

HATTHA KAKSEKAR LIMITED
(Rural Credit and Savings Institution)

BALANCE SHEET
AS AT 27 APRIL 2001

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**REPORT OF THE AUDITORS TO THE BOARD OF DIRECTORS OF
HATTHA KAKSEKAR LIMITED
(Rural Credit and Savings Institution)**

We have audited the balance sheet of Hattha Kaksekar Limited, a micro-finance institution (the "MFI") on page 3 which has been prepared in accordance with the accounting policies set out in note 2 to the balance sheet.

Respective responsibilities of the Directors and the Auditors

The MFI's Directors are responsible for the preparation of the balance sheet which gives a true and fair view. In preparing the balance sheet which gives a true and fair view, it is fundamental that appropriate accounting policies are selected.

It is our responsibility to form an independent opinion, based on our audit of the balance sheet, and to report our opinion to you.

Basis of opinion

We conducted our audit in accordance with International Standards on Auditing. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of whether the accounting policies are appropriate to the MFI's circumstances and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the balance sheet is free of material misstatement. In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion, the balance sheet gives a true and fair view, in all material respects, of the financial position of the MFI as at 27 April 2001, in accordance with the accounting policies set out in note 2 to the financial statements.

PRICEWATERHOUSECOOPERS (CAMBODIA) LIMITED
Phnom Penh, Cambodia
Date: 11 July 2001

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	Note	27 April 2001 US\$
ASSETS		
Cash on hand and in banks	3	31,803
Loans receivable, net	4	1,228,215
Grants receivable	5	495,263
Fixed assets	6	72,509
Other assets		<u>29,377</u>
TOTAL ASSETS		<u><u>1,857,167</u></u>
LIABILITIES AND EQUITY		
LIABILITIES		
Bank loan	7	550,000
Subordinated loan	8	845,107
Deposits of members	9	62,288
Deferred grant income	10	296,413
Other liabilities		<u>25,509</u>
		<u>1,779,317</u>
EQUITY		
Share capital	11	<u>77,850</u>
TOTAL LIABILITIES AND EQUITY		<u><u>1,857,167</u></u>

Mr. Hout Ieng Tong
Director

Date: 11 July 2001

The accompanying notes on pages 3 to 8 form an integral part of this balance sheet.

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1. General

Hattha Kaksekar, a non-governmental organisation (“NGO”) established in November 1996, has created Hattha Kaksekar Limited (“HK Ltd.”) in order to comply with Prakas No. B700-06 dated 11 January 2000, a regulation issued by the National Bank of Cambodia (“NBC”) on licensing of micro-finance institutions. The creation of HK Ltd. seeks to convert the NGO’s micro-lending operations into a licensed and commercially oriented micro-finance institution (the “MFI”). HK Ltd. aims to carry out the NGO’s micro-finance activities and conduct banking operations as defined in the Law on Banking and Financial Institution. This conversion was achieved by transferring and assigning all the assets and liabilities of the NGO as at 27 April 2001, the effective date of transfer, to HK Ltd. including all grant contracts and the outstanding receivables arising from these contracts as at the date of transfer (see note 5), conditions and obligations relating to a bank loan (see note 7), all employment contracts, conditions, obligations and benefits, leases on premises or houses for office branches or headquarters, and all others related to micro-lending operations of the NGO. The transfer and assignment of all these were effected through an agreement to transfer assets and liabilities, and the subordinated loan agreement between the NGO and HK Limited (see note 8), both dated 27 April 2001.

On 27 April 2001, the Ministry of Commerce issued a business license dated 3 April 2001 to HK Ltd. to operate as a public limited company with the aim to provide credit and savings services for the lower segments of the market. HK Ltd. is in the process of completing all the requirements of the National Bank of Cambodia (NBC) in order to obtain a banking license.

Hattha Kaksekar operates in four branches located in the provinces of Pursat, Kampong Thom and Siem Reap, with primary source of revenue derived from interest income earned on providing loans to clients. It also provides voluntary savings accounts service to its clients, and business training courses for its female borrowers.

