

RISK ASSESSMENT AND RISK MANAGEMENT PLAN

Risk Description	Risk Assessment	Mitigation Measures or Risk Management Plan
National Risks		
Macroeconomic instability and volatility delay the implementation of reforms	Medium	Macroeconomic risks to the economy appear to be well mitigated. During 2011–2013, the country’s GDP growth exceeded 7% each year, driven by solid performances in industry, services, and agriculture. Foreign direct investment has played an increasingly important role in industrial development, reaching \$1.2 billion in 2013. The influx of investment is supporting the rapid structural transformation of the economy from low value-added activities in traditional growth areas (garments, tourism, construction, and low-yield rice paddy production) to integration into higher value-added global supply chains, including new (e.g., auto parts and electronics) and agriculture-based activities. The government’s development policy for 2013–2018 targets average annual GDP growth of 7% and a reduction in the poverty rate by at least 1 percentage point per year. More importantly, this latest policy framework heightens the government’s emphasis on commercializing agriculture, building urban infrastructure, supporting the development of the private sector, expanding vocational training, and strengthening social protection including health and nutrition. Importantly, the government’s commitment to economic reform appears to have intensified.
Public financial management is weak and lacks transparency and accountability	High	A review of the country’s PFM systems was carried out as a part of this program. While progress is noted, more needs to be done to ensure PFM systems in Cambodia are transparent and support accountability. A number of mitigation measures are in progress. The recent implementation of PFM reforms has continued to strengthen budget credibility and financial accountability. ADB is promoting accountability in public expenditures by improving capacity in individual ministries and is supporting PFM reform in SNAs focusing on fiscal decentralization. ADB has also supported institutional strengthening of the NAA, including the agency’s capacity to deliver findings to the National Assembly. ADB will build on earlier achievements to improve budget responsibility and accountability in rural development ministries and will continue to support decentralization and deconcentration and PFM reforms for SNAs. In addition, ADB will consider additional support to the NAA for auditing externally financed projects, particularly in major sectors and projects of relevance for ADB, and will continue to support the NAA in engaging with the National Assembly to discuss audit findings and follow up on recommendations.
Procurement capacity is insufficient	Medium	ADB project-level procurement risk mitigation actions are being implemented and monitored during project reviews and quarterly portfolio review missions. ADB-financed projects are managed under the government’s standard operating procedures, procurement manual, and financial management manual for externally financed projects. ADB provided support to draft, adopt, and implement the 2012 public procurement law and has provided capacity development, although additional efforts will be needed to develop detailed

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Corruption practices undermine the efforts of reform	High	<p>implementing decrees and guidelines, and to establish an effective complaint handling mechanism. Building on previous support for public procurement, ADB will undertake a procurement risk assessment. ADB will also strengthen procurement capacities in additional ministries (particularly ministries responsible for priority sectors under the CPS, 2014–2018) and SNAs, and, in cooperation with the Operations Services and Financial Management Department, deliver training on ADB's guidelines and procurement procedures. At the project level, ADB will continue to identify procurement risks and implement mitigation measures.</p> <p>Fundamental deficiencies in governance complicate efforts to combat corruption. The check and balance mechanism between the National Assembly and the executive is weak and the capacity of the ACU to fully implement the 2010 Anti-Corruption Law is low. Inadequate legal and judicial institutions and lax enforcement of laws, combined with weaknesses in the governance structure of the NAA, inhibit prosecution of violations. Nevertheless, the ACU has made some initial progress and has arrested, prosecuted, and imprisoned high-ranking police, court, and government officials. However, the ACU still faces challenges with regard to operational effectiveness, carrying out anticorruption activities, and systematically implementing the Anti-Corruption Law. To address this concern, ADB and other development partners have been providing support to the ACU as it implements the Anti-Corruption Action Plan for Asia and the Pacific, which is being coordinated by the ADB–OECD Anti-Corruption Initiative. ADB will continue to explore entry points to support the ACU in fulfilling its mandate. While ADB is not involved in legal and judicial reform, these efforts are being supported by other development partners.</p>
Contextual Risks		
Reforms are pursued in an ad hoc manner, compromising their integrity.	Medium	<p>IFSD program mitigates this risk by continuing ADB's sequenced approach to financial sector development. ADB's initial efforts focused on the development of an appropriate legal framework and then concentrated on the banking subsector. Research indicates that this approach yields the largest impact in terms of growth in real GDP when working in nascent financial systems. Beginning in IFSD's subprogram 1, the government will begin a well-sequenced process to introduce a government bond market and institutional investors, both of which are fundamental prerequisites to development of the nonbank financial subsector. This reform agenda will begin with efforts to increase liquidity in the money market, followed by the completion of the legal foundation (subprogram 2), and then progress to the development of an implementation road map (subprogram 3).</p>

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Coordination across ministries complicates the implementation of comprehensive sector reforms.	Medium	To mitigate this risk, the IFSD program includes reforms designed to enhance interministerial coordination. To support the development and implementation of a comprehensive financial inclusion strategy, the government established a working group encompassing 12 line ministries. Similarly, the government has established an MOU between the NBC, MEF, and SECC to enhance financial sector stability and to better coordinate market development activities.
The completion of legal reforms takes longer than expected, compromising the reform timelines.	Medium	The risk that enabling legislation will be delayed is difficult to fully mitigate. To minimize this risk, the IFSD program recognizes the timing and sequencing of the legislative process in Cambodia. Proposals to amend or enact new laws are first coursed through the Council of Ministers as a policy action in recognition of the mandatory screening role played by the council prior to securing the prime minister's approval. Approval by the National Assembly is deferred to the next subprogram to provide the necessary time for a full vetting and vote. In addition, technical assistance will be provided under the IFSD program to build an understanding for the need to amend or enact laws, and to provide technical support to the Council of Ministers.
Staff capacity is not adequate to implement complex reforms.	Medium	The IFSD program is supported by technical assistance to provide inputs to some of the more challenging technical reforms. For example, the program will directly support the development of a deposit insurance fund, SME guarantee and related listing schemes, and the enhancement of the payment system.
Lack of key data inhibits the government's ability to assess program effectiveness.	Medium	The IFSD program and the related technical assistance will support a variety of data gathering activities. For example, the implementation of the financial inclusion strategy and the SME lending support schemes will be supported by comprehensive data collection, including gender disaggregated data.
Overall	High	Overall, national risks are considered, on average, high because of concerns over PFM and corruption. Mitigation measures have been adopted and include efforts by ADB and development partners to strengthen PFM, devolve expenditure authorities and accountability, and further enhance the NAA. Contextual risks are generally considered medium and well mitigated. The programmatic approach ensures that ADB's support for complex capital market reforms is long term and employs a sequenced approach. Program design helps mitigate coordination risks and ensures program timing mirrors the legislative process. Technical assistance will be utilized to support the completion of complex reforms.

ACU = Anti-Corruption Unit, ADB = Asian Development Bank, CPS = country partnership strategy, GDP = gross domestic product, IFSDP = Inclusive Financial Sector Development Program, MEF = Ministry of Economy and Finance, MOU = memorandum of understanding, NAA = National Audit Authority, NBC = National Bank of Cambodia, OECD = Organisation for Economic Co-operation and Development, PFM = public financial management, SECC = Securities and Exchange Commission of Cambodia, SMEs = small and medium-sized enterprises, SNA = subnational authority.

Source: Asian Development Bank.