

## **CAMBODIA Country Profile**

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Decades of internal conflict had disastrous consequences on Cambodia, depleting its human resources and destroying much of its infrastructure, including its financial sector. During the Khmer rouge regime money and banking activities were abolished, while the subsequent regimes failed to promote an open and dynamic financial sector. In 1992, after the signing the peace accords, Cambodia emerged from isolation and large-scale aid and relief operations followed, with the first microfinance experiments laying the foundations of a microfinance industry now reaching almost half a million microentrepreneurs.

### **Needs for Microfinance**

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Cambodia has a population of 13.8 million, of which approximately 85% live in rural areas. An estimated 36% of the population lives under the poverty line. The financial sector is still underdeveloped, lacking rural development banks and limited by a weak rural finance network. 17 commercial and specialized banks only operate in Phnom Penh and the major provincial towns. The development of regular commercial lending activities have been constrained in rural areas by the high costs of operations, the inability to verify and enforce property rights, and the low level of economic activity. In result, the vast majority of the rural population has almost no access to formal forms of financial services.

It is estimated we the total demand for credit by micro and small business entrepreneurs could amount to US\$ 100-125 million. Only 45 to 55% of this amount is provided by existing providers of financial services.

### **Microfinance sector development**

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#### ***Chronology***

Microfinance started in the early 1990s as Cambodia came out from a long period of conflict. Microcredit was first provided by NGOs, to fill the gaps left by the banking sector. The first microfinance experiments were credit-oriented, to provide a kick-start to new business activities. Without a working banking system, organisations such as GRET (1991), World Relief (1992) and ACLEDA and CRS (1993) had to first run microcredit projects by physically handling cash transfers themselves. After 1993 and the international recognition of a new Cambodian government, aid started to flow in the country.

However, by 1994, microfinance initiatives were only reaching a limited number of people - 44,000 – which led to their transformation into larger, more focused institutions, capable of increasing significantly their outreach.

By 1998, the new industry was serving 214,000 people. Reaching a significant size also meant increased risks for clients as well as for microfinance promoters, and the microfinance stakeholders felt that a regulatory framework was needed. The National Bank of Cambodia issued a sub-decree to license large deposit-taking institutions and to register the smaller ones. Since then, microfinance has grown to encompass more than 75 MFIs in the country. ACLEDA, the Association of Local Economic Development Agencies, was the first NGO specialised in microfinance, registered in 1992, and became a specialised microfinance bank in 2000, and a full commercial bank in 2003. Ten MFIs are now licensed by the central bank, nine former NGOs and one being originally set up as a private company. Behind ACLEDA, the largest microfinance provider is AMRET, reaching more than 100,000 borrowers. 27 NGOs are registered with NBC as providing microfinance.

Since 2004, microfinance has become an industry in Cambodia, with a diversity of players (commercial banks, microfinance institutions, credit union) and a growth of outreach and increased diversity of services provided. The newest entrants in the industry are private company, with a business background, but no prior NGO experience (such as Maxima, Cambodia Microfinance, Tong Fa Microfinance). At the end of 2004 the microfinance industry in Cambodia was serving approximately 450,000 borrowers and 150,000 depositors.

### ***Competition***

There has been a rapid growth in the outreach of microfinance programs in Cambodia, with all providers needing to expand the number of clients served, most often in the same regions. It has provided benefits to the poor, such as more demand-based products, and decrease of interest rates, from 5% (flat) in 2000 to 3% (declining balance) offered by some providers in 2005. There is also a high turnover of staff within the microfinance sector in Cambodia, with staff moving from one organisation to the other. In the next few years, it is likely that the microfinance industry will enter in a phase of consolidation, with weaker institutions disappearing or merging with larger ones.

### ***Challenges***

There are almost no branches of banking institutions operating in rural areas, with the exception of ACLEDA. This makes the movement of cash for MFIs very difficult, and restrains their expansion to rural regions. In consequence, most MFIs compete in urban and easily accessible rural areas. Outreach is still limited in more remote, rural regions.

Competition is likely to increase in coming years, and the need for a credit bureau is already identified, to avoid over-indebtedness of clients borrowing simultaneously from different MFIs.

Some international NGOs manage integrated development projects including a credit component, offering subsidised loans. They represent an unfair competition to formal microfinance providers, who have difficulties to develop their outreach in areas where these projects are implemented.

### ***Regulations and government initiatives***

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#### ***Chronology***

In 1995, the government established the Credit Committee for Rural Development (CCRD), with funding support from UNDP and AFD, to formulate a strategy for rural credit development, strengthen management, and manage funding.

In 1997, the National Bank of Cambodia set up the Supervision Office of Decentralized Banking System Bureau. The office was then separated in 2000 into the 'Specialized Bank & MFIs Supervision Office' (coordination, supervision and regulation sector) and the Project of Support Microfinance Sector -PASMF- (capacity building).

