Linkage between Formal and Informal Financial Sectors in Cambodia

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1. Definition of Formal and Informal Financial Sector

Many authors generally defined formal and informal financial sectors in different ways. Germidis, Kessler, and Meghir (1991) categorized the financial sector into three levels: the formal, semi-formal, and informal financial sectors. The formal financial sector included the central bank, banking and non-banking financial intermediaries (commercial banks, merchant banks, development banks, savings banks, building societies, postal savings networks, specialized financial institutions, social security schemes, provident funds, and insurance companies), and capital markets.

The semi-formal entities included savings and credit co-operatives and credit unions. "Semi-formal" was defined as having no registration or regular supervision although the rules of functioning may have been laid down by law. The co-operative movement was significant because it provided an alternative form of financial intermediation for small-scale savers and borrowers. It was based on the concept of self-help through mutual solidarity.

The three basic types of informal financial sector were individual moneylenders, groups of mutually organized individuals, and partnership firms. The individual moneylenders included friends, neighbors, relatives, landlords, professional moneylenders, input dealers, output processors, produce and itinerant traders, market vendors, storeowners, and more. Group of individuals consisted of savings arrangements like fixed-fund associations, savings clubs, and combined savings and credit arrangements. Partnership firms included indigenous bankers and pawnbrokers in India and other non-bank financial intermediaries such as finance, investment, leasing and hire-purchase, and chit fund companies.

Pagura and Kirsten (2006) defined formal and informal financial institutions by dividing them into four groups. The most formal group consisted of commercial banks, state development banks, postal banks, insurance companies, leasing companies, and money transfer firms. The least formal included self-help groups, farmers' organizations, women's associations, indigenous savings clubs, and deposit collectors

In addition, Erhardt (2002), who studied the financial markets for small enterprises in urban and rural northern Thailand, proposed the formal-informal continuum specifically for Thailand. In order of degree of supervision and regulation from formal to informal level, the continuum started from commercial banks, BAAC, non-financial government institutions, cooperatives, pawnshops, traders, money-lenders, len shares (ROSCAs) to friends and relatives.

Steel (2006) segregated financial institutions into four groups and made the division more clearly by providing more information related to their definition, institutions, and principal clients. For example, formal banks, such as commercial and development banks and other kinds of banks, obtained licenses from the central banks. The informal ones were not legally registered at a national level although they may belong to registered association.

Based on Steel's segregations, I divided the financial system in Cambodia into formal, semi-informal, and informal segments. As of December 31, 2009, the formal financial sector consisted of *twenty-seven commercial banks, six specialized banks (one Rural Development Bank), and twenty licensed MFIs*. The semi-formal sector included *standard chartered, Vietnam Bank for agriculture and development, and twenty-six registered NGOs.* The informal financial sector contained around 60 unregistered NGOs, money lenders, family, and friends. It was tough to decide whether some registered NGOs should be included in the informal financial sector because they registered their whole bodies but not their financial program with the central banks. Therefore, it was based on the list[1] of the central bank to differentiate which registered NGOs were included in the informal financial sector.

2. Contribution of Formal Financial Sectors to the Industries

Based on the central bank of Cambodia, the total credits of the banking sector (commercial and specialized banks) increased from 28% (2005/2004) to 80% (2007/2006) but down to 57% (2008/2007); meanwhile, the total loans of MFIs increased from more than 72% (2006/2005) to 83% (2008/2007) (NBC, 2008). The banking sector's total loan and deposit to GDP (2007) are around 29% and 32% as of December 31, 2008 while the MFI's total loan and deposit to GDP are only 3.33% and 0.06% (Table 1).

Table 1: Assets, Deposits, Loans, and Net Profits of Financial Institutions in Cambodia

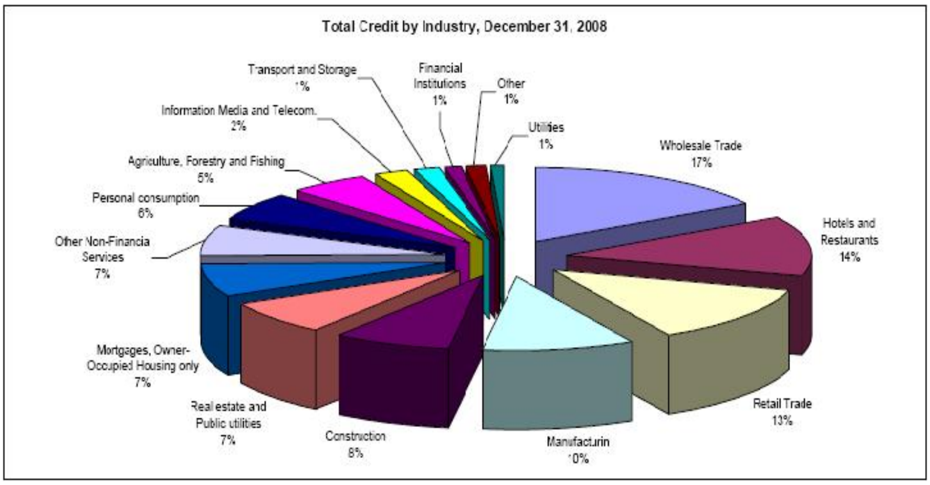
	Total Assets*	TA/GDP (07)	Total Deposit	TD/GDP	Loans*	Loans/GDP	Net Profit*	NP/GDP
Commercial Banks	16,796,989	49.47%	10,703,513	31.52%	9,709,542	28.60%	487,466	1.44%
Specialized Banks	199,471	0.59%	5,301	0.01%	123,144	0.36%	2,012	0.01%
MFIs	1,362,380	4.01%	22,281	0.06%	1,130,585	3.33%	63,316	0.19%
Total	18,358,840	54.07%	10,731,095	31.59%	10,963,271	32.29%	552,794	1.64%

Note: *In millions of KHR
Source: Compiled by author using data from Banking Supervision Department's Annual Report 2008.

Among the banking sector's total credit as of December 31, 2008, it is contributed mainly to wholesale trade (17%), hotels and restaurants (14%), retail trade (13%), manufacturing (10%) but to transport & storage, utilities, and financial institutions only 1% (Figure 1). The MFI's total loan contributes to agriculture (43.81%), trade and commerce (33.33%), households (7.72%), and construction (1.80%) (Figure 2).

