



Angkor Mikroheranhvatho (Kampuchea) Co Ltd (AMK) Phnom Penh, Cambodia

Table with risk assessment details: Rating grade alpha, Assessment: Highly recommended, High safety, good systems, Visit dates: 11-14 December, 2006, Operational head: Mr Tanmay Chetan, Maximum validity of rating\*: till December 2007

Rating

AMK records good performance on management and financial indicators and reasonable performance on governance and strategy, with the only issue being uncertainty on account of the imminent change in the leadership of the organisation.

In M-CRIL's view, on account of good overall performance and the potential of the organisation to emerge as a market leader, AMK can absorb - from all sources - commercial loan funds of US\$3.0 million over the next one year for on-lending to its borrowers.

A rating update after one year is suggested to ascertain changes in the creditworthiness and absorptive potential of the institution. This rating is valid, subject to no other substantial inflows of loan funds into the organisation beyond the limits specified here and to no other significant changes in the organisational structure and external operating environment.

for Micro-Credit Ratings International Ltd

Handwritten signature of Sanjay Sinha

Sanjay Sinha, Managing Director

\*Validity This rating is valid till the next loan proposal made by the MFI to any financial institution or till any other significant change in the structure of the loan programme or in its external environment.

Liability The rating assigned is a professional opinion of the assessors and M-CRIL does not guarantee the information and cannot accept any legal responsibility for actions arising out of the recommendations made.



### Category wise rating

<u>Category</u>	<u>Rating grade<sup>1</sup></u>
A <i>Governance aspects</i>	<b>α–</b>
B <i>Management factors</i>	<b>α</b>
C <i>Financial performance</i>	<b>α+</b>
<b>Overall</b>	<b>α</b>

### Key Risk Factors

- 1 **Uncertainty on account of change in leadership:** The contract of the expatriate CEO of AMK comes to an end in June 2007 and the selection of a new CEO was in progress at the time of the rating visit. Although the organisation has well-defined strategies and good management systems, the future performance of the organisation would depend to a significant extent on the capabilities of the new CEO, particularly since the second line of leadership is presently unproven.

The process of recruiting a new CEO was initiated by the Board of AMK almost a year ago and multiple rounds of very detailed assessments of candidates were carried out. In developments after the rating visit, a person having about two decades of experience in microfinance has been selected and will join AMK in May 2007. Although not a Cambodian national, the new CEO has been living in Cambodia since 1992. The present CEO is expected to orient the new one to the policies, procedures and culture of AMK over a period of 6-8 weeks during May-June 2007.

### Key Programme Strengths

<b>Governance, experience and strategy</b>	<b>Management and operations</b>	<b>Financial</b>
1 Professional and visionary leadership 2 Clear focus on sustainability 3 Good credit culture	1 Qualified and experienced senior management team 2 Good MIS and control systems 3 Effective system for tracking overdues	1 Excellent portfolio quality 2 High capital adequacy 3 Good performance on profitability and sustainability

<sup>1</sup> M-CRIL’s grading sheet is attached at the end of the report.



## AMK – Risk Assessment

### Organisational Profile

Legal form	Years of m-f Operation	Number of			
		Active borrowers	Staff	Branches	Active borrowers/ Staff member
Limited Company licensed as an MFI	3.5 years	67,586	188	9	360

### Microfinance programme: Operational highlights

Client savings outstanding (KHR million, US\$ '000)	Outstanding borrowings (KHR million, US\$ '000)	Loan portfolio (KHR million, US\$ '000)	Cumulative loans disbursed (KHR million, US\$ '000)	Average loan size from MFI to borrowers (KHR, US\$)
173	12,851	21,220	46,025	349,358
43	3,205	5,293	11,480	~85

### Key financial ratios

Portfolio at risk (>=60 days)	Current repayment rate	Risk weighted capital adequacy ratio	Weighted average cost of funds	Yield to APR ratio
0.02%	99.2%	103.6%	1.7%	98.0%
Yield on portfolio	Other income to average portfolio	Financial cost ratio	Loan loss provisioning ratio	Operating expense ratio
35.7%	1.4%	0.5%	0.7%	28.4%
Total income to average total assets	Total expenses to average total assets	Return on average total assets	Operational self sufficiency	Financial self sufficiency
33.6%	26.1%	7.4%	122.6%	104.9%

#### Notes

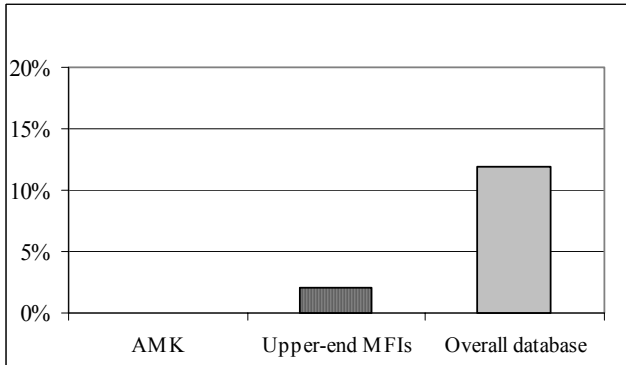
- All figures are for the organisation's microfinance programme as on 31 December 2006
- Throughout this report, US\$=KHR4,009
- The active borrowers figure includes Village Bank clients as well as individual clients. As on 31 December 2006, the organisation had 63,667 clients organised into Village Banks and 3,919 individual clients.
- Loan loss provisioning has been made for the current year at 0.7%, maintaining loan loss reserve (LLR) at 1.02% of the total managed portfolio.
- Other income consists mainly of bad debts recovered and foreign exchange gain.
- Capital adequacy is high for AMK since the funds are mainly equity from Concern Worldwide and long-term concessional loans provided by Concern.
- For calculation of FSS, the market rate of interest has been taken as six-month LIBOR+5%. As on 31 December 2006, the six-month LIBOR was 5.37%. The rate of inflation has been assumed at 5% (as estimated by The World Fact Book, 2006)
- The ratio of repayment rate and PAR<sub>60</sub> has been calculated from the MIS reports generated by AMK. The accuracy of data generated by the MIS has been verified by the rating team through an audit of the systems at AMK.



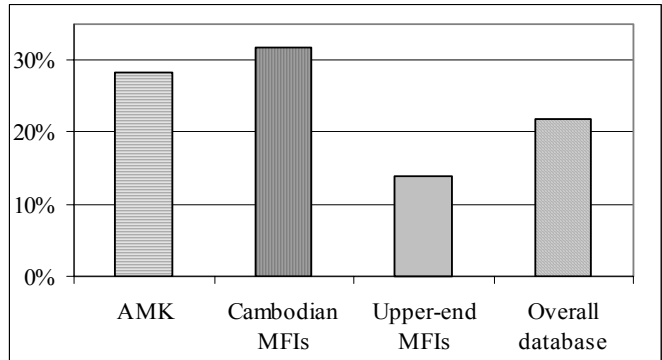
## AMK – Risk Assessment

### AMK – financial overview

Portfolio at risk (>=60 days): 31 December 2006



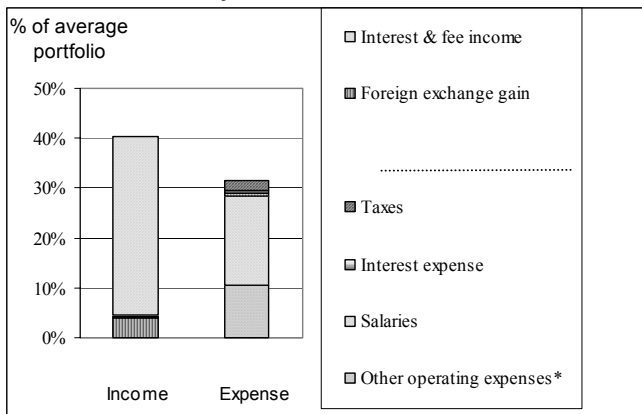
Operating expense ratio: 1 Jan 2005-31 Dec 2006



- Note:**
1.  $n_{\text{upper-end}} = 10$        $n_{\text{database}} = 120$ ; Database figures as on 31 December 2005
  2. Outliers and rated MFIs with no direct lending have been removed for analysis. Upper-end figures reflect top 10 MFIs.
  3. The upper-end MFIs and overall database ratios represent simple averages for their respective samples.
  4. The performance of either the Upper-end MFIs or all MFIs (overall database), do not necessarily reflect M-CRIL's rating standards.