In 1998, the government set up the Rural Development Bank as main promoter of rural finance, and a state-owned apex institution, established to promote microfinance in Cambodia.

In 1999, under the laws on banking and financial institutions, the government of Cambodia adopted a two-tier system for supervising microfinance. A 'Prakas' (i.e. government decree), on microfinance regulation was enacted in 2000, and implemented by the National Bank of Cambodia. MFIs with a portfolio over R100 million (tier 1) only need to be registered with NBC, while MFIs with a portfolio over R1 billion need to be licensed, as limited liability company or as a cooperative.

Only licensed MFIs and banks are eligible to access the US\$20 million ADB's credit line channelled through RDB and established in 2001. RDB has experienced difficulties in disbursing funds because of the strict eligibility criteria.

By its involvement and interest in microfinance, the government of Cambodia is committed to support the expansion of rural and savings services. It encourages the entry of private licensed MFIs and commercial banks, which develop competition in microfinance, and result in interest rates decrease, and more efficient and sustainable microfinance providers.

### **Legislation**

The "Law on Banking and Financial Institutions" enacted in November 1999 and the government decree (Prakas) for implementation, enacted in early 2000, recognizes three categories of banking institutions:

- Commercial banks, which require a minimum registered capital of US\$13 million and can carry out all banking activities.
- Specialized banks, which require a minimum registered capital of Riel 10 billion (US\$2.5 million) and can carry out a limited number of banking activities, as specified in the terms of their license.
- Micro Finance Institutions (MFIs), which require a minimum registered capital of Riel 250 million (approx US\$62,500).

Registration or licensing by the National Bank of Cambodia (NBC) of microfinance providers is compulsory when operators meet one or more of the following conditions:

<b>Financial products</b>	<b>Registration</b>	<b>Licensing</b>
Credit	Loan portfolio outstanding Riel 100 million (US\$25,000) or more	Loan portfolio outstanding Riel 1 billion (US\$250,000) or 10,000 borrowers or more
Savings	Voluntary savings mobilized: Riel 1 million (US\$250) or more or 100 depositors or more	Voluntary savings mobilized Riel 100 million (US\$25,000) or more or 1,000 depositors or more

Therefore, the NBC is basically enforcing two main alternatives for microfinance operators in Cambodia: licensing for the 'medium-sized' microfinance providers or registration for the 'small' microfinance providers.

Among others, key prudential regulations for MFIs include the following:

- Capital guarantee deposit of 5% of capital;
- Capital adequacy ratio of 20%
- Reserve requirement: minimum 5% of voluntary deposits;
- Liquidity ratio: liquid assets of at least 25% of voluntary savings;
- Aggregate loan commitment to any one client cannot exceed 10% of net worth; and
- Loan classification and provisioning regulation as 'substandard,' 'doubtful,' and 'loss' according to the following table:

Types of Loan	Definition	Provision requirements
Standard	Loans with payments of principal and interest on time	None
Substandard	Loans between 30-59 days past due	10%
Doubtful	(a) Loans with original maturity <1 year that are 60-89 days past due (b) Loans with original maturity >1 year that are 60-179 days past due	30%
Loss	(a) Loans with original maturity <1 year that are past due for >90 days (b) Loans with original maturity >1 year that are past due for >180 days	100%

According to the legal framework, microfinance is defined as: "the delivery of financial services such as loans and deposits, to the poor and low-income households, and to micro-enterprises." All microfinance operators, whether licensed or registered, are excluded from a range of financial sector activities including leasing, derivatives, gold and commodities dealing, the provision of cheque facilities and swap or forward dealing in foreign currencies. Registered and licensed operators must report to the NBC. In addition, licensed MFIs established as limited liability companies must pay taxes.

## Practices

Microfinance in Cambodia is still very much credit-driven, by donor-supported organisations, with the exception of a few organisation such as AMRET or ACLEDA with savings products well developed. In general credit portfolios are still financed by external donors or investors, and not by depositors. Interest rates are still high, due to high costs of operations, low cost efficiency, relatively expensive borrowings from local and overseas sources, due to the underdeveloped savings market, and a strong push towards sustainability. Interest rates tend to decrease, as competition forces higher efficiency in operations.

Credit methodologies seemed to have shift from village banking experimentation (1991-1995) to solidarity groups (1995-2002) to individual lending (2002 to now). However, a majority of the MFIs offer provide a mix of lending products, group and individual loans, while some are still using an adapted village banking structure to channel the funds more efficiently.