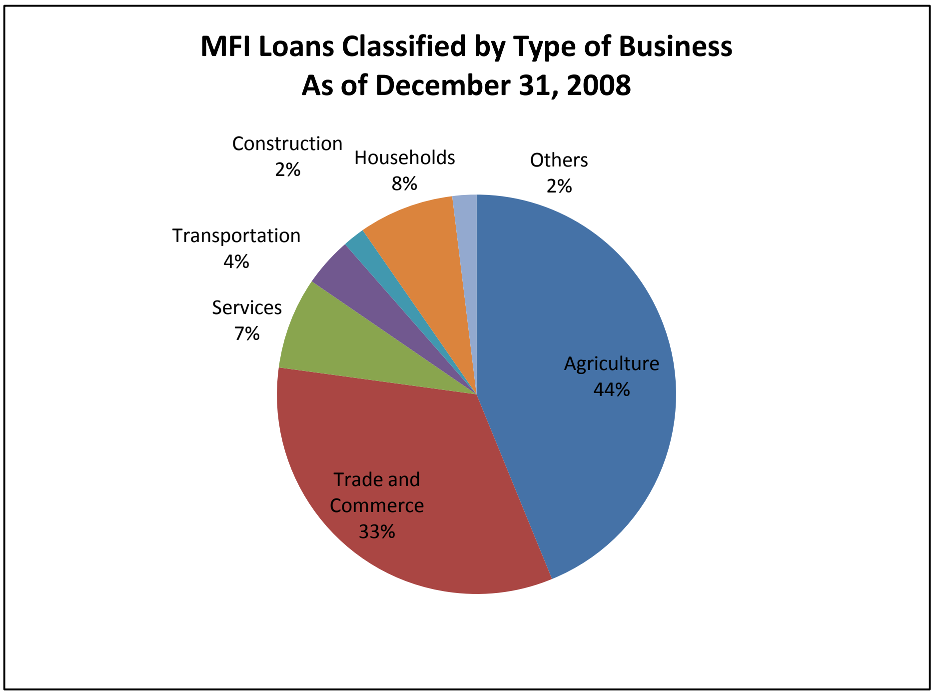
[1] The list of the central bank shows that 26 NGOs have registered with the central bank of Cambodia, so the NGOs which are not included in the list are informal.

Figure 1: Total Credit by Industry, December 31, 2008



Source: Banking Supervision Department's Annual Report, NBC (2008)

Figure 2: MFI Loans Classified by Type of Business, December 31, 2008

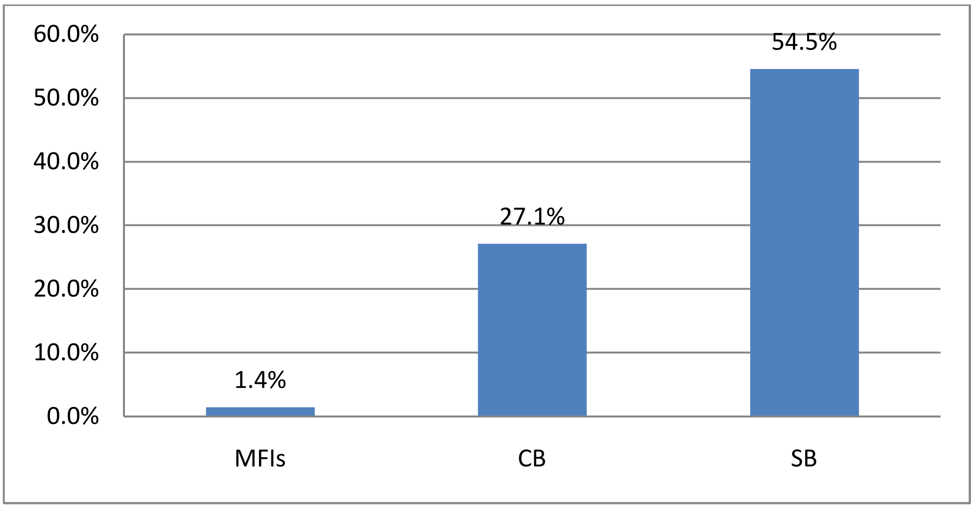


Source: Banking Supervision Department's Annual Report, NBC (2008)

3. The Problems of Financial Sector in Cambodia

The structure of commercial banks, specialized banks, and MFIs was analyzed to see the problems of the financial sector in Cambodia. As of December 31, 2009, there are 100 (around 54% of the total) offices of commercial banks, 19 (1.4%) MFIs, and 6 (27%) specialized banks in Phnom Penh. This indicates the concentration of the commercial and specialized banks in the city and the concentration of MFIs in and around the rural areas. This also shows the target clients which the banks and MFIs serve. (See Figure 3)

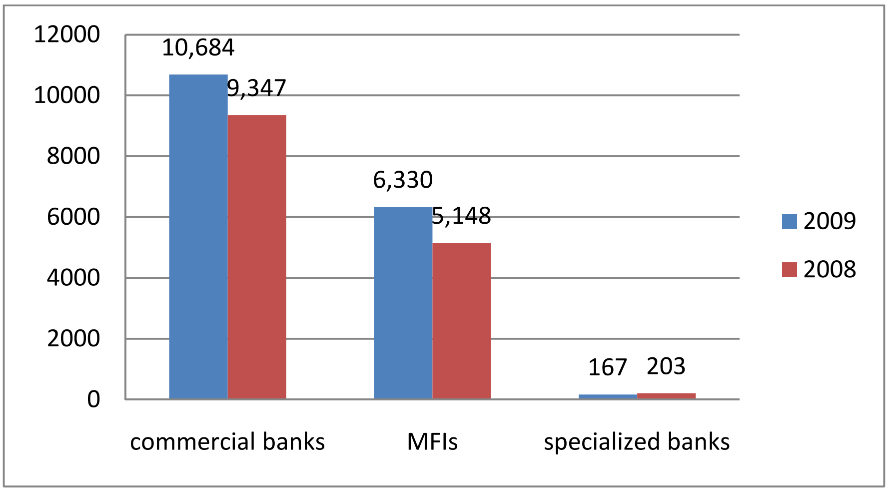
Figure 3: Distribution Percentage of Offices in Phnom Penh



Note: This figure is done by the author by using the secondary data from NBC.

The financial sector has employed a noticeable number of employees. Commercial banks employed 9,347 people in 2008 and 14% increase to 10,684 in 2009. MFIs also employed many staff: 5,148 people in 2008 and 6,330 in 2009. Finally, specialized banks employed 203 in 2008 but 17% decrease to 167 people in 2009. (See Figure 4)

Figure 4: Number of Staff



Note: This figure is done by the author by using the secondary data from NBC.