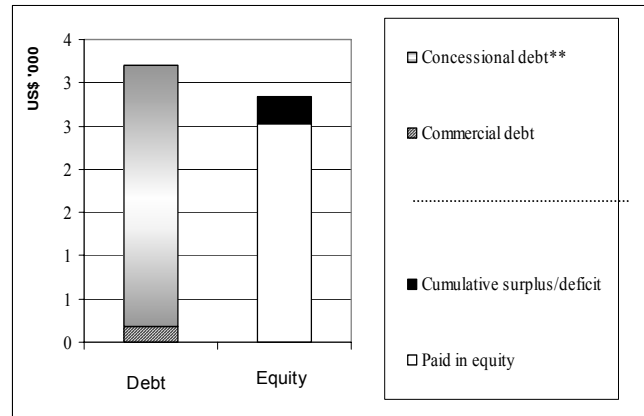
#### Income and expense distribution:

1 Jan 2005-31 Dec 2006



#### Debt and equity composition:

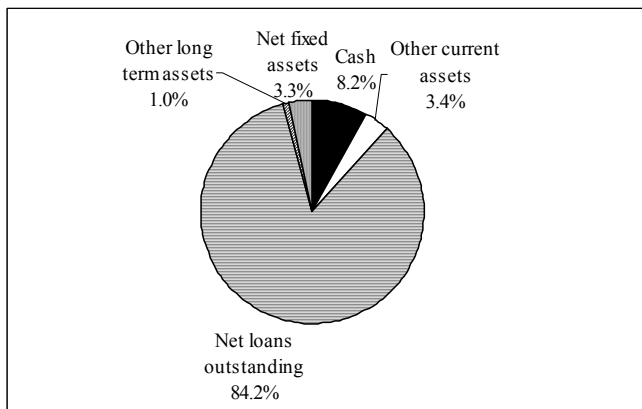
31 December 2006



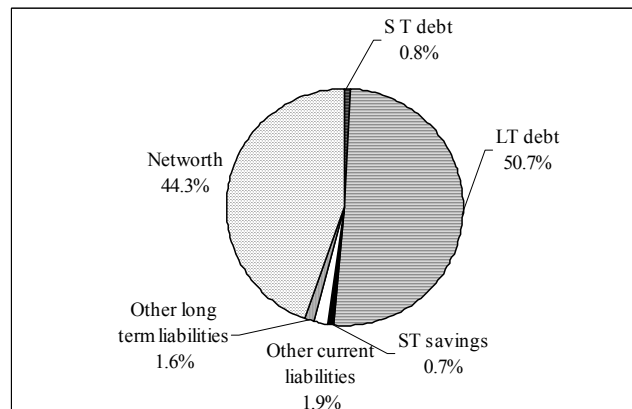
\* Other operating expenses include travel, depreciation and administrative expenses

\*\* Concessional debt is borrowing+comp.savings taken at < Bank PLR, voluntary savings taken at < bank deposit rates

#### Asset composition: 31 December 2006



#### Liability & net worth composition: 31 December 2006





### Country Profile<sup>2</sup>

Cambodia is a Southeast Asian country, bordering the Gulf of Thailand, located between Thailand (in the West), Vietnam (in the East), and Laos (in the North). A majority of the population is Buddhist and speaks the Khmer language. The country has a parliamentary democracy.

The country has had a history of invasions, wars and political unrest. After it gained independence from the French in 1953, the communist Khmer Rouge forces captured power in 1975. At least 1.5 million persons were either executed or killed due to forced hardships during the three-year Khmer Rouge regime. In 1978, the Cambodian army together with the Vietnamese army attempted to overthrow the Khmer Rouge regime, which started a 13-year period of civil war. The Paris Peace Accord in 1991 brought about the establishment of a democratically elected coalition government in 1998. Elections were again held in 2003, leading to the establishment of another coalition government in 2004.

Cambodia is one of the world's poorest nations, as a result of its history of domestic unrest. In 2005, its rank on Human Development Index of the United Nations Development Programme was 130. Subsistence farming employs 75% of the workforce. Conditions are ideal for the cultivation of its chief crop, rice, with availability of water from the Mekong River and a fertile soil. Corn, vegetables, fruits, peanuts, tobacco, cotton, and sugar palms are widely cultivated. Livestock raising (cattle, buffaloes, poultry, and pigs) and extensive fishing are the other major economic activities.

The Cambodian economy grew by an average of 7.6% annually from 1987 until 1993 and then by about 4.5% annually during 1994-99. Growth remained about 5% from 2000 to 2004, but has been estimated at about 13% (by the Economic Institute of Cambodia) during 2005. The number of people living on less than one dollar per day declined from 36% in 1998 to 28% in 2005, according to the World Bank's estimate. Economic growth has been largely driven by expansion in the garment sector and tourism. Clothing exports were fostered by a US-Cambodian Bilateral Textile Agreement, which gave Cambodia a guaranteed quota of US textile imports. From January 2005, after the expiry of the WTO Agreement on Textiles and Clothing, Cambodia-based textile producers are in direct competition with lower priced products from countries such as China and India.

The long-term development of the economy after decades of war remains a challenge. The population lacks education and productive skills, particularly in the poverty-ridden countryside, which suffers from an almost total lack of basic infrastructure. Fear of renewed political instability and a dysfunctional legal system coupled with extensive government corruption discourage foreign investment.

The Cambodian government continues to work with bilateral and multilateral donors to address the country's many pressing needs. Donors including ADB and the World Bank, pledged \$504 million in aid for 2005 on the condition that the Cambodian government begins taking steps to address rampant corruption.

The major economic challenge for Cambodia over the next decade will be in fashioning an economic environment in which the private sector can create enough jobs to handle Cambodia's demographic imbalance. More than 50% of the population is 20 years or younger. In this scenario, microfinance is one of the areas that has attracted the attention of policy makers and the country has made significant progress in microfinance policy and regulation. The National Bank of Cambodia – the central bank – has been instrumental in bringing about regulatory changes that include the provision of a separate licence for microfinance institutions.

<sup>2</sup> Source: *The CIA World Factbook*, U.S. Department of State, *Area Handbook of the US Library of Congress*, <https://www.cia.gov/cia/publications/factbook/geos/cb.html>



## 1 Organisational background

Angkor Mikroheranhvatho (Kampuchea) Co Ltd (AMK) was created out of the credit and savings programme of Concern Worldwide in Cambodia, which started in 1993. In 2000-01, Concern started moulding the credit and savings programme into an independent MFI, adhering to the new Cambodian microfinance regulation that stipulated the creation of a separate company and obtaining an MFI license once the outstanding loan portfolio exceeded KHR 1,000 million (equivalent to approx US\$250,000).

Concern Worldwide is an international non-government organisation working for reducing extreme poverty in about 30 developing countries around the world. As on 31 December 2005, Concern Worldwide had restricted as well as unrestricted funds of about 43 million Euros (US\$57 million) and, during the year ended 31 December 2005, the organisation had spent about 75 million Euros (US\$ 100 million) in charitable activities worldwide. Concern works through focused development programmes (for education, health or livelihoods) and partnerships with local organisations.

On 20 May 2003, Concern's credit and savings programme in Cambodia was renamed as AMK and it was registered as a Limited Liability Company, wholly owned by Concern Worldwide. In May 2004, AMK obtained its MFI license from the National Bank of Cambodia (NBC), the Cambodian central bank.

AMK continues to be a fully-owned subsidiary of Concern Worldwide Dublin (99.98%) and Concern Worldwide UK (0.02%). The total paid-up equity capital of AMK as on 31 December 2006 was KHR10,149 million (US\$2,531,441).

The organisation has a nine-member Board, with most of the members being associated with Concern Worldwide. The Chairperson of the Board is also a member of the governing council of Concern Worldwide and was previously a partner in PricewaterhouseCoopers and is an international expert on corporate governance. The Vice-Chairperson is Regional Director-Asia for Concern Worldwide and has previously held the position of Country Director of Concern Worldwide in Cambodia. The Secretary of the Board is a Cambodian national who has worked extensively in Community Forestry in Cambodia both with Concern and the Cambodian government and was involved in the setting up of the credit and savings programme of Concern Worldwide.

Other members include the Microfinance Advisor Concern Worldwide; the Head of Community Development Finance at the ANZ Banking Group; the Finance Director of Concern Worldwide; the CEO of DEPFA Bank, Dublin; and an international expert on agriculture and animal husbandry, who is presently a Policy Director of Concern Worldwide. The present CEO of AMK is also a member of the Board. Before taking up this position, he had nearly six years of experience in microfinance and rural development consultancy and in credit rating of microfinance institutions in India and other countries of Asia and in Africa. He has been CEO of AMK for about four years.

Since its inception, AMK has maintained its focus on poor households in the rural areas of Cambodia. The stated mission of AMK is “to help large numbers of poor people in rural Cambodia to increase their livelihood options through the sustainable delivery of appropriate and viable microfinance services to the economically active poor”.



## 2 Microfinance operations

### 2.1 Background of microfinance operations

AMK was initially drawn out of Concern’s credit and savings programme, which was operating in the Bantaey Meanchey and Battambang provinces in Western Cambodia. Over the years, AMK has expanded to seven other provinces in North and Central Cambodia. On 31 December 2006, AMK had an outreach of 67,586 borrowers spread across 928 villages in 29 districts of 9 provinces. Operations in four of these nine provinces started as recently as January 2006.

Apart from the CEO, the Head Office includes Managers for Operations, Finance, HR, MIS, Inspections and Training and Market Research. The CEO and Managers constitute the senior management team. The Managers are supported by officers in their respective departments. The Inspections Team had six staff on 31 December 2006.

