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Cambodia Is Hard Sell for Investment Companies

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PHNOM PENH — Douglas Clayton arrived in Phnom Penh in 2007 to start a [private equity](#) fund, looking to get \$100 million in funds under management. His firm, Leopard Capital, started in 2008, is one of four private equity funds here backed by overseas investors, and the first to have completed an investment.

“Anyone can announce they want to start a fund, but getting investors to back you is a challenge,” Mr. Clayton, Leopard’s chief executive and managing partner, said in an interview. “All the groups that started here had no track record, including us. It’s a doubly hard story to sell.”

Mr. Clayton was drawn to Cambodia after experiencing years of double-digit growth in Thailand, where he worked for a hedge fund during the 1990s.

Now ranked at 145 out of 183 countries in the [World Bank](#)’s “Doing Business” report, Cambodia is going through its own period of rapid growth. Before the global economic crisis hit in 2008, gross domestic product grew about 9 percent a year for almost a decade. After shrinking by 2.5 percent in 2009, growth is forecast to reach about 5 percent this year.

With \$34 million collected so far from an array of international investors, Leopard has completed six investments, including a \$2 million, 55 percent stake in Kingdom Breweries, a new microbrewery, and a 31.5 percent share in a recently built shrimp-processing factory. It has loaned about \$1 million to an electricity supplier in Kompong Cham Province, in eastern Cambodia.

The traditional private equity strategy of buying out and investing in profitable, pre-existing businesses is rarely an option here, Mr. Clayton said. “The biggest range of opportunities are the businesses that have not started yet.”

Still, in a country where everything is still to be done, “for people who are willing to come in and work very hard and be very entrepreneurial and blaze their own trails, Cambodia is a paradise.”

After decades of civil war and a deadly communist regime that between 1975 and 1979 killed 1.7 million people, Cambodia remains deeply underdeveloped, with four million of its 14 million people living below the poverty threshold, according to the [United Nations](#).

Leopard raised its first \$10 million before the financial crisis struck. Cambodia Emerald, a would-be rival, also started in 2008, was not so lucky.

As the crisis bit, “we sort of basically put the fund on hold,” Peter Brimble, founding partner of Cambodia Emerald, said recently. Still, U.S. investors are starting to show interest again, and “we have plans to bring it back,” he said.

Beyond the problems of attracting foreign capital, businesses here say they are confronted with numerous local barriers, the most frequently cited being the extremely limited access to domestic capital, and high transportation and electricity costs.

In 2008, Cambodian bank lending was worth about 25 percent of gross domestic product, compared with more than 90 percent in Vietnam and Thailand.

“Capital is one of the main constraints here,” said Joshua Morris, managing director of Emerging Markets Investments, a private development fund backed by the International Finance Corp. — the World Bank’s private arm — and the Norwegian and Finnish governments. Small and medium-size enterprises “struggle to raise the money they need for expansion,” he said.

Lending is limited by low confidence in the judicial system and a lack of credit information, investment managers say. Mr. Morris, whose \$10 million fund operates in both Cambodia and Laos, says he has been “incredibly careful” in identifying prospective business partners and has so far found just two in which he hopes to complete investments this summer.

Apart from their lack of access to cash, Mr. Morris said, Cambodian businesses rarely build proper corporate governance into strategies and fall short on accounting and auditing standards.

“While many businesses excel in generating revenue, there is still a lot of work that needs to be done in terms of the internal processes of the company,” he said. Skilled labor is also limited, although “a pretty solid set of business managers” is starting to emerge from the country’s universities, he added.

Yet, for all the shortcomings, Cambodia is at the heart of developing Asia, surrounded by dynamic economies in Vietnam, Thailand and Laos. Its currency, the riel, is pegged by the central bank at a stable rate of about 4,100 to the U.S. dollar, and inflation is low, at about 4 percent a year.

International road links are developing quickly, and last year Toll Group of Australia signed a contract to operate the long-neglected rail network, which is being rehabilitated. Toll says the first line, between Phnom Penh and the port city of Sihanoukville, will be open to freight by October.

“It’s a very pro-business government here,” Mr. Morris said. “They have placed very few restrictions with regards to where you can invest.”

“The private sector is our engine of economic growth,” Sun Chanthol, vice chairman for the Council for the Development of Cambodia, the government’s investment board, told a business seminar in Phnom Penh this month. “We want to be the facilitator of the private sector.”

Bretton G. Sciaroni, an adviser to the government and a partner at the law firm Sciaroni & Associates in Phnom Penh, said Cambodia had advantages that did not exist elsewhere in the region.

Foreign investors are allowed to own a company outright, without a local partner. There are no restrictions on fund transfers, no exchange controls, and Cambodia is one of the few least-developed countries to have joined the [World Trade Organization](#).

The government is also hoping to establish a stock exchange this year.

“Senior government officials are focused on attracting investment and creating jobs,” Mr. Sciaroni said. “In addition, because Cambodia is a relatively new country with a new economy, there are business opportunities that do not exist in more developed economies. Much needs to be done in Cambodia, and opportunity abounds.” Still, the cost of doing business is higher there than in many other countries in the region. Electricity costs are high because much of the energy is imported, while transportation is costly and slow because of poor infrastructure. Moreover, “the courts do not provide an adequate venue for commercial disputes,” Mr. Sciaroni said. “Dispute resolution remains an important issue for the business community.” Corruption is another problem. “Corruption exists at many levels and is sometimes only the manifestation of a former economy based on informal processes,” said Christophe Forsinetti, vice president of the [venture capital](#) fund Devenco. Yet, the fact

that Cambodia's development lags behind that of its neighbors means there is a higher growth potential as the country catches up, Mr. Forsinetti said. Devenco has invested in Gaea, a waste collection company in the main tourist hub — Siem Reap — and in Pharm@link, a Phnom Penh pharmacy chain. "Many sectors are underdeveloped and companies with a specific knowledge can become a leader on their market with small investment amounts," he said. "We therefore work on a smaller pie. But it is a growing one."