The characteristic of the commercial banks and MFIs' paid-up capital is inspiring. The share of Cambodian paid-up capital of banks and MFIs are 28.7% and 21.5% relatively. There is more foreign paid-up capital than domestic capital in the financial market in Cambodia. Seven banks including Canadia Bank Plc., Cambodia

Mekong Bank Public Ltd., Vattanac Bank Ltd., Foreign Trade Bank of Cambodia, Rural Development Bank, PHSME Specialized Bank, Anco Specialized Bank are pure Cambodian banks.

Cambodian MFIs consist of Cambodian Business Intergrate in Rural Development, Entean Akpevath Pracheachun, First Finance, Intean Poalroath Rongroeung, Tong Fang Microfinance, YCP are Cambodian microfinance institutions.

The following is the analysis of the distribution of banks' and MFIs' assets as of December 31, 2009. For commercial banks, around 48% of the assets are distributed to loans and advances to private sector, and 29% is distributed to the central bank. The deposits with, loans and advances to banks is only 6.7%. A similar trend is for specialized banks: 64% to loans and advances to private sector, 14% to the central bank, and 6% for the deposits with, loans and advances to banks (Table 2). Assets of MFIs are contributed as loans and advances to customers for 81%, and as cash and balance with NBC and other banks for 16% (Table 3).

The analysis demonstrates that the main distribution of assets of MFI to the customers is higher than that of the commercial bank in Cambodia. Commercial banks have to deposit more (around 30%) to the central bank, which might cause credit rationing in the banking system.

Table 2: Percentage Distribution of Assets of Banks as at December 31, 2009

	Cash	Deposits With NBC	Due From Banks	Deposits with, Loans and advances to Banks	Loans and advances to private sector	Accrued interest receivable	Prepaid Expenses	Fixed Assets	Other assets
Commercial banks	6.2	28.9	5.1	6.7	48.4	0.3	0.4	3.5	0.4
Specialized banks	9.7	14.1	1.1	6.1	64.1	0.7	0.5	3.5	0.2

Source: The data from NBC

Table 3: Percentage Distribution of Assets of MFIs as at December 31, 2009

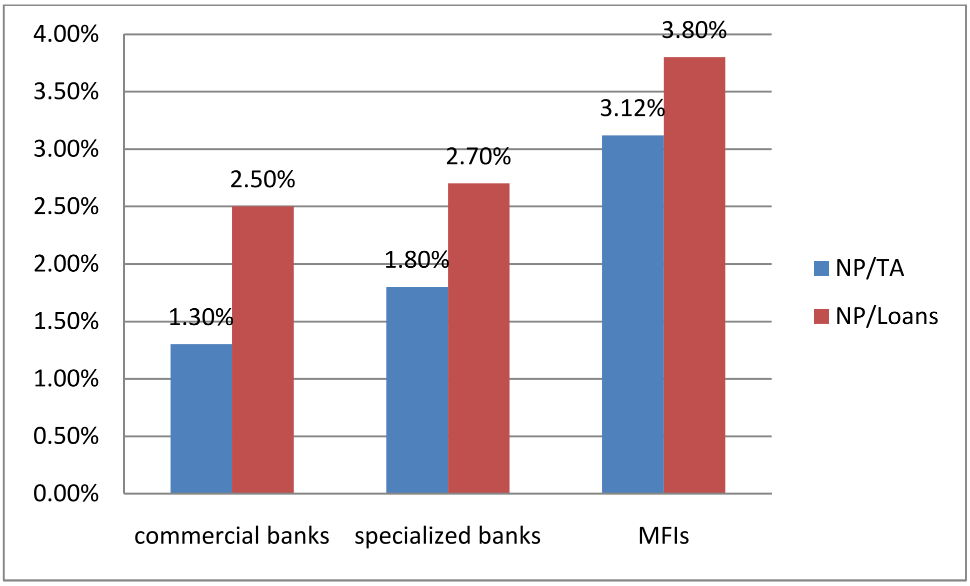
	Cash and Balance with NBC and other Banks	Loans and Advances to Customers	Prepayment and short term Receivable	Long Term Investment	Property and Equipment	Other Assets
MFIs	16.16	81.1	0.84	0.01	1.79	0.1

Source: The data from NBC

The distribution of liabilities and equity of the banks and MFIs demonstrates their operation management. For commercial banks, the main distribution is to demand deposits (13.6%), saving deposits (22%), and fixed deposits (31%). The distribution to the paid-up capital is also significant at 14.5%, and they owed to banks only at 8.4%. For specialized banks, the distribution is mainly for the paid-up capital (60%) and borrowed fund (26%). Interestingly, MFIs have to spend a lot on loan payables (75%) and paid-up capital (11%).

It is noticeable that the ratio of net profit to total assets and net profit to loans of MFIs are higher than those of the banks (Figure 5).

Figure 5: Net Profits to Total Assets and Loans



Note: This figure is done by the author by using the secondary data from NBC.

The delinquency ratio of the commercial banks and MFIs grow from 3.60% and 0.42% in 2008 to 4.40% and 2.80% in 2009 (Figure 6). In contrast, the delinquency ratio of specialized banks decreases from 9.30% in 2008 to 5.20% in 2009 (Figure 6). The highest delinquency rate of the bank is up to 36.40% in 2009 (Cambodia Mekong Bank Public Ltd.) (Figure 7) but 5.25% for Intean Poalroath Rongroeung (Figure 8).