Field operations are managed by the Operations Manager, who is assisted by two Regional Managers. At the branches, the operations are led by the Branch Manager, supported by 2-4 Area Managers, 6-8 Credit Officers and one Teller/Cashier. Apart from these staff, senior branches also have an Accountant.

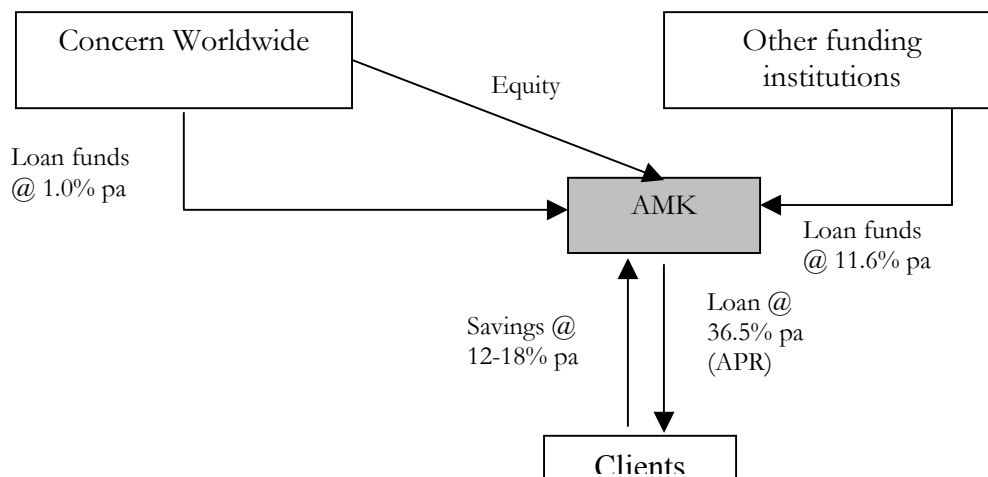
The sub-ordinated loans received from Concern Worldwide are the major source of funding for AMK. The organisation has also recently borrowed commercial funds from the Microfinance Alliance Fund (MAF). **Table 2** below shows the details of loan funds received by AMK.

**Table 2: Sources of loan funds**

Source of funds	Amount sanctioned (US\$ '000)	Outstanding on 31 Dec 2006 (US\$ '000)	Loan term (years)	Rate(s) of interest per annum
Concern Worldwide	2,500.0*	2,977.4	15	1.0%
MAF	199.5	177.4	3	11.6%
<b>Total</b>	<b>2,699.5</b>	<b>3,154.8</b>		

Although Concern Worldwide had initially sanctioned only US\$2.5 million, on account of fast growth of AMK, it agreed to put in more funds

The flow of funds to and from the organisation is depicted in the following diagram:





## 2.2 Microfinance policies

AMK lends to women and men from poor households, who may be organised into Village Banks or VBs (consisting of 20-60 clients) or may be individual clients not associated with VBs. The Village Banks are formed by grouping together 4-10 solidarity groups, which are groups of 4-6 clients (men or women) formed by the clients themselves. Clients within the solidarity groups are required to stand guarantee for each others' loans. The VB clients elect a Village Bank President (VBP) who is responsible for ensuring credit discipline within the VBs and also supports the Credit Officers in organising meetings for collections. The VBPs are paid an incentive based on the amount of interest and principal collected from VB clients.

Appraisal of loans is mainly the purview of the Area Managers and Branch Managers, who approve the loans based on the recommendations of and information provided by the Credit Officers. For loans to individual clients, a detailed monthly cash-flow statement for one year is prepared by the Credit Officer, based on discussions with the clients. Loans are disbursed in cash in the field, in the presence of the Area Manager and/or the Branch Manager.

Disbursements are made in Riel in all the branches except Banteay Meanchey, where loans are also given in Thai Baht.

### Savings

AMK offers two kinds of savings products: 1) Loan-linked compulsory savings for individual loan clients and 2) general voluntary savings. Individual loan clients are required to deposit 2% of the loan amount up-front as compulsory savings, which are not withdrawable till the loan is paid off. These savings may be returned to the client together with 12% pa interest, once the loan is closed. The client also has the option of converting these savings into a general voluntary savings account.

The general voluntary savings product provides clients (both VB and individual clients) sufficient flexibility in depositing and withdrawing their savings. The minimum balance required to be maintained is KHR500 (US\$0.125) and deposits or withdrawals are in multiples of KHR100 (US\$0.025). Interest is provided at the rate of 18% pa and is credited at the end of June and December every year. A savings account is considered to be dormant if no transaction has taken place for 12 consecutive months and is liquidated if there has been no transaction for 24 consecutive months.

### Loan products

AMK offers three group-based loan products, one individual loan product to individual clients and an emergency loan product to clients who have completed at least one cycle with AMK. The group loan products are described in the table on the following page.

No physical collateral is required for the group loan products and the “social collateral” of the group guarantee is sufficient.



## AMK – Risk Assessment

End-of-term VB (EoT-VB)	Instalment VB (Inst-VB)	Credit line VB (CL-VB)
<p><u>Eligibility:</u> all VB clients</p> <p><u>Maximum loan size:</u> KHR200,000 (US\$50) for the first cycle, with increment of KHR100,000 for two subsequent cycles. Thereafter, the maximum loan size is KHR500,000 (US\$125)</p> <p><u>Loan term:</u> 12 months (monthly payment of interest, bullet repayment of principal)</p> <p><u>Interest rate:</u> 3% per month on outstanding monthly balances</p> <p><u>Processing fee:</u> 0.5% of loan amount</p> <p><u>Prepayments:</u> allowed, no penalty</p> <p><u>Late payment fees:</u> 1% per month on outstanding principal balance</p>	<p><u>Eligibility:</u> VB clients having regular cash flows</p> <p><u>Maximum loan size:</u> Same as that for EoT-VB</p> <p><u>Loan term:</u> 12 months</p> <p><u>Interest rate:</u> 2.8% per month on declining balances</p> <p><u>Processing fee:</u> 0.5% of loan amount</p> <p><u>Prepayments:</u> allowed, no penalty</p> <p><u>Late payment fees:</u> 1% per month on outstanding principal balance</p>	<p><u>Eligibility:</u> VB clients who have completed two loan cycles</p> <p><u>Maximum loan size:</u> KHR500,000 (US\$125)</p> <p><u>Loan term:</u> 13-24 months</p> <p><u>Interest rate:</u> 3% per month on outstanding balances</p> <p><u>Processing fee:</u> 0.5% of loan amount</p> <p><u>Late payment fees:</u> 1% per month on outstanding principal balance</p>

The instalment loan for individual clients is provided to rural/semi-rural individual entrepreneurs. The loan size ranges from KHR1.0 million (\$250) to KHR2.0 million (\$500). The maximum loan size for the first cycle is \$375, with subsequent increments of \$50 for each cycle up to the upper limit of \$500. The maximum term is 18 months and the interest rate is 3% per month for the first three cycles (or two years) and 2.5% per month thereafter. In addition, processing fees of 0.5% of the loan amount are collected up-front.

Repayment takes place in monthly instalments with fixed principal and declining interest and there is no penalty for complete or partial pre-payment of the loan principal. However, In case of late repayment, there is a penalty of 1% per month on the outstanding principal balance.

Individual loans require physical collateral and personal guarantors. The original documents of landed property are generally taken as collateral security. However, the collateral is only to create pressure on clients and cannot easily be forfeited and sold, due to the unclear title of property in rural areas of Cambodia.

The emergency loan product is available to group or individual clients who have completed at least one loan cycle with AMK, and is given to help clients cover medical expenses or funeral expenses in case of a death in the family. A client can request an emergency loan from the Credit Officer in the village or the office staff at the branch and disbursement takes place within four working hours of receipt of the request.

The maximum loan amount is KHR400,000 or Thai Baht4,000 (\$100) and the maximum term is 10 months. Interest is charged at 2.5% per month and there is no processing fee.

There are no fixed instalments for repayment of the emergency loan but it must be cleared on or before the end of the loan term. The penalty for late payment is 1% per month on the outstanding principal balance. There is no physical collateral but one personal guarantor is required.



## Insurance

AMK has experimented with an in-house insurance product for clients which required contributions of KHR10,000 (\$2.50) per annum for the family to be eligible for an assured sum of KHR1.0 million (\$250) in case of their death. However, this product was discontinued since Cambodian laws do not permit MFIs to offer insurance products. AMK plans to start similar products soon after legal sanction is obtained.

## 3 Observations

### 3.1 Governance & strategy

AMK performs reasonably on governance with a grade of **α-**. The grade reflects the organisation's professional and experienced Board, a clear vision for growth and sustainability and well-defined strategies for its operations and key functional areas. The grade is restricted only by the uncertainty on account of the imminent change in the position of Chief Executive Officer, particularly since the present operational managers may not be strong enough to take full charge of operations.