2. Significant Accounting Policies

Basis of preparation

The balance sheet was prepared under the historical cost convention.

The balance sheet as at 27 April 2001 was prepared upon request by the NBC as part of its licensing requirements. The balance sheet should establish the beginning balances of the MFI’s assets and liabilities following the transfer and assignment of all micro-finance related assets, liabilities and operations of the NGO to the MFI as discussed in note 1. These beginning balances were extracted from the audited assets and liabilities of the NGO as at 27 April 2001, which were all transferred to the MFI.

Loans

Loans are stated net of provision for doubtful loans.

Fixed assets

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Fixed assets are recognised in the books of the MFI at the respective costs these were acquired by the Organisation, less accumulated depreciation as at the effective date of transfer.

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2. Significant Accounting Policies (Continued)

Fixed assets (continued)

Depreciation was provided by the Organisation using the straight-line method over the estimated useful lives of the fixed assets based on the following annual rates:

	Percentage (%)
Communication and transportation equipment	16.67
Furniture and fixtures	12.5
Office equipment	25

Foreign currency translation

The financial statements are expressed in United States Dollars ("US\$"). Assets and liabilities denominated in foreign currency as the effective date of transfer were converted into US\$ at the rates of exchange ruling at the balance sheet date.

3. Cash on Hand and in Banks

	US\$
Cash on hand	31,241
Cash in banks	<u>562</u>
	<u><u>31,803</u></u>

4. Loans Receivable, Net

All loans were provided to Cambodian rural residents. Details of loans receivable by location are as follows:

	US\$
Sampov Meas, Pursat	447,709
Kampong Thom	423,653
Siem Reap	284,917
Phnum Kravaanh, Pursat	<u>128,600</u>
Gross loans receivable	1,284,879
Provision for doubtful loans	<u>(56,664)</u>
	<u><u>1,228,215</u></u>

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4. Loans Receivable, Net (Continued)

Factors that were considered by the NGO in determining the provision for doubtful loans include the size of the loan portfolio, previous loss experience, current economic conditions and their effect on clients, the financial condition of individual clients, and the performance of individual loans in relation to contract terms.

The amount of provision transferred to the MFI is determined by applying defined percentages to the outstanding balances in various aging categories. The amounts obtained are then multiplied by a 2/3 fraction in determining the required month-end provision balance. Defined percentages applied are as follows:

Loan status/classification	Percentage (%) Applied
Sub standard loans (where repayments are more than 30 days overdue)	50
Doubtful loans (where repayments are more than 60 days overdue)	75
Loss (where repayments are more than 90 days overdue)	100

Further details of gross loans receivable as at the date these were transferred are as follows:

	Monthly Interest Rate	Loan Term in Months	US\$
Small business loans	3%	1 - 10	1,195,268
Agricultural loans	4%	1 - 12	89,611
			<u>1,284,879</u>

5. Grants Receivable

Details of grants receivable are as follows:

	US\$
Ministry of Economy and Finance- Agence Francaise de Development (AFD)	
Technical assistance	318,413
Loan fund for Siem Reap	137,500
Fixed assets fund	31,250
	<u>487,163</u>
Deutsche Gesellschaft fur Technische Zusammenarbeit (GTZ)	8,100
	<u>8,100</u>
Total	<u><u>495,263</u></u>

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5. Grants Receivable (Continued)

AFD's grant for technical assistance is intended to provide for a technical advisor for three years on the ongoing transformation programme as discussed in note 1, and should cover the MFI's whole operations and strategies. The grant should also be able to provide an accounting advisor for eighteen months to strengthen the MFI's finance unit and oversee its accounting computerisation, including management information systems and human resource development. Hattha Kaksekar must submit quarterly reports showing the degree of its accomplishment to date in terms of the indicators specified by AFD and one final report at the end the third year. All requests for payments must be supported by a copy of bills or invoices, to be sent to the project coordinator of the Ministry of Economy and Finance who will then pass the requests to AFD for payment processing.