Figure 6: Delinquency Ratio Summary of Banks and MFIs

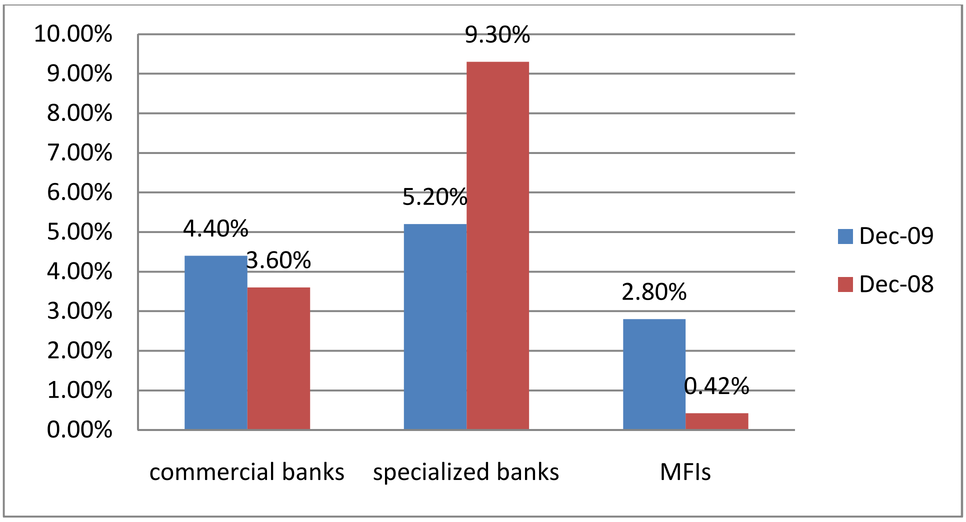


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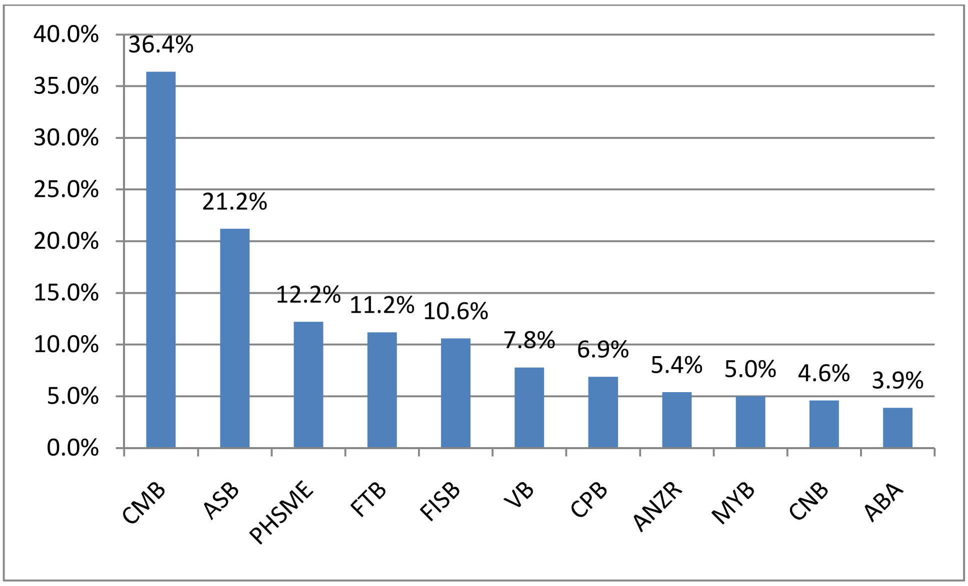
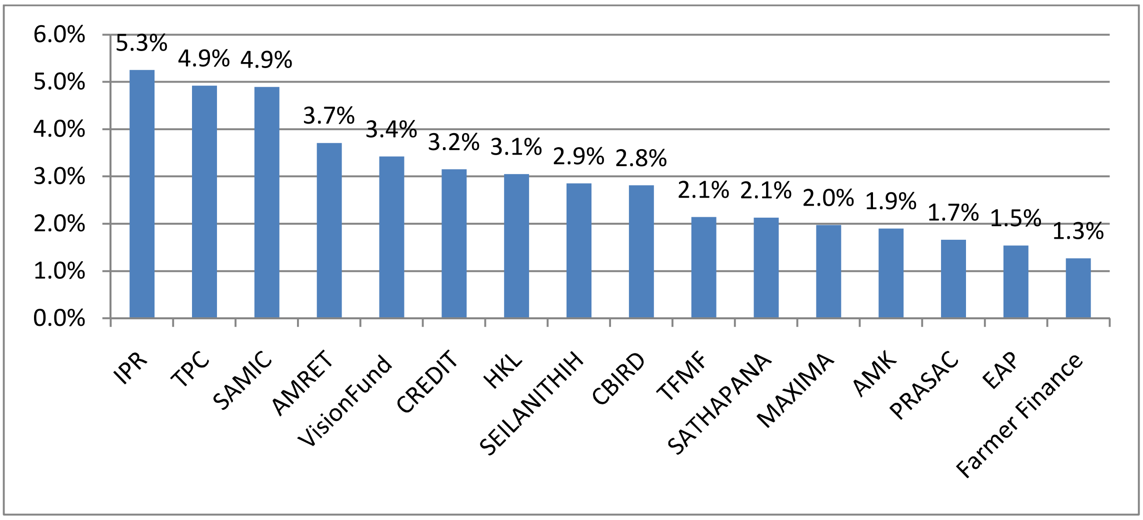
Figure 7: Delinquency Ratio of Banks as of Dec-09



Note: This figure is done by the author by using the secondary data from NBC.

Figure 8: Delinquency Ratio of MFIs as of Dec-09



Note: This figure is done by the author by using the secondary data from NBC.

Summarily, MFIs performed better than the bank because it has used asset wisely by providing more loan to the customers. MFIs get high profits and low delinquency rate if compared to the banks. The credit supply from the commercial bank is still limited because the bank has to put high deposits to the central bank of Cambodia and because the idle assets of the banking system are not effectively used.

This study is to analyze the linkage structure between the formal and informal financial sectors in Cambodia. To achieve this objective, the following questions need to be answered:

- To what extend have the informal /less formal financial sectors received loans from the formal sector?
- Are there any financial linkages in the banking system?
- What are the reasons of lacking of financial linkages?

4. Research Method

I interviewed both formal and informal financial sectors to find out the lending policies and the situation of the financial linkage of formal and informal financial sector in Cambodia. To triangulate the information, I interviewed the central bank of Cambodia and some NGOs as well.

5. Literature Review

The linkage study would be incomplete if there is no study about the characteristics or the strengths and weaknesses of the formal and informal financial sectors and the importance of financial linkage.

5.1 Operational Aspects of the Formal and Informal Financial Sectors

Germidis et al (1991) presents the characteristics of the formal finance as having rigid and bureaucratic procedures, cumbersome paperwork, high transaction costs (loan appraisal, documentation, and legal fees), and stringent collateral requirements for large sums of loans. The transaction costs when dealing with small clients are high, while interest rates are usually fixed at low levels by the monetary authorities.