#### ➤ Governance

Although composed mostly of persons associated with Concern Worldwide (which presently has full ownership of AMK), the Board of the organisation consists of professionally qualified persons of international repute. The Board has a mix of senior professionals from banking and finance as well as professionals experienced in microfinance, rural development, social welfare and human rights.

With the governing body consisting of both professionals having a commercial background and those from the field of social development, AMK has clearly defined financial and social objectives that emphasise financial sustainability and adherence to financial standards and credit discipline as well as sensitivity towards clients, staff, other marginal communities and the general environment.

To ensure transparency and good corporate governance, the Board is assisted by two Advisory Committees, one for Audit and the other for Social Performance Management (SPM). Both the committees have external experts as members, in addition to Board members. Meetings of the Audit Committee are also held every quarter and the SPM committee met three times during 2006.

AMK also has clearly drawn-out strategies for key operational areas such as client targeting, human resource skill development, product development, MIS and internal control. In addition, the medium to long-term strategy for governance and ownership, human resources and management of the external environment have also been clearly defined. This reflects the Board's involvement in the strategic management of AMK and also indicates the focus of the AMK leadership on the long-term sustainability of the organisation.



## AMK – Risk Assessment

The AMK leadership is aware that the Board needs to be broad-based with the inclusion of members with a better knowledge of the country and experience in microfinance across a range of countries. AMK also plans to include people who are not associated with Concern Worldwide, by diversifying the ownership structure through the sale of shares to investors.

### ➤ Leadership

AMK has a reasonably strong cadre of Managers who form the second line of leaders next to the CEO. The second line Managers are qualified and have sufficient experience in their respective areas. Four of the Managers have also worked in other MFIs in Cambodia, while one of them was also associated with Concern's credit and savings programme. Although the second line Managers are good, they do need further capacity building and experience to be able to lead the organisation without the support of an expatriate CEO. Specifically, the capabilities of the second line Managers in negotiating with international funding agencies and investors and in managing crises have not been sufficiently tested. While most of the major MFIs in Cambodia (CEB, Hattha Kaksekar, Amret, Prasac) have Cambodian operational leaders, AMK has recruited an expatriate as the new CEO, indicating that the Board also lacks complete confidence in the second line Managers.

The contract of the present expatriate CEO of AMK ends at the end of June and he has declined an extension for personal reasons. At the time of the rating visit, the Board and the CEO were in the process of recruiting another expatriate as CEO. After the rating visit, a person having about two decades of microfinance experience has been selected to replace the incumbent CEO. Although not a Cambodian national, the new CEO has been living in Cambodia for more than a decade and has been associated with MFIs in Cambodia.

The new CEO is expected to join in May 2007 and the present CEO will hand over his responsibilities at this time. He will orient the new CEO to the organisation's culture, policies and procedures. The new CEO would need to gain the trust and loyalty of staff at all levels, apart from being able to represent AMK to national and international agencies and also negotiate with international funding agencies.

### ➤ Microfinance products

Unlike most other MFIs in Cambodia, AMK continues to cater mainly to poor households as indicated by its low loan size of \$85 and its rural focus. In the case of other MFIs in Cambodia large loans of the order of \$300-500 to individuals from urban and semi-urban areas constitute a major proportion of the portfolio.

AMK's loan portfolio, on the other hand, is still made up to a significant extent by end-of-term loans (46%), credit line loans (26%) and instalment loans (12%) offered to rural households through Village Banks. Both the end-of-term loan and credit line loans are offered to households whose main economic activity is agriculture and the instalment loan is offered to rural households having more regular cash-flows (where the main economic activity is agriculture, but it is also supplemented by wage employment, self-employment in trade or remittances). The loan sizes for these loans is also smaller than the Village Bank loans offered by other major MFIs in the country.



## AMK – Risk Assessment

Loans to individuals constitute another 14% of the loan portfolio. However, even in the case of these loans, the average loan size (US\$250-500) is much lower than that offered by most other MFIs in Cambodia. AMK offers these loans to individual entrepreneurs in rural areas, who typically sell their agricultural or other produce in urban or semi-urban markets or trade in fruits and vegetables, livestock or fish.

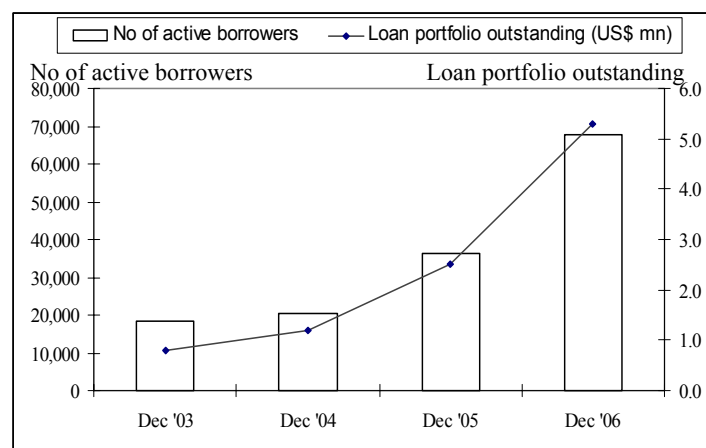
AMK has had limited success with its voluntary savings product. The proportion of voluntary savers to active borrowers has remained low (1.0-2.5%). The low demand for the savings product is largely a reflection of the bad experience of ordinary Cambodians with unscrupulous finance companies in the turbulent years of the 1990s and marketing the product may, therefore, need substantial efforts and, possibly a fundamental redesign. Given the relatively poor banking infrastructure in the areas where AMK works, a low savings inflow in AMK means that savings remain with the households in cash, which also increases their vulnerability. AMK would do well to consider carefully the cost-benefit of continuing with this product.

As indicated above, AMK has also experimented with a life insurance product, but the product has been temporarily shelved. Apart from the life insurance product, AMK also plans to introduce remittance/money transfer products across its branches during 2007. The operational modalities for this product are yet to be worked out.

### ➤ Growth and expansion

AMK has been growing steadily over the years. The figure alongside shows the growth of the organisation in terms of number of borrowers and loan portfolio outstanding.

The number of active borrowers has grown at a CAGR of 82%, while the loan portfolio outstanding shows a growth of 100% (CAGR) since December 2004.



The growth of AMK has been funded mainly by soft loans and equity support from its promoter, Concern Worldwide. According to the CEO, the fund support received from Concern Worldwide over the years has been sufficient to achieve the strategic targets set out by the organisation. Concern has, in fact, provided more loan funds than initially sanctioned to AMK, to enable the organisation to meet its expansion plans.

AMK plans to expand operations to all the 22 provinces of Cambodia during 2007-09 and have a presence in all the districts by 2011. In the future, it plans to operate in the semi-urban and urban areas also. The organisation has presently covers only nine provinces. AMK plans to have an outstanding loan portfolio of \$8 million by December 2007, with an outreach (active borrowers) of 112,000 clients. By 2011, the loan portfolio and outreach are planned to increase to \$28.5 million and 267,000 respectively.



## AMK – Risk Assessment

The organisation follows the cost-effective strategy of “amoebic growth”, where new branches are created by hiving off existing branches. Typically, a sub-office (with one staff) is first set up near the operational area of an existing branch, and a fully functional branch office is opened after attaining a critical mass. The sub-offices may later be shut down, depending on the cost of travel from the branch office to the Village Bank locations.

However, the rating team observed that in some of the new provinces, branch offices were opened within two-three months of the sub-offices and a Branch Manager was also appointed. The Branch Manager was supervising the operations around the sub-offices, which were located 50-60kms from the branch office. The process of promoting new clients around the branch office had been delayed, making the branch office almost non-functional. While appointing a Branch Manager may be necessary for monitoring operations, opening a non-functional branch office adds to the cost of operations.

### ➤ Operational risk management strategy

AMK operates with the strategy that reducing the household or livelihood risks among client communities contributes to reducing the operational risks of the organisation also. The market research function, which is one of the key operational functions within AMK, is oriented towards assessing and understanding the cash-flow patterns of clients’ households as well as their financial dependence and vulnerabilities.

In order to minimise foreign exchange risk, the organisation plans to negotiate with Concern Worldwide for a hedging arrangement, whereby repayments to Concern would be made at a pre-decided exchange rate. AMK presently faces the risk of loss due to devaluation of the Cambodian Riel or Thai Baht in relation to the US dollar (which is the currency in which it receives funds from Concern and also has to make repayments in). However, during the year-ended 31 December 2006, the Cambodian Riel has remained more or less stable in relation to the US dollar, while the Thai Baht has appreciated in relation to the dollar.

During 2005, AMK had to bear a foreign exchange loss of \$9,200 but in 2006, the organisation had a gain of nearly \$160,000. During 2003-06, AMK has made a net foreign exchange gain of nearly US\$118,000, mainly due to transactions in Thai Baht (which has been appreciating in relation to the US dollar) in the organisation’s oldest and largest branch.

