

Microfinance in Cambodia

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In Cambodia, economic activities are dominated by micro, small and medium enterprises (MSMEs) which are largely based in rural areas. These MSMEs are beyond the reach of the banking sector, which tends to concentrate on serving businesses in urban areas. Thus, microfinance institutions (MFIs) are principally the main providers of financial services to the rural economy.

The Cambodia banking system started in the early 1990s when the government launched economic reform program from a centrally planned to a free market economy. Reform programs have been introduced and good progress has been achieved in regulating and supervising banks and microfinance institutions. Most rural financial operators in Cambodia have been transformed from non-government organizations (NGOs) that were involved with humanitarian work in late 1970s and have moved out of relief and rehabilitation works and redefined their roles in interventions in the development process.

Microfinance also helps mitigate vulnerability to shocks such as sickness and natural disasters, and develops micro-enterprises. Microfinance, hence, plays an important role in the development of the country and alleviating poverty.

Cambodia has one of the most rapidly developing microfinance sectors globally and is also internationally recognized as a success story. Presently, there are about 33 licensed microfinance institutions, in addition to 26 NGOs providing microfinance services which are registered with the National Bank of Cambodia (NBC).

Among those interventions, microfinance undertakings have thrived since the early 1990s, and most of the country's 24 provinces and cities now

have microfinance services provided by MFIs and NGOs. Services provided by MFIs could help the rural population, especially the poor, to increase their incomes and build up their assets.

In recent years, the microfinance sector in Cambodia has played a leading role in expanding the reach of the financial sector to the rural poor. Microfinance has been especially successful in Cambodia because MFIs have years of experience, they are well managed, and they are committed to achieving high standards of governance and transparency. MFIs are also willing to innovate and adapt, government regulators and donors support innovation, and there is healthy competition among MFIs.

Given a continuous growth of microfinance industry and a special attention from the NBC in gathering the microfinance operators to come under supervision of the NBC, the individual institutions as well as other microfinance operators have strengthened their institutions to become more professional and proper structure. In addition, those MFIs have been concentrated on defining their share structure and actual price value of each share held by their shareholders.

Most of MFIs had started their operations by initial funding source supported the activities of NGOs. Then, this fund was registered with the NBC as they transformed to a licensed MFI which is the legal form granted by the NBC. Moreover, those institutions have also ensured their governing body by defining the roles and responsibilities of the board of directors in pursuit of working proficiency that is directly held by their management team. On the other hand, this important division has not yet visibly seen within all MFIs whereby some of them have not yet been licensed and registered by the NBC. Those operators mostly service credits and savings under the project or particular activities of NGOs or a specific cooperative.

There are two main funding sources of MFIs, which are firstly come into the forms of owners' equity whether its equity injection or proceedings from initial capital of rural credit operator with NGOs. And, another proportionate equity injection comes from ongoing additional investment of interested shareholders. The second funding source comes into the form of liability which is financed by commercial and concessional loans of foreign

financial institutions, development agencies or governments of developed countries. Importantly, savings mobilized from the public are also acting as crucial sources to support microfinance operations.

Recently, the NBC has established a separate legal form for licensed MFIs that want to mobilize savings from public to apply for this regulatory status as well. To obtain this separate license, the MFI has to fulfil certain regulatory requirements of the NBC.

Cambodian MFIs are continuing to innovate with new products and services. New regulations that allow taking deposits will be of great help to MFIs in mobilizing local funds for their lending operations. Although previously restricted to lending, with very limited deposits, MFIs that meet government standards can now accept deposits. This will benefit customers by giving them a safe place to save money and the opportunity to earn interest from savings. Additionally, taking deposits will give MFIs a cheaper and more secure source of funds for lending than what they currently borrow from international lenders.

Innovation is also taking place in microfinance infrastructure. MFIs strongly support government plans to improve credit reporting. More comprehensive credit reporting will help to avoid client over-indebtedness, reduce the risks of lending, and decrease loan processing time. This, in turn, should help to reduce the costs of lending and interest rates, especially for borrowers with a good credit history.

The around the world, microfinance plays a key role in providing financial services to the poor. In Cambodia, about 19 years of impressive growth indicates that microfinance can also reach large numbers of poor people. Greater cost efficiencies and higher revenues in the MFI sector have led to expanded outreach in all 24 provinces—cities. Interest rates have fallen, and the quality of loan portfolios has improved as well. The government has been supportive of this evolution. Moreover, the government's well-directed policy in the Rectangular Strategy has proven crucial in leading to the successful development of the financial sector, especially in the role of microfinance for poverty reduction.

Cambodia's MFIs are among the country's most successful financial institutions, and through a combination of good management, innovation and a supportive regulatory environment, MFIs will continue to expand poorer peoples' access to finance and financial services, and serve as role models, both locally and internationally.

Despite the tremendous success of microfinance in Cambodia, the sector still faces challenges that include a legal framework limiting the ability of MFIs to diversify products and services, and the high cost of funding that prevents MFIs from achieving their potential in helping to develop the rural economy as well as the country as a whole. For MFIs to achieve their potential to serve more clients, they need to be able to offer a wider range of products and services, to access local currency and to reduce their costs of funds so as to remain commercially sustainable, while serving the lower end of the market.

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