However, informal finance is characterized by the flexibility of operations and loan terms (short-, medium-, and long-term), easily understood rules and regulations, rapid processing of requests and delivery of credit, willingness to handle the small amounts corresponding to the requirements and the capacity of clients, minimal red tape involved in transactions, low transaction costs in the informal sector and higher interest rates but higher repayment rates. The transactions are face-to-face relationships between creditor and debtor. No collateral is involved but sometimes tangible guarantees (such as jewellery, household appliances, etc.). Security on loans is dependent on the borrower's past savings and credit record and on social pressure to abide by certain rules of behavior. Furthermore, in the informal financial sector, default risk is minimized because the information on the credit worthiness of potential borrowers can be obtained easily and cheaply; lenders usually live and work in the nearby area of their financial operations, which allows for effective follow-up on outstanding loans. Also, lenders employ an additional means of minimizing default risk through interlinked credit contracts and through the overlapping roles of money-lenders, landlords, employers, or produce dealers.

Germidis et al (1991) also presents the two main arguments for the interest rate differential between the two financial sectors. The first argument is that informal credit markets are non-competitive and lenders have monopolistic control extracting substantial rents by taking advantage of the relative inelasticity of demand for credit by informal sector clients. The second argument is that the informal sector is competitive and that interest rates reflect the real cost of loanable funds. The two arguments are difficult to be judged because it is difficult to estimate the share of the various determinants of interest rates: a premium to cover transaction costs, opportunity cost of funds, a premium for risk, and monopoly profits in the global rate charges.

Although the characteristics of informal finance are better than those of the formal one, the informal finance is still limited, meaning that SMEs in Cambodia cannot get access to long-term and large amount of loans. To respond to this, many researchers and international organizations have raised the strategy of the financial linkage of the informal and formal financial sectors to ensure that more credit can be accessed by SMEs.

5.2 Financial Linkage

Many authors have emphasized the importance of both formal and informal finance and suggested various kinds of linkage between the two sectors. They have raised the importance and the successful cases of linkage. For example, Gallardo, Goldberg, and Randhawa (2006) showed that alliances and partnerships enabled the rural finance institutions to access significant new capital resources, manage transaction costs, acquire technical and management skills, link up to banking technology and infrastructure, and provide an expanded range of financial products and services. Moreover, Varghese (2005) added that if banks can link with moneylenders, borrowers can have access to further bank loans. Linkages can potentially improve upon a monopoly bank and bank competition. The result of the study indicates that borrowers can still prefer linkages to competition in the banking sector. Finally, Seibel and Parhusip (1990) denoted that linking informal and formal financial institutions, with financial self-help groups acting as intermediaries between micro-entrepreneurs and the banks reduces transaction costs substantially, for the benefit of both.

Seibel (1997) & (2006) presented the successful cases of linkage adopted by APRACA (pilot projects in Indonesia, the Philippines, Thailand, and Nepal). Starting in 1988, GTZ supported bilateral projects in Indonesia, the Philippines and Thailand. At the end of a two and a half year pilot period, 1600 SHGs, 16 bank branches and 15 NGOs had entered into commercial linkages in Indonesia. Later the methodology was conducted in India and AFRACA was established in 1996. As a result, ROSCAs in Gambia have been successfully linked to NGO banks. Finally, the real success of linkage was in India, where NABARD built what is now the largest and fastest-growing rural microfinance program.

As pointed out by FAO's publication "Expanding the Frontier in Rural Finance" in 2008, there are three mains kinds of linkages: informal sector driven linkage, formal sector driven linkage, and capacity-building driven linkages. The informal sector driven linkage means that the informal institutions established linkages with a range of financial and non-financial partners in order to expand their service offerings and/ or to establish more stable sources of funds. For examples, Gonzalez-Vega and Quirós (2008) presented about FADES, a non-regulated NGO and the third largest MFI in Bolivia which decided to enter into strategic alliances with several public and private institutions, with the sole purpose of expanding its rural outreach, despite the existence of restrictive legislation and infrastructure constraints. León (2008) presented the case of Confianza, a regulated MFI in Peru which was formerly an NGO, of which partnership with other MFIs and financial institutions in sustainable terms help the MFI to supply financial services in longer perspective while minimizing volatility risk of resources.

In regard to the formal sector driven linkages, they presented commercial banks and insurer which can reach rural markets through connecting with selected NGOs/MFIs. Harper and Kirsten (2008) pointed out a partnership between ICICI Bank and selected NGOs/MFIs, according to which the latter takes the responsibility of monitoring and recovering loans from individuals and self-help groups, but the credit (and most of the risk) is directly between ICICI Bank and the SHG or individual clients. Pathak (2008) presented an insurer named AVIVA India, a leading global insurance company, which has taken initiative and is developing linkages with some leading microfinance institutions (MFIs) to reach out to the rural market in a profitable manner.

The capacity-building driven linkages presented the range of strategies that different formal actors have undertaken when partnering with local organizations to cope with their low level of institutional capacity. It includes the case of FINCA/Costa Rica which specialized in the creation and linking of incorporated village banks with financial and non-financial actors in Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua (Gonzalez-Vega & Quirós, 2008), the diversity of intra-and extra-group linkages with a range of financial and non-financial sectors of the Jose Maria Covelo Foundation in Honduras (Falck, Quirós, and Gozalez-Vega, 2008), and the linkages between the Regional Development Bank (BPD) and village credit institutions (LPDs) in the province of Bali (Budastra, 2008).

Besides the linkage suggested above, Seibel (1997) proposed four linking methods such as downgrading, upgrading, linking formal and non-formal financial institutions, and infrastructural innovation (establishing new microfinance institutions). Aliber (2002) proposed that the elements of informal financial institutions can be strategically borrowed and adapted to suit the needs of the MFI or bank. Furthermore, MFIs and banks can seed to form strategic links with informal financial institutions. Finally, Germidis et al (1991) suggested the financial integration (horizontal integration) and interlinkage (vertical integration).

5.3 Vertical linkage or horizontal linkage?

Many researchers have emphasized the importance of formal finance to economic growth in comparison with informal finance. In order to provide credit to SMEs, some of them have suggested various linkage techniques including the vertical linkage between formal and informal finance. The effectiveness of such mechanisms is questionable because there can be a case of collusion, strategic cooperation, or monopolistic competition among the credit suppliers. Furthermore, some authors have also raised the constraints of the development of such a linkage.

Floro and Ray (1997) looked at the evidence from the Philippines and proposed that the effects of stronger vertical links depended on a form of the lenders' competition. If the relationship between lenders is one of strategic cooperation (collusion), an expansion of formal credit may reduce the expansion of the supply of credit.