The loan from the Microfinance Alliance Fund has been received in Riel and AMK plans to negotiate with all future lenders to provide loan facilities in the local currency or to sign a hedging contract.

Another area that needs to be addressed is the relatively high rate of client drop-out, which has been estimated by AMK to be nearly 25% per annum. The rate of client drop-out has been noted to be particularly high in the Banteay Mean Chey branch, where the target population temporarily migrates to Thailand for work, for some months during the year. AMK has noted that a significant proportion of clients who exit the programme do come back later. Studies of exit clients have also shown that clients prefer to remain inactive for some time, in accordance with their household income flows. AMK is in the process of arriving at a definition of drop-out clients (based on probability) as differentiated from dormant clients. AMK has estimated that the drop-out rates based on probability of drop-



## AMK – Risk Assessment

out is in the range of 12-20% in the older branches and is likely to be lower for the organisation as a whole.

One of the reasons behind the high drop-out rate may also be the long time taken to disburse the next loan to clients who have finished their loan. This has also been noted by the Inspections Department of AMK in 2005, after which AMK started sending additional credit officers to the branches at the time of harvesting of the crop, for speeding up the process of loan application and disbursal. However, delay in taking loan application from a client whose previous loan had been closed was also noted by the rating team.

### ➤ Competition

AMK offers well-designed products to suit the needs of customers in its low-end segment of the microfinance market. The end-of-term and credit line loan products are suited to the needs of clients whose main economic activity is agriculture, where cash-flows are of a seasonal nature. The emergency loan product provides clients with easy access to money to meet unprecedented needs such as healthcare or funeral expenses. In addition to this, the interest rates charged by AMK are lower than those charged by other MFIs – Amret (3.5% per month for group-based products, 2.5-3.5% per month on reducing balances for individual loans), Hattha Kaksekar Limited (2.0%-4.0% per month on individual loans), CREDIT and PRASAC (3.0%-3.5% per month on group-based loans and individual loans).

The senior management of AMK carries out a competition analysis on a quarterly basis, based on secondary data available from the Cambodia Microfinance Association, the national association of MFIs in Cambodia. The market share of the organisation has been growing steadily, while that of its competitors has remained constant or has even declined.

### Client protection and transparency

**Policy and mechanisms:** AMK has clearly defined policies and a written code of practice for client protection. The code of practice seeks to maximise the inclusion of poor and other marginalised sections of the population in the organisation's client-base. The code also mentions that AMK would take steps to prevent over-indebtedness of clients and to provide complete information on products and policies, so as to enable clients to choose freely. The code seeks to ensure appropriate and respectful behaviour towards clients by staff and management. In addition, AMK's operational risk management strategy is based on the principle that any activity that contributes to reducing the risk and vulnerability of clients also has a bearing on the risk profile of the organisation.

AMK has a separate department for Market Research which has conducted a detailed sample study profiling its typical clients. The study was aimed at understanding the income and expenditure sources of AMK clients, the seasonality patterns in their cash-flows and their vulnerability to economic "shocks".

**Communication and transparency:** There is effective communication on products and services in the organisation. At the pre-loan training sessions held in the villages, the products, policies and procedures of AMK are clearly explained to the clients.

**Fair pricing:** AMK's loan products are reasonably priced and the interest and fee charged by AMK on its loan products is lower than that of most other MFIs in the region. The Annualised Percentage Rate (APR) of AMK's loan products works out to 36.5% (weighted average across all products) and its yield is 35.7% compared to the 38.5% typical yield for 8 leading Cambodian MFIs rated by M-CRIL .



## AMK – Risk Assessment

**Responsiveness to clients:** AMK's products, policies and procedures are oriented towards the needs of its clients – the poor-income households in rural Cambodia. Village Bank meetings are held at the convenience of clients, and they are given sufficient flexibility to come to the meeting at any time and leave after their transaction is complete. The timings of Village Bank meetings are also changed based on the convenience of the members.

Recognising the vulnerability of its clients to unforeseen expenses, the Emergency Loan product, helps them meet medical exigencies or funeral expenses. The other main loan products (the end-of-term and the credit line product) are also designed to suit the uneven cash-flows of AMK's clients, who are mostly involved in agriculture and allied activities.

**Staff behaviour:** Staff behave respectfully with clients. The Area Managers and Internal Auditors visit VB meetings and clients on a random basis, which acts as a check on the staff. Repayments are ensured mainly through group pressure, enforced by providing incentives for 100% collection to the Village Bank President. In case of default, the Branch Manager and Area Manager generally follow up with the Village President and other members of the Village Bank, encouraging them to put pressure on the defaulting client.

### 3.2 Management issues

AMK displays good performance on management with a grade of **α**. The grade reflects the organisation's qualified and experienced human resources and good MIS and control systems, which are also being continuously improved.

#### ➤ Human resource quality and management

AMK has been increasing the number of its staff to match its growth. The organisation has done well to create a separate HR department and to standardise the processes for recruitment, training and induction of field staff.

As discussed earlier, AMK has a qualified and professional senior management team. All the senior Managers have significant experience in their present area of work, in other microfinance institutions in Cambodia or in other professional organisations. The heads of the departments (Operations, Finance, MIS, HR, Market Research and Inspections) have 4-7 years of prior experience (mostly in other MFIs of Cambodia) related to their present responsibilities and have been with AMK for more than 3.5 years. The HR Manager also has nearly 20 years of experience in training and capacity building in Concern Worldwide's savings and credit programme and later AMK. Several senior staff in the field have also been with the organisation since it was the credit and savings programme of Concern.

The senior staff in AMK are provided training in-house and also sent for external training programmes and exposure visits. During 2006, seven middle and senior management staff attended external training programmes on topics such as HR management, internal control, tax compliance and financial services management. All the heads of the departments and one senior staff also visited CARD-MRI, a prominent MFI in the Philippines for a five-day exposure visit. Apart from this, training in accounting and general management was provided in-house to staff at different levels.

AMK provides a range of financial benefits to its staff, which include staff loans, deposit facility for staff, insurance cover (health, accident and life) and pension/gratuity. Staff dropouts have been very low at 2% over the last two years.



## AMK – Risk Assessment

The MFI has developed a good incentive system for its field staff, whereby incentives are provided based on their performance across parameters such as active clients managed and repayment rate as well as on the basis of internal assessment by their superiors. Staff in the Head Office are also assessed by the immediate superiors, while the senior management staff are assessed by the CEO and by one other senior Manager.

### ➤ Accounting and MIS

AMK uses the MicroBanker software for accounting and MIS. It has a good accounting system. Monthly Trial Balance statements from all the branches, prepared in MicroBanker are downloaded from the database (which is shared and can be accessed in the Head Office). These are transferred to MS-Excel and consolidated financial statements are prepared, along with the Head Office Trial Balance.

The financial statements are presented to the Board on a quarterly basis. On a monthly basis, the financial statements along with reports on liquidity, capital adequacy and foreign currency exposure are sent to the National Bank of Cambodia.

Audited statements are prepared on an annual basis by PricewaterhouseCoopers (Cambodia) Limited. Since the statutory auditor is required to be changed every three years, the audit of AMK's financial statements are being carried out by KPMG from financial year 2006. All incomes and expenses are accounted for on an accrual basis. Interest income on loans with overdues is transferred to an interest suspense account, as per the guidelines of the National Bank of Cambodia.

AMK provides for loan losses in accordance with the guidelines of the central bank in this regard. In addition to the reserve requirement specified by the central bank, AMK maintains an additional loan loss reserve of 1% on all outstanding loans. Loans are written off when unpaid for more than one year and/or when the senior management believes that there is no prospect of recovery. Branch-wise income and expenditure statements are prepared and profitability analysis, without loading the Head Office administrative costs, is carried out

AMK has a good computerised MIS. The MicroBanker software allows the Head Office staff to check the transactions on-line after the transactions are closed at the end of the day. One weakness in the present MIS software is that if the date of the Village Bank meeting (or due date for repayment transactions) is changed, the Collection Sheet shows a nil-demand for that day. This makes it difficult to monitor collections and leaves scope for misappropriation of money from collections.

Another weakness noted by the rating team is in the appraisal process for loans to individuals. The household cash flow information entered by the Credit Officer is often based on rough estimates and is not verified by the Area Manager/Branch Manager in a significant proportion of cases. AMK has faced at least one case of default by an individual client, where it was found that the cash flow information was incorrectly entered.

While the MicroBanker software is sufficient to meet the present MIS requirements of AMK, the organisation has faced difficulty in getting service support from the MicroBanker team in Bangkok. Moreover, MicroBanker may not be able to support the new products that AMK plans to introduce in the near future. Thus, the organisation is planning to purchase and set up another MIS software developed by a Vietnam-based company that has supplied software to three banks in Cambodia and to some organisations involved in microfinance in Vietnam.



## AMK – Risk Assessment

### ➤ Tracking system for overdues

AMK has good systems for tracking overdues. The collection sheets and separate reports on clients with overdues that are generated by the software are used for follow-up on overdues. The software allows the Operations Department at the Head Office to monitor transactions online and cases of collections less than demand are followed up immediately by telephone.