GTZ grant is to be used exclusively for costs to be incurred by the MFI for the introduction of public saving services in the province of Kompong Thom. The amount can be collected in one installment after the expenses as budgeted for in the grant agreement have been carried out.

6. Fixed Assets

	Cost	Accumulated	Net Book
	US\$	Depreciation	Value
		US\$	US\$
Transportation equipment	69,506	22,358	47,148
Office equipment	24,832	14,531	10,301
Communication equipment	12,080	4,881	7,199
Furniture and fixtures	11,556	3,695	7,861
Total	<u>117,974</u>	<u>45,465</u>	<u>72,509</u>

7. Bank Loan

This account represents a loan from Rural Development Bank obtained in 2000 aggregating to US\$ 550,000. The loan bears interest at 12% a year and is secured by all assets of the MFI. Principal and interest repayments are due after two years from the respective dates the loan proceeds were received. A 0.5% commission fee of the proceeds received is being charged by the Bank.

8. Subordinated Loans

	27 April 2001
	US\$
Hattha Kaksekar, NGO	682,381
Ministry of Economy and Finance (MoEF) - AFD	<u>162,726</u>
	<u>845,107</u>

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8. Subordinated Loans (Continued)

HK NGO has loaned funds to HK Ltd. following the transfer and assignment of all micro-finance related assets, liabilities and operations of the NGO to the MFI as discussed in note 1. Among the terms and conditions the subordinated loan agreement dated 27 April 2001 between the NGO and HK Ltd. contain are as follows:

- i) The subordinated loan will not be repayable to HK NGO unless HK Ltd. ceases to provide credit to the rural population of Cambodia or unless it decides to repay all or part of the loan;
- ii) The loan is a non-distributable fund; and
- iii) Being a public grant, it will be considered as "Tier II Capital" in the context of Article 15 of Prakas No. B700-006 issued by NBC, and shall be computed in computing HK Ltd.'s capital adequacy ratio.

HK Ltd. shall pay to HK NGO a management fee of 1% per annum on a pro-rata basis. Furthermore, the agreement provides that if HK NGO divests its investment in HK Ltd. should a new shareholder purchase a part or all the shares of HK Ltd., the proceeds will be added to the subordinated loan and transferred to HK Ltd.

HK Ltd. also accepts the liability for repaying the total value of the loan to the MoEF of the Royal Government of Cambodia (RGOC) under the terms and conditions of the subordinated loan agreement dated 27 December 2000, most notably, that the loan will not be repayable to the RGOC unless the MFI ceases to provide credit to the rural population of Cambodia or unless it decides to repay all or part of the loan.

9. Deposits of Members

	27 April 2001 US\$
Sampov Meas	22,692
Kampong Thom	23,381
Phnum Kravaanh	8,206
Siem Reap	8,009
	62,288
	62,288

As at the date of transfer, these deposits bear interest at the following rates:

<u>US\$</u>	Interest rate per annum		Interest rate per annum
	%	<u>Riel</u>	
1.00 – 5.00	0	4,000 – 20,000	0
6.00 – 30.00	1	20,100 – 100,000	3
31.00 – 150.00	3	100,100 – 600,000	5

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More than 150.00

4

More than 600,000

7

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10. Deferred Grant Income

This account represents the portion of the grants receivable transferred to the MFI which are to be recognised as grant income subsequent to balance sheet date, following the MFI's fulfillment of certain terms and conditions in the respective grant agreements (see note 5).

11. Share Capital

Details of authorised, issued and fully paid share capital of the MFI are as follows:

	<i>Number of Shares</i>	<i>Price/Share US\$</i>	<i>Total US\$</i>
Hattha Kaksekar, NGO	1,167	30	35,010
Staff association	844	30	25,320
SIDI	500	30	15,000
Mr. Jean Thiboutot	84	30	<u>2,520</u>
			<u><u>77,850</u></u>