In addition, Hoff and Stiglitz (1997) did not support the policy of vertical linkage by claiming that subsidies may have perverse effects under monopolistic competition. The negative externalities among suppliers may raise the informal interest rate by raising the costs of loan enforcement which results from an increase in the number of lenders in the informal credit market. Their findings were parallel with the puzzling evidence that injecting of government-subsidized formal credit have not improved the terms offered by moneylenders.

However, Chaudhuri and Dwibedi (2002) found that the policy of forming vertical linkage between the formal and informal credit institutions is clearly superior to a policy of horizontal linkage (substituting the informal sector by the formal one). They pointed that the policy of vertical linkage ensures lower informal interest rate and higher agricultural productivity if compared with horizontal linkage case. They also studied the case of collusion between the informal lenders and found that the interest rate is still lower in the vertical linkage case, which is in contradiction to the findings of Floro and Ray (1997) and Hoff and Stiglitz (1997).

Even though the possible linkages of informal and formal sectors have been suggested, many problems of the development of such a linkage have been perceived. For example, trying to propose to organize the opportunities for improving and extending financial markets and safety nets for the poor, Conning and Kevane (2002) suggested four explanations for the sluggishness of adoption of the linkage: problems of information asymmetry, lack of intermediary capital, and crowding-out; lock-in and few incentives to deal with an intermediary from the more anonymous national market; social norms against cooperation with intermediaries; and political economy model of resistance to new institutions because of possible shifts in relative bargaining power.

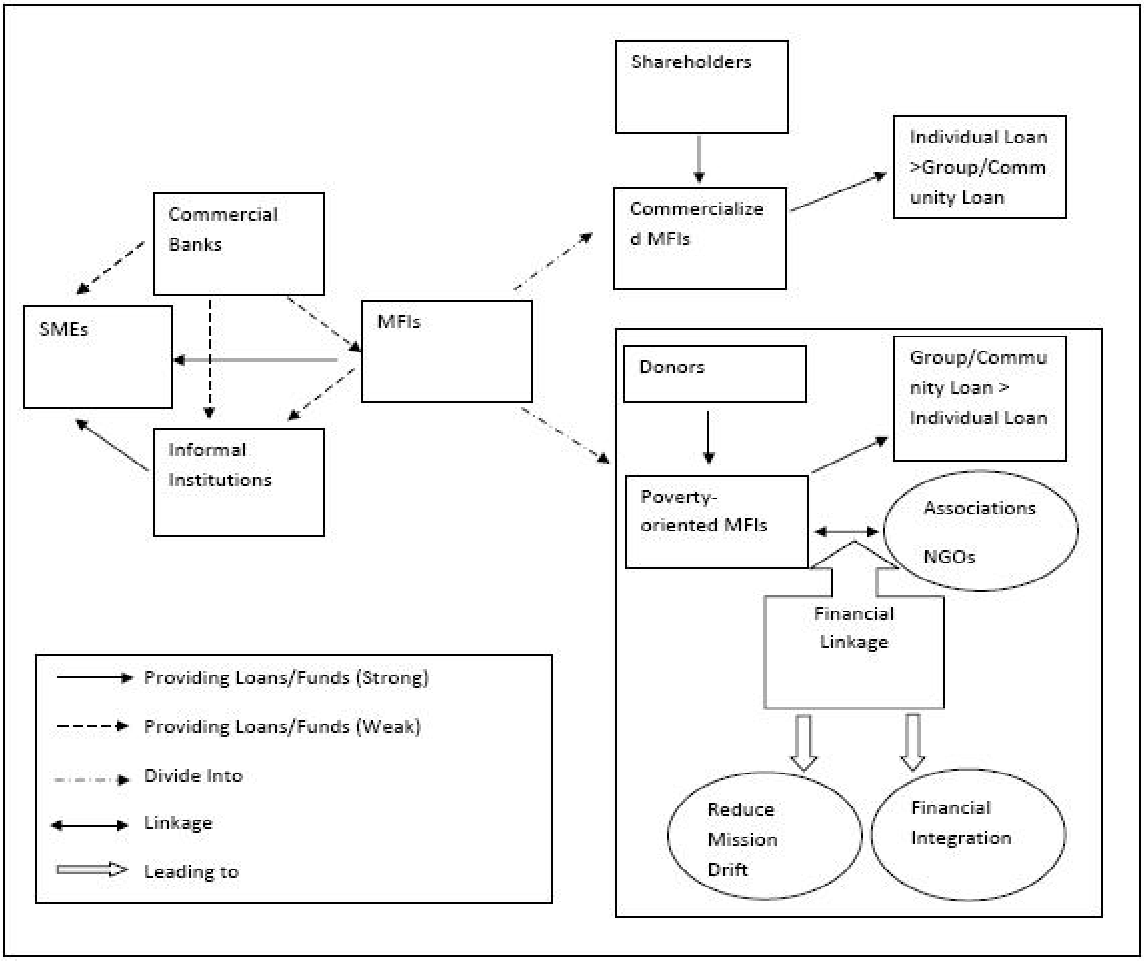
In addition, Pagura and Kirsten (2006), who studied about formal-informal financial linkages by conducting twelve case studies in eleven countries in Africa, Asia and Latin America, showed that formal financial institutions increasingly used financial linkages to target rural clients by taking less formal or rural financial institutions as linkage partners. They confirmed that even though financial linkages seems promising they are difficult to set up and manage, require less strong formal as well as formal institutions, and rarely yield a significant expansion of financial services beyond credit.

Aryeetey (2008) remarked that many formal financial institutions in Sub-Saharan Africa have not linked up with informal finance sector because of considerable distrust, inadequate knowledge about the informal sector and in some cases prejudice. Therefore, there is an obvious need for national policy frameworks that have appropriate levels of incentive and regulatory policies as a context for achieving these desired linkages. It is also necessary for this framework to draw on broader economic relationships by ensuring that the approach is truly driven by demand from the real sector.

6. Framework of the Study

There are likely to be two groups of microfinance institutions in Cambodia. The first one is a profit-oriented MFI, of which most of their funds owned by shareholders and least from donors. The first group tends to get access to commercial banks' loans for the back-up of the illiquidity. The second group, on the contrary, mainly receives funds from donors, which aim at reducing poverty. They tend to link with other associations and NGOs to get access to more funds to serve specific group of clients (Figure 9).

