies can be. Social protection reinforces resilience and prevents inequality from widening. Without redistributive policies, unequal, socially fragmented and less resilient social fabric are likely to aggravate a crisis of unprecedented magnitude. And the longest the COVID-19 crisis is to last the more these mitigating policies will be needed to prevent social and economic effects to be durable.

In Cambodia, the COVID-19 crisis has been the catalyst for a large-scale development of its social protection schemes. Even if the emergency interventions remain limited in time and provide large scale safety nets for less than a year, they represent a political and institutional development that could pave the way for more permanent, effective and ambitious programmes. This would not only promote economic recovery but also open the way for the establishment of a social protection floor.