The low level of savings can be explained by a weak demand, with a lack of trust of potential depositors towards financial institutions, due to the history of failed banks in Cambodia in the

past (1960s and 1990s). In more recent times (2000), the central bank put higher capital requirements for commercial banks, forcing 14 banks to close, with only 5 to 8% of savings refunded to clients. The weak demand for savings could also result from old savings habits, savings in-kind. However, the underdeveloped savings market could also result from a limited supply of savings services by financial institutions. ACLEDA has demonstrated that with attractive products and strong institutional development, savings can be mobilised in Cambodia. With the granting of more microfinance licences, it is expected that MFIs will also grow their deposit portfolio in the future.

A savings pattern survey conducted by TPC in 2003 highlighted some savings behaviours in Cambodia:

- 96% of TPC clients kept their savings at home, while 2% kept it on themselves (cash, jewellery, etc.)
- Despite the large proportion of clients with savings, 52% claimed that they save on an irregular basis.
- Takmau and Phnom Penh were the regions with the highest amount of savings per depositor.
- 37% use the savings for family reasons (daily support), 15% to improve their current life, 10% for loan repayment.
- In case of emergency, 57% of people will borrow from friends, 28% from a moneylender.

## Innovations

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There is no real incentive from regulators to innovate in microfinance in Cambodia, but rather a push for standardisation to achieve sustainability. There is a need for donor support to develop savings and other financial products, and to experiment new delivery systems for reaching remote areas.

The microinsurance project of **GRET**, focusing on health insurance, could be an interesting product to be integrated by MFIs.

In addition, **CCSF** is the only microfinance institution structured as an umbrella organisation for savings banks, using a credit union model.

**ACLEDA** brings new products to Cambodia such as a deposit account in Euro, and new personal loans.

## Providers

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There are twelve main players in the microfinance market in Cambodia, each holding more than Riel 1 billion (US\$250,000) in outstanding loans and having more than 5,000 clients. One is a commercial bank (ACLEDA), the others are licensed microfinance institutions (limited liability companies) and a registered organisation, a credit union federation (CCSF) operating in Battambang region.

Licensed MFIs have to meet stringent regulations, such as paying as many as 15 different taxes, while major shareholders (over 20% of ownership) are liable for the MFI's solvency.

Behind ACLEDA as leader, AMRET has the second largest network, with PRASAC being the third. In addition to these top providers, there are also one newly licensed MFI (Tang Fang Microfinance) and other MFIs (Credo and Maxima) with smaller portfolio, which were created directly as limited liability companies, without going through an NGO or project transformation stage. Finally, there are approximately 60 unregistered small providers, and probably hundreds informal schemes.

As of September 2004, the main microfinance providers were:

	Loan Portfolio outstanding (in US\$ million)	Number of borrowers (rounded)	Amount of deposits (in US\$ million)	Number of depositors
ACLEDA Bank	57	115,000	29.2	51,437
PRASAC MFI	7.5	65,000	0	0
AMRET (ex. EMT)	7.3	101,000	0.2	110
Cambodian Entrepreneur Building (CEB)	3.4	8,000	0.16	8,147
Thaneakea Phum (Cambodia) Ltd (TPC)	3.1	36,000	0.37	59,931
Hattha Kaksekar Ltd (HKL)	2	6,000	0.08	7,723
Seilanithih	1.6	13,000	0.2	13,012
CREDIT	1.4	10,000	0.16	10,054
AMK	1.3	23,000	0.002	393
Vision Fund	1.2	19,000	0.02	1,745
CCSF	0.4	14,700	0.15	14,673
Maxima	0.2	1,000	0.02	10
Credo	0.1	3,000	0.02	2,033

## **Funding and Supporting Organisations**

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### ***Funding***

ACLEDA and most licensed MFIs have access to the ADB wholesale fund channelled through the Rural Development bank, which provides wholesale credits (US\$1 million) of three years terms to microfinance providers. There are no alternative, private wholesale funds in Cambodia. In addition the leading microfinance providers have either access to international funds such as the Microfinance Alliance Fund, SIDI, Triodos, BlueOrchard, etc, or are supported by International NGOs. However, MFIs outreach growth is still constrained by the lack of funds available to them, and MFIs try to attract new international investors in taking an equity participation in their capital.

### ***Support***

The “Cambodian Microfinance Association” (CMA) was created by a group of six MFIs in April 2004. It is a useful platform to share information, to represent the microfinance industry, to organise training (MIS in 2004), and to publish benchmarking reports. It could also be used as a vehicle for sharing information on clients, to make a collective investment in MIS development, a resource center, or share other industry-specific costs. However, CMA is not recognised by the regulator, the National Bank of Cambodia, as it only acknowledge the Association of Banks in Cambodia (ABC), and would like to see CMA as a subsidiary of ABC. However, ABC serves commercial banks and has higher membership fees.

CMA needs financial support to grow and develop into an independent organisation, to fully contribute to the development of microfinance in Cambodia. For the moment CMA is managed directly by staff of member MFIs (AMRET in management, CEB in Chairmanship).

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