Figure 9: The Financial Linkage Framework



7. Findings

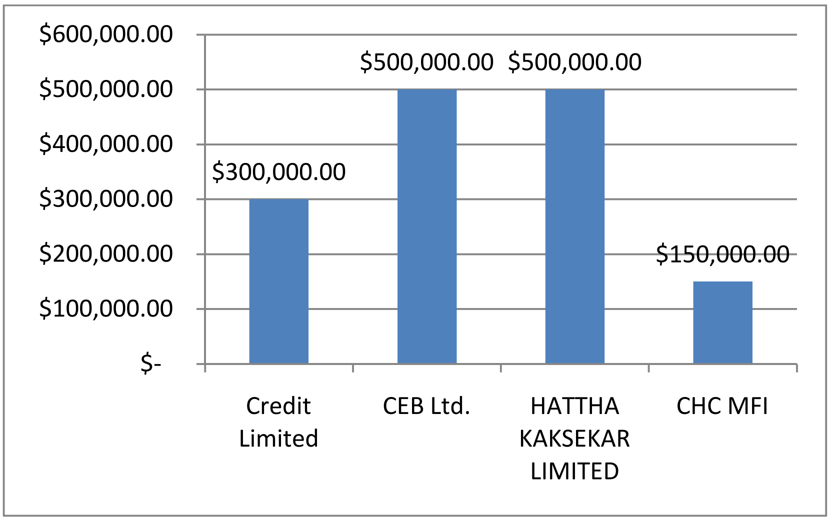
The following section is the result of the analysis of the information gathered from the commercial banks, MFIs and NGOs. The analysis mainly focuses on how commercial banks and MFIs link with other institutions and also the problems of the linkage.

7.1 Commercial Bank and the Financial Linkage

Acleda Bank is one of the famous banks in Cambodia. According to its loan characteristics and criteria, Acleda provides loans to various kinds of clients, including credit lines to MFIs as well. The following graph shows the credit line amount as of the end of January, 2009 of about 0.26% of the total loan in December 31, 2009 (Figure 10) and as of the end of January 2010 of about 0.12% to the total loan in December 31, 2009 (Figure 11). The credit lines are mostly used for the reserve funds. Only six out of eighteen MFIs can get access to the credit lines of Acleda Bank, probably partly due to the urgent demand of the institutions.

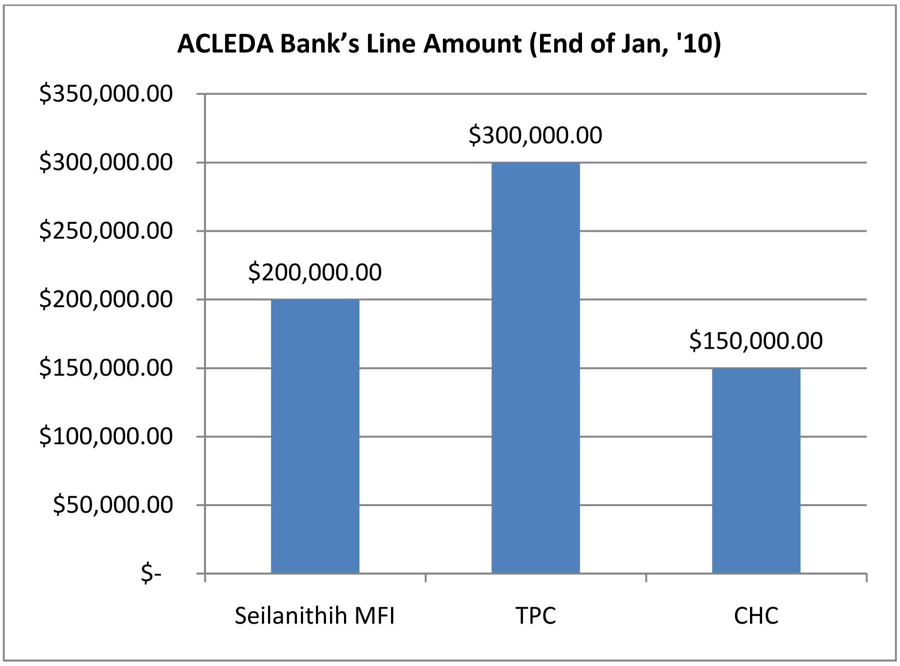
The analysis of the data above is reinforced by the results of the interview with a credit supervisor at Steung Meanchey Branch. According to the interview, he claimed that Acleda is willing to provide loans to any NGO, association, and informal lender with special interest rate. However, the bank rejects all the linkage requests from any institutions because he claimed that the linkage will not work in the case of Cambodia. Currently, the bank has just announced the new mobile financial services system in Cambodia while Wing Mobile is affiliated with other financial institutions in Cambodia such as VisionFund and AMK.

Figure 10: ACLEDA Bank's Credit Line to MFIs (End of Jan, '09)



Source: The figure is done by the author using data from ACEDA BANK

Figure 11: ACLEDA Bank's Credit Line to MFIs (End of Jan, '10)



Source: The figure is done by the author using data from ACEDA BANK

7.2 MFIs and the Linkage

As a result of the interview, there are two kinds of microfinance institutions in Cambodia. The first group is more social-oriented and the second group is more profit-oriented. Both of them have different and similar characteristics, and we can see through their vision and mission. The pro-poor group mostly get fund from the international organizations or associations and tend to link with other local and international financial institutions. They mainly focus on the group/community loans (loans which are provided to the poor).

In contrast, the second group tends to receive funds from the shareholders, who are likely in the risk-averse countries, plus the funds from donors. They sometimes get loans from the commercial banks and institutions to meet their short-term illiquidity. They tend to deviate from the financial linkage or reject the request from any external financial organizations or associations. They see the linkage as the hindrance for their profit earning because they perceive the linkage as a complicated or sophisticated system which is costly and hard to manage. This kind of group tends to focus on the individual loans with a large amount of loan size because it is more secure with collaterals.