AMK's Credit Officers generally do not leave the Village Bank meeting till the collection from all clients has come in. Village Bank Presidents have an interest in ensuring that all clients pay their dues on time, since they get an incentive only in case of full collections.

### ➤ Financial planning and control systems

AMK has good systems for planning and internal control. Financial planning is based on the operational plans provided by the Credit Officers, who plan the number of new clients and amount of loan to be disbursed (all products except credit line, based on maturity reports generated by the software). These plans are submitted to the Area Manager and Branch Manager, who send consolidated plans to the Regional Managers. The Regional Managers discuss the plans with the Branch Managers and make changes where necessary. Once finalised by the Regional Managers, these plans are sent to the Operations Manager at the Head Office. The Operations Manager enters the plan in Microfin software, and targets to the field staff are assigned by matching the operational plans with the overall strategic plan of the organisation.

Each branch sends details on variance from the target alongside the actual achievement every month. In addition, overall target vs achievement analysis is carried out on an annual basis in meetings at the Head Office. Variance analysis is done and the targets are revised if deemed necessary.

Regular cash planning is the responsibility of the Finance Manager, who monitors the cash position in branches on a daily basis online. Branches are instructed to deposit excess cash (if cash is more than specified limits) in the bank. Any excess cash is transferred to the Head Office and sent to other branches as per their need.

Internal control: AMK has a six-member Inspections Team, which is headed by a person who has previously worked with Pricewaterhouse Coopers and has experience in auditing of MFIs as well as corporate organisations in Cambodia. Other senior members of the team include an ex-Manager/Supervisor of Financial Institutions in the National Bank of Cambodia and a senior auditor from another MFI.

The audit process covers operations and documents in the field, branch as well as the Head Office. The process is oriented towards assessment of risk in different aspects of operations at the above three levels. Each branch is audited at least once every year. However, the rating team noted that there is scope for improving the frequency of audits, since two branches (Siem Reap and Kampong Speu) had been audited only once during the previous financial year, while the operations in Otdar Mean Chey (which were managed from Banteay Mean Cheay branch) had not been audited even once during the last financial year.

The audit of field operations covers a sample check of loan documents and cross-checking of the Passbooks with information in the software. The sampling process is designed to



## AMK – Risk Assessment

specifically include a selection of new Village Banks formed, recent loan transactions, high-ticket size loans, new Credit Officers, districts with high growth and low growth and also all cases of clients with overdues. In addition, a certain proportion of exit clients are also interviewed.

Both in the Head Office and the branches, activities across the key functional areas of Operations, HR, Finance and MIS are covered, and a risk assessment is carried out. The risk assessment in Operations is based on loan applications, passbooks, field visit reports and agreements for collateral. In Finance, risk assessment covers cash management, control over expenditures, accounting documents and reporting to government authorities and the National Bank of Cambodia. Similarly, the key aspects of MIS of HR are also covered for the risk assessment.

### ➤ Quality of clients/member groups

Visited Village Banks showed good performance on repayment of loans and overall discipline. Awareness about the organisation's loan and other products was found to be reasonable. In some VBs visited, members who could not attend the meeting themselves had sent their repayments through other members or their relatives.

### ➤ Infrastructure

AMK has an infrastructure base of about US\$265,000 as on 31 December 2006, which is adequate for the present scale of operations. This includes mainly vehicles, computer hardware and software, apart from furniture and fittings in the Head Office and branch offices.

## 3.3 Financial performance

The financial performance grade of AMK is excellent at **α+**. The grade reflects the MFI's excellent portfolio quality and good performance on profitability and sustainability.

### ➤ Credit performance and asset quality

AMK has excellent credit performance. Its current repayment rate is 99.2% and the PAR<sub>60</sub> is 0.02% as on 31 December 2006. This is mainly due to the well-designed loan products supplemented by strong credit discipline and immediate follow-up on overdues that the organisation has been able to maintain.

While a large proportion of loans are used for agriculture AMK's clients are not solely dependent on agriculture, and the sale of livestock is also an important income source. The other major sources of income are self-employment (in trade or manufacturing) and wage employment. Therefore, crop failure due to drought or low rainfall is unlikely to affect the quality of AMK's loan portfolio significantly.

### ➤ Mobilisation of funds

The main source of funds for AMK has been its promoter – Concern Worldwide. The subordinated loans from Concern constitute 48% of the total assets of AMK on 31 December



## AMK – Risk Assessment

2006. Only in 2006 has AMK obtained loan funds from another lender – a loan of \$200,000 from the Microfinance Alliance Fund (MAF). The organisation plans to obtain more commercial loans in the financial year 2007, mainly to diversify its sources of funds.

### ➤ Asset, liability and equity composition

AMK records good asset utilisation with the loan portfolio contributing to 84% of the total assets on 31 December 2006. Cash balances at 8% of the total assets are relatively high, but are required to be maintained since the organisation has a voluntary savings product that is freely withdrawable. On the liabilities side, long-term sub-ordinated debt from Concern Worldwide and the loan from MAF constitute a significant 50% of the total, while the net worth contributes to 44% of the assets.

With this high equity level, AMK has an excellent capital adequacy position with the risk-weighted capital adequacy at 103.6%. The organisation has a high leverage capacity and should not have any difficulty in borrowing from commercial sources.

### ➤ Profitability and Sustainability

AMK records good performance on profitability and sustainability, although operational self-sufficiency was achieved only during 2005. The organisation has a high positive RoA of 7.4% (4.1% excluding foreign exchange gain) during 2006. The operational expense ratio (OER) of the organisation is relatively high at 28.4%, but is lower than the 31.8% of the typical MFI in Cambodia rated by M-CRIL. AMK has a relatively high yield of 35.7% on its loan portfolio, which is however lower than the 38.5% of Cambodian MFIs (simple average of portfolio yield of MFIs rated by M-CRIL).

AMK's Operational Self-Sufficiency at 136.1% (122.6% excluding foreign exchange gain) and Financial Self-Sufficiency at 116.4% (104.9% excluding foreign exchange gain) are very good. The OSS and FSS are expected to improve in the short-term, but the OSS is likely to stabilise at about the same level or be lower in the long term, as the organisation starts borrowing from commercial sources. The FSS is likely to move up and closer to the OSS in the long term, for the same reason.



## 4 Conclusions

Strengths	Weaknesses
<p><u>Organisational</u></p> <ul style="list-style-type: none"> <li>✓ Professional and visionary leadership</li> <li>✓ Clearly defined operational strategies</li> <li>✓ Well-designed loan products</li> <li>✓ Long-term support from Concern Worldwide</li> </ul> <p><u>Managerial</u></p> <ul style="list-style-type: none"> <li>✓ Qualified and experienced senior management team</li> <li>✓ Good MIS and control systems</li> <li>✓ Effective tracking system for overdues</li> </ul> <p><u>Financial</u></p> <ul style="list-style-type: none"> <li>✓ Excellent portfolio quality</li> <li>✓ Sound capital adequacy position</li> <li>✓ Good performance on profitability and sustainability</li> </ul>	<p><u>Organisational</u></p> <ul style="list-style-type: none"> <li>✗ Lack of experienced and strong second line leaders</li> </ul> <p><u>Managerial</u></p> <ul style="list-style-type: none"> <li>✗ Relatively weak information system for appraisal of loans to individuals</li> </ul> <p><u>Financial</u></p>

## 5 Creditworthiness

AMK has achieved a rating grade of *alpha (α)*.<sup>3</sup> In terms of creditworthiness this implies **high safety**. AMK’s performance on management and financial indicators is excellent, while its performance on governance is good. The grade is restrained only on account of the present uncertainty arising out of the transition to a new CEO. The organisation has high capital adequacy, and has maintained good portfolio quality. It has good performance on profitability and sustainability indicators, with good projected future profitability. One of its major strengths is the support it receives from its promoter – Concern Worldwide. A strong governing body, well-developed operational strategies and an able and qualified senior management team are major strengths.

**In M-CRIL’s view**, on account of overall good performance and the potential of the organisation to emerge as a market leader, AMK can absorb – from all sources – commercial loan funds of US\$3.0 million over the next one year for on-lending to its borrowers.

A rating update after one year is suggested to ascertain changes in the creditworthiness and absorptive potential of the institution. **This rating is valid, subject to no other substantial inflows of loan funds into the organisation beyond the limits specified here** and to no other significant changes in the organisational structure and external operating environment.

<sup>3</sup> The Rating Grade given measures performance on the rigorous standards established by M-CRIL. The assessment uses an instrument designed specifically for the conditions and nature of MFIs operating in Asia and is comparable with other ratings done by M-CRIL in this region.



AMK – Risk Assessment

Financial statements of AMK's microfinance programme

Balance Sheet

<u>As on 31 Dec 2005</u>		<u>As on 31 Dec 2006</u>	
US\$	Assets	US\$	US\$
	<b><u>Current assets</u></b>		
467,720	Cash in hand and bank		508,923
126,960	Cash with NBC		129,066
20,331	Other assets		36,431
31,102	Staff loans		46,861
	<b><u>Loans outstanding</u></b>		
2,506,807	Gross loans outstanding	5,292,870	
(25,985)	(Loan loss reserve)	(54,188)	
2,480,822	Net loans outstanding		5,238,682
<b>3,126,935</b>	<b>Total current assets</b>		<b>5,959,964</b>
	<b><u>Long term assets</u></b>		
32,852	MIS software and hardware	60,281	
90,309	Net property and equipment	204,989	
<b>123,161</b>	<b>Total long term assets</b>		<b>265,270</b>
<b>3,250,096</b>	<b>Total Assets</b>		<b>6,225,234</b>
	<b><u>Liabilities and Net Worth</u></b>		
	<b><u>Current liabilities</u></b>		
11,722	Client savings		43,017
67,253	Accrued expenses		52,498
	Interest payable to lenders		1,520
	Interest payable on savings		1,249
	Taxes payable		62,944
	<b><u>Short term debt</u></b>		
	Concern Worldwide	50,546	
	Total short term debt		50,546
<b>78,975</b>	<b>Total current liabilities</b>		<b>211,774</b>
	<b><u>Long term liabilities</u></b>		
52,212	Provision for retirement benefits		98,049
	<b><u>Long term debt</u></b>		
	MAF	177,390	
710,021	Concern Worldwide	2,977,378	
710,021	Total long term debt		3,154,768
<b>762,233</b>	<b>Total long term liabilities</b>		<b>3,252,817</b>
	<b><u>Net worth</u></b>		
2,530,817	Paid-up-equity (Concern Worldwide Dublin)		2,530,817
624	Paid-up-equity (Concern Worldwide – UK)		624
(96,745)	Retained net surplus/(deficit)		(122,553)
(25,808)	Current net surplus/(deficit)		351,755
<b>2,408,888</b>	<b>Total net worth</b>		<b>2,760,643</b>
<b>3,250,096</b>	<b>Total Liabilities and Net Worth</b>		<b>6,225,234</b>

Exchange rate: US\$ = KHR 4,009

<sup>4</sup> The Rating Grade given measures performance on the rigorous standards established by M-CRIL. The assessment uses an instrument designed specifically for the conditions and nature of MFIs operating in Asia and is comparable with other ratings done by M-CRIL in this region.



AMK – Risk Assessment

Income Statement

<u>1 Jan 2005 – 31 Dec 2005</u>		<u>1 Jan 2006 – 31 Dec 2006</u>	
	<u>Income</u>	US\$	US\$
657,262	Interest on loans	1,377,732	
14,832	Fee income on loans	31,244	
2,009	Bad debts recovered	460	
	Bank interest	11,262	
4,385	Other income	<u>11,648</u>	
<b>678,488</b>	<b>Total income</b>		<b>1,432,347</b>
	<u>Financial costs</u>		
	Interest on borrowings	18,963	
926	Interest on savings	<u>2,717</u>	
<b>677,563</b>	<b>Gross financial margin</b>		<b>1,410,668</b>
(3,732)	Provision for loan losses	<u>28,202</u>	
<b>681,295</b>	<b>Net financial margin</b>		<b>1,382,466</b>
	<u>Operating expenses</u>		
445,401	Staff costs	674,345	
39,852	Travel	85,118	
46,106	Depreciation	69,344	
164,100	Administrative/office expenses	<u>289,688</u>	
<b>695,459</b>	<b>Total operating expenses</b>		<b>1,118,494</b>
<b>(14,164)</b>	<b>Net Surplus/Deficit</b>		<b>263,972</b>
4,786	Non-operational income (training & consultancy, foreign exchange gain)		158,163
9,196	Foreign exchange loss		
(18,574)	Profit before tax (PBT)		<u>422,134</u>
7,234	Tax		<u>70,379</u>
<b>(25,808)</b>	<b>Profit after tax (PAT)</b>		<b>351,755</b>

Exchange rate: US\$ 1 = KHR 4,009



## Notes to the financial statements

1. Income includes interest income, fees and earnings from other microfinance related services offered by the MFI. All loan portfolio related income is recognised only when it is actually received (**cash basis**).
2. Financial costs (interest on borrowings and savings, if any) and operating costs are calculated on an **accrual basis**. Loan loss provisioning expense and the corresponding balance sheet entry (loan loss reserve) has been computed based on the quality of the portfolio.
3. The income and expenditure account for the year ended 31 December 2005, as prepared by M-CRIL, shows a loss on account of adjustment for interest income accrued but not received. However, in spite of the loss, the accounting for tax has not been changed, in order to reflect the true picture.

## Glossary

1. Current repayment rate  
Ratio of principal recovered (net of pre-payments) to the principal due during the current year.
2. Portfolio at risk (PAR<sub>60</sub>)  
Ratio of the principal balance outstanding on all loans with overdues greater than or equal to 60 days to the total loans outstanding on a given date.
3. Yield on portfolio  
The interest income on loans divided by the average loan portfolio for the year.
4. Other income to average portfolio  
Total income other than from the interest on loans divided by average portfolio.
5. Financial cost ratio  
Total interest expense for the year divided by the average portfolio.
6. Loan loss provisioning ratio  
Total loan loss provisioning expense for the year divided by the average portfolio.
7. Operating expense ratio  
Ratio of salaries, travel, administrative costs and depreciation expenses to the average loan portfolio.
8. Average loan portfolio  
This represents the average loan outstanding for the year computed on a monthly basis.
9. Average total assets  
This represents the average total assets for the year calculated on an annual basis.
10. Operational Self-Sufficiency  
Ratio of total income to total costs for the year.
11. Financial Self-Sufficiency  
Ratio of total income to total adjusted expenses for the year. Adjustments have been made for subsidised cost of funds (w.r.t. market interest rate), equity (w.r.t. inflation) and in-kind donations.
12. Risk weighted capital adequacy ratio  
Ratio of networth to risk weighted assets (Risk weights: 100% for all assets except the following: fixed assets & interest bearing deposits: 50%; cash 0%; cash with central bank: 0%).



## Projected Cash Flows and Financial Statements for five years

- The following assumptions and projections - derived from the limited information available from the organisation on its future financial projections – are tentative in nature. These **should not be viewed in isolation nor be regarded as a basis for investing in the future** - only the main risk rating report provides an opinion on investments.
- All assumptions are based on the data gathered during the rating exercise and the savings and credit methodology used by the organisation.

### 1 Basic Assumptions

(see also Notes to Cash Flow Projections below)

For the year ending:	31-Dec-06	Dec-07	Dec-08	Dec-09	Dec-10	Dec-11
Active borrowers	67,586	111,823	167,939	208,821	237,434	266,927
No of voluntary savers (incl staff)	1,477	4,236	7,069	9,214	10,439	11,800
Savings per saver/year (US\$)	3.3	3.5	3.6	3.8	4.0	4.2
Yield on average portfolio	35.7%	35.0%	35.0%	35.0%	34.0%	34.0%
Interest paid on savings	13.0%	12.0%	11.0%	10.5%	10.5%	10.5%
Cost of external funds	1.5%	2.9%	3.8%	5.5%	6.9%	7.8%
Repayment rate from groups	99.2%	98.0%	98.0%	98.0%	98.0%	98.0%
Loan loss reserve ratio	1.0%	1.2%	1.2%	1.3%	1.3%	1.3%
Number of loans disbursed – I		90,000	120,000	149,904	144,586	147,720
Number of loans disbursed – II		16,000	30,000	37,018	44,563	52,694
Average loan size (US\$) – I		59	62	72	79	82
Average loan size (US\$) – II		191	208	235	245	250

**I** – End of Term / Credit Line and Emergency Loan products

**II** – Instalment loan products to VBs and individuals



## AMK – Risk Assessment

### 2 Projected balance sheets

US\$ '000

As on:	Dec-06	Dec-07	Dec-08	Dec-09	Dec-10	Dec-11
<b>Assets</b>						
Cash balance	510	422	594	819	1,044	1,073
Cash with central bank	129	207	300	421	482	522
Loans outstanding – I	4,032	6,378	8,142	11,388	12,445	12,621
Loan outstanding – II	1,273	1,911	3,874	5,438	6,836	8,254
Total loan outstanding	5,305	8,289	12,016	16,826	19,281	20,875
Loan loss reserve	-54	-99	-144	-219	-251	-271
Net loans outstanding	5,251	8,190	11,872	16,607	19,031	20,603
Staff loans	47	75	108	151	174	188
Other current assets	37	41	60	84	96	104
Net fixed assets	266	324	456	625	694	755
<b>Total Assets</b>	<b>6,239</b>	<b>9,259</b>	<b>13,391</b>	<b>18,708</b>	<b>21,520</b>	<b>23,246</b>
<b>Liabilities and Net Worth</b>						
Concessional loans	3,035	4,733	5,371	5,714	5,776	5,339
Commercial loans	178	1,178	1,911	4,394	6,544	8,004
Savings (clients and staff)	43	62	83	115	156	206
Provision for retirement benefits	98	157	228	320	366	397
Taxes payable	63	52	70	71	103	132
Other liabilities	55	83	120	168	193	209
Provision for forex losses		17	42	78	124	174
Paid-up-equity	2,537	2,537	4,847	6,847	6,847	6,847
Retained surplus/deficit	-123	230	439	719	1,002	1,412
Current surplus/deficit	353	210	280	282	410	527
Net worth	2,767	2,977	5,567	7,849	8,259	8,786
<b>Total Liabilities and Net Worth</b>	<b>6,239</b>	<b>9,259</b>	<b>13,391</b>	<b>18,708</b>	<b>21,520</b>	<b>23,246</b>