The example of the first group of financial institutions is VisionFund MFI whose mission is to provide financial services to help the poor liberate themselves from poverty. It is a huge mission for the company since there are lots of poor people in

Cambodia. According to the result of the fieldwork study, the company has joined partnership with many institutions such as World Vision, KHANA, Plan Cambodia, ILO in Cambodia, Hagar, Wing, and CEDAC. As pointed by the prevailing missions of the mentioned organizations, VisionFund has provided financial services to the clients of the organizations' members. It includes Food and Water Security, Health and Nutrition, HIV/AIDS, Peace and Justice, and Education, Agricultural Activities, Child Labor, Women Employment, Mobile Financial Services, and Enhanced Agriculture Productivities. The linkage points out the strongest point of VisionFund Cambodia although it is hard for the institution to control. According to the Senior Operation Manager, the financial partnership or linkages with other NGOs is complicated system and hard to control. It might be a part of the reason why the growth of the company is sluggish during the economic crisis, in addition to the willingness to stick to the mission which is to help the poor out of the poverty.

VisionFund receives loans from various financial institutions such as Deutche Bank, Oikocredit, Blueorchard, ANZ Royal, Planet Finance, DWM. Among the institutions, only ANZ Royal is located in Cambodia so we can see the linkage from the bank to MFI. The question is why VisionFund cannot receive fund from other domestic banks.

The financial linkage of VFC is complicated. Even though the linkage exists between VFC and the partners, the clients have to present their collaterals before getting a specific number of loans.

At another end of linkage, VisionFund also has intention to provide loans to the informal moneylenders, other NGOs, or associations directly as long as they have collateral to back up. Still, collateral is needed for the NGOs or associations which are not well linked with the company.

AMK MFI is another example of the first group of MFIs. AMK MFI is an exceptional case and its mission is "to help large numbers of poor people to improve their livelihood options through the delivery of appropriate and viable microfinance services." It has partnership with many international organizations such as IFC, KIVA, UNITUS, Imp-Act, and the Clean Business Initiative.

AMK just starts mobilize savings to be used as a source of fund. Mostly, they get unsecured loans and external funds with low interest rates. The interest rate is very low compared to local banks. It gets funds mainly from various shareholders (Concern Worldwide, Dublin & UK), lenders abroad (Moringaway, ICO, Symbiotics SA Information, Oikocredit, Hivos-Triodos Fonds, BlueOrchard, Rural Impulse Fund, KIVA Microfunds, The Minerva Treehouse, Micro Finance Alliance Fund), and Foreign Trade Bank of Cambodia (FTB). AMK gets loan from FTB to hedge against the exchange risk. AMK has not received loans from the banks (beside FTB) in Cambodia yet since the banks are not open to MFIs and interest rate is still expensive compared to AMK's partners.

AMK puts deposits (the leftover fund) to ANZ Bank because of its fame, and it puts deposit at Acleda Bank because it has branches in 24 provinces so it is easy to clear money and payroll payment.

Related to the linkage, AMK is not willing to provide loan to the clients (NGOs, Associations, money lenders) which borrow the credit to relend because it is the conflict of interest, which is a bit different from VisionFund. AMK is afraid of the influence of the association leader on the members (charging higher interest rate) and beside the small-scale association is fragile. However, it takes partnership with Wing in 2010 piloting for 3 years.

Based on the interview with the Product Development Manager, the difficulty of linkage is the Mission and Vision of each institution. If their missions are the same, the linkage is easy. Moreover, the operation department has to expand their transactions. He said, “Our partners do not understand our business clearly so it is time-consuming to work with each other.” He raised the advantage of the linkage that it is a kind of synergy business and it can boost better services.

The example of the second group is Sathapana Limited of which the mission is “to empower entrepreneurial poor people, especially women in urban & rural areas to develop their income-generating activities & micro-enterprises through access to microfinance services, including credit & saving, at reasonable rates.” It follows the model of Acleda Bank with the hope to get more profits and savings in order to attract more shareholders. However, it has rejected the requests from Forte Insurance company and Wing Mobile.

The linkage between MFIs and the commercial banks can make the banking system in Cambodia more systematic in a sense that the financial liberalization can be fastened, but there needs to be more prudential regulations and safeguard framework to avoid the system risk occurring during the crisis.

7.3 Wing Mobile, CEDAC, NBC

To understand more about the linkage, some companies, NGOs, and the central bank of Cambodia were interviewed. Wing is a subsidiary of ANZ Royal (55%) and the rest from Royal Group. Wing gets license from NBC so it can operate in KHR and US dollar. The purpose is to serve the people who do not have bank accounts and people who are ignored by the banks. Wing has many cash outlets with around 650 merchants: cell phone shops, money exchange places, pharmacies. Wing also uses Wing pilot sale force plus commercials, radio, financial literacy, and bill board.

Wing provides the products such as cashing, deposit, payment, wing-to-wing and wing-to-no-wing transfer, phone top-up and bill payment. It has linked with almost all phone operators and two MFIs (VFC, AMK) to share benefits.

Based on the interview with the Strategic Partner Manager, the difficulties of linkage are regulations, technical and process of linkage. He said Wing Mobile plan to link with other MFIs and international organization such as UNICEF.

Cambodian Center for Study and Development in Agriculture (CEDAC) was set up in August 1997 as a national Cambodian NGO to develop sustainable agriculture and rural development in Cambodia in response to the country’s desperate need for national construction. CEDAC has set up many kinds of groups including Saving for Self-

Reliance or Saving Group. There are 5,085 groups, 88,631 members (Female: 56,686) in 20 provinces, and the total amount of savings is around 4 million US dollars.

So far CEDAC takes partnership with VFC so that VFC can give loans to its famers' association (25 groups in 8 provinces) but so far VFC could provide loans to one group only based on its collateral (land and rice storage). CEDAC is willing to guarantee (100%) the famers' association but VFC has not accepted it yet.

Based on the result of the interview with the National Bank of Cambodia (NBC), the interbank market is not yet ready, but there is only loan agreement among banks which have good relationship. NBC can provide loans to the commercial bank when they face shortage of liquidity but collateral is needed.

The Central Bank cannot interfere with the commercial banks' transactions although it requires the commercial banks to have sound lending policy and loan committee. Therefore, the commercial bank can provide loans to any kind of borrower but the amount cannot exceed 20% of the net worth.

Regarding the financial linkage, the Deputy Division Chief, MFIs Supervision Division said, "NBC cannot interfere with the financial linkage but the linkage sounds promising."

8. Conclusion

In conclusion, the financial linkage among the formal, semi-formal, and informal financial sectors is still limited in Cambodia, but there is a possibility to expand if the central bank plays a role as a facilitator and if the banks and MFIs shift their strategies by accommodating deposits/savings from saving groups. In addition, the banks and MFIs have to show their willingness and have to expand their internal structure such as the operation section's workloads.

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