I – End of Term / Credit Line and Emergency Loan products

II – Instalment loan products to VBs and individuals



AMK – Risk Assessment

3 Projected Income Statements

US\$ '000

For the year ending:	Dec-06	Dec-07	Dec-08	Dec-09	Dec-10	Dec-11
<b><u>Income</u></b>						
Interest	1,381	2,379	3,553	5,047	6,138	6,827
Fee income	31	11	23	33	41	50
Other income	23	8	15	22	27	33
Foreign exchange gain	159	0	0	0	0	0
<b>Total Income</b>	<b>1,594</b>	<b>2,398</b>	<b>3,592</b>	<b>5,102</b>	<b>6,207</b>	<b>6,909</b>
<b><u>Cost</u></b>						
Financial	22	150	268	511	809	1,032
Loan loss provision	28	45	45	75	32	21
Depreciation	70	91	145	216	271	288
Provision for forex losses	0	17	25	36	45	50
Operating costs (excl.depr.)	1,052	1,833	2,759	3,912	4,537	4,859
<b>Total Cost</b>	<b>1,171</b>	<b>2,136</b>	<b>3,242</b>	<b>4,749</b>	<b>5,694</b>	<b>6,251</b>
<b>Surplus/Deficit</b>	<b>423</b>	<b>262</b>	<b>350</b>	<b>353</b>	<b>513</b>	<b>658</b>
Tax	71	52	70	71	103	132
<b>Profit to balance sheet</b>	<b>353</b>	<b>210</b>	<b>280</b>	<b>282</b>	<b>410</b>	<b>527</b>



## AMK – Risk Assessment

### 4 Projected Cash Flow Statements

US\$ '000

For the year ending:	Dec-07	Dec-08	Dec-09	Dec-10	Dec-11
<b>Inflows</b>					
Opening cash	510	549	750	1,007	1,219
Concessional loans	2,000	1,000	750	500	0
Commercial loans	1,000	1,125	3,250	4,000	4,250
Repayments from members – I	2,963	5,676	7,547	10,365	11,937
Repayments from members - II	2,422	4,262	7,135	9,520	11,756
Equity investments		2,310	2,000		
Voluntary savings deposits	15	26	35	42	50
Compulsory savings deposits	32	58	93	123	151
Increase in provision for retirement benefits	59	71	91	47	30
Increase in other liabilities	28	37	48	25	16
Interest income	2,379	3,553	5,047	6,138	6,827
Other income	19	39	54	68	83
<b>Total Inflow</b>	<b>11,427</b>	<b>18,706</b>	<b>26,802</b>	<b>31,834</b>	<b>36,318</b>
<b>Outflows</b>					
Disbursement – I	5,310	7,440	10,793	11,422	12,113
Disbursement - II	3,060	6,225	8,699	10,918	13,174
Repayments to lenders – concessional	302	362	407	437	437
Repayments to lenders – commercial	0	392	767	1,850	2,790
Withdrawal of savings	28	63	96	123	150
Operating expenses (excl. depr.)	1,833	2,759	3,912	4,537	4,859
Interest paid on borrowings	143	260	500	794	1,013
Interest paid on savings	7	9	11	14	19
Increase in cash with central bank	78	93	120	61	40
Increase in staff loans	28	34	43	22	14
Increase in other current assets	5	19	24	12	8
Taxes	63	52	70	71	103
Fixed assets purchase	149	277	385	339	350
<b>Total Outflow</b>	<b>11,005</b>	<b>17,984</b>	<b>25,827</b>	<b>30,602</b>	<b>35,070</b>
<b>Net cash balance</b>	<b>422</b>	<b>594</b>	<b>819</b>	<b>1,044</b>	<b>1,073</b>

I – End of Term / Credit Line and Emergency Loan products

II – Instalment loan products to VBs and individuals



## AMK – Risk Assessment

### 5 Key projected performance ratios

<b>For the year ending:</b>	<b><i>Dec-06</i></b>	<b><i>Dec-07</i></b>	<b><i>Dec-08</i></b>	<b><i>Dec-09</i></b>	<b><i>Dec-10</i></b>	<b><i>Dec-11</i></b>
Operational self-sufficiency	<i>123%</i>	113.2%	111.7%	108.3%	109.9%	111.4%
Return on average assets	<i>7.4%</i>	2.7%	2.5%	1.8%	2.0%	2.4%
Operating expense ratio	<i>28.4%</i>	28.3%	28.6%	28.6%	26.6%	25.6%
Average outstanding/borrower (US\$)	<i>78</i>	74	72	81	81	78
Portfolio growth rate	<i>111.1%</i>	50.1%	102.7%	40.4%	25.7%	20.7%
Risk weighted capital adequacy ratio	<i>103.6%</i>	45.8%	39.9%	29.6%	34.3%	42.0%



## AMK – Risk Assessment

### 6 Notes to the projections

1. The operating expense ratio is based on current levels and is projected based on changes in overall productivity and growth in staff, branches and portfolio.
2. Estimated external borrowings are subject strictly to performance based on the findings of this microfinance capacity assessment (credit rating).
3. Average loan size to members increases steadily over the projected years, stabilising at US\$82 for the EoT-VB, Credit Line and Emergency Loan products and at US\$250 for the instalment loan products
4. Interest income is taken as [yield on portfolio\*average portfolio for the year]. The yield is projected to reduce over the years, assuming that the organisation would have to reduce its interest rates on account of competition..
5. Other income is the income that the organisation earns as interest on staff loans, bad debts recovered and bank interest.
6. Disbursements are taken as the [number of loans disbursed during the year\*average loan size to borrowers].
7. Estimates on growth in outreach and demand for loans from the organisation have been made based on current growth levels and future expansion potential and capacity.
8. Repayments to lenders is 6% per annum for the concessional loan and the 33.33% per annum on the commercial loans.
9. Interest paid is taken as the [average cost of external funds \* the average external borrowing liability figure].
10. In the projections the net worth figure includes equity, retained surpluses and current surplus.
11. A provision of 0.25% of the outstanding portfolio has been created every year, to provide for foreign exchange losses.
12. It has been assumed that the organisation would have to maintain cash with the central bank at 2.5% of the outstanding loan portfolio.
13. Taxes are assumed to be 20% of the annual taxable income
14. The currency exchange rate used throughout the projected financial statements is US\$ 1 = KHR 4,000.



## AMK – Risk Assessment

### 7 List of abbreviations

ADB	Asian Development Bank
AM	Area Manager
AMK	Angkor Mikroheranhvatho (Kampuchea) Co Ltd
APR	Annual Percentage Rate
BM	Branch Manager
CEO	Chief Executive Officer
CO	Credit Officer
DCB	Demand Collection Balance
FSS	Financial Self-Sufficiency
HO	Head Office
HR	Human Resource
KHR	Khmer Riel
LIBOR	London Interbank Offered Rate
LT debts	Long Term Debts
MAF	Microfinance Alliance Fund
M-CRIL	Micro-Credit Ratings International Ltd
MFI	Micro Finance Institution
MIS	Management Information System
NBC	National Bank of Cambodia
NGO	Non Government Organisation
OER	Operating Expenses Ratio
OSS	Operational Self-Sufficiency
PAR <sub>60</sub>	Portfolio at Risk (greater than 60 days)
PAT	Profit after tax
PBT	Profit before tax
ROA	Return on Assets
VB	Village Bank



## M-CRIL’s Microfinance Rating Symbols

M-CRIL Grade	Description
<b>α++</b> alpha double plus	Highest safety, very good systems ➤ most highly recommended
<b>α+</b> alpha single plus	Very high safety, good systems ➤ highly recommended
<b>α</b> alpha	High safety, good systems ➤ highly recommended
<b>α–</b> alpha minus	Reasonable safety, good systems ➤ recommended
<b>β+</b> beta plus	Reasonable safety, reasonable systems ➤ recommended, needs monitoring
<b>β</b> beta	Moderate safety, moderate systems ➤ acceptable, needs improvement to handle large volumes
<b>β–</b> beta minus	Significant risk, poor to moderate systems ➤ acceptable only after improvement
<b>γ+</b> gamma plus	Substantial risk, poor systems ➤ needs considerable improvement
<b>γ</b> gamma	Highest risk, poor systems ➤ not worth considering