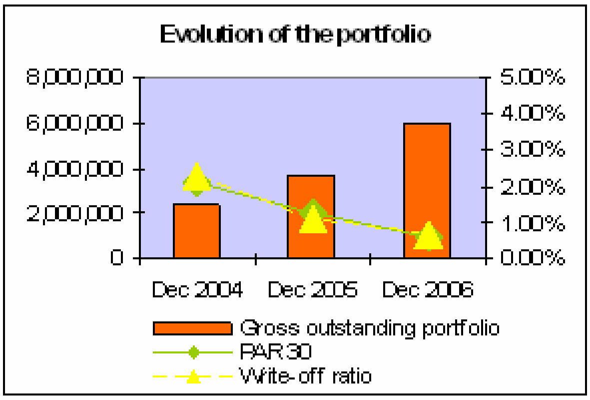
February 2007

Hattha Kaksekar Limited (HKL) – Cambodia

Final rating		BBB+
Outlook	Positive	Validity: 1 year if no relevant changes in operations or within the operation context will happen.
First rating		

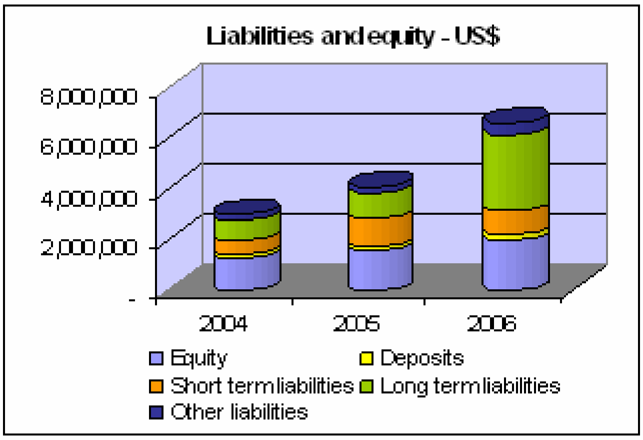
Hattha Kaksekar Limited (HKL) was established in 1996 as a non-governmental organization thanks to the initial support of OCSD/OXFAM from Canada. HK NGO started its microfinance program in the Pursat province providing financial services to the poor. In 2001, in order to accomplish with the regulation issued by the National Bank on licensing MFIs, HK NGO registered the limited liability company (HKL). Over years HKL expanded geographically opening 7 branches and 21 sub-branches and has been able to manage a successful growth of portfolio, getting to an outstanding portfolio of almost US$ 6ml. In the last three years HKL has continued to consolidate its organizational and financial structure, maintaining a very good portfolio quality and strengthening its performances. HKL portfolio is mostly financed by commercial liabilities.

Legal form	Limited Liability Company
Starting date	1996 – 2001 (licensing)
Network of reference	-
Area of activity	rural, peri-urban
Credit methodology	Individual and group



US$	Dec 2006
Average disbursed loan size	629
Gross outstanding portfolio	5,950,760
Total assets	6,566,064

Number	2004	2005	2006
Active borrowers	6,620	8,475	11,490
Branches (hubs)	5	6	7
Satellites	15	18	21
Total staff	113	139	169
Loan officers	35	43	58



Financial Indicators	2004	2005	2006
PAR 30	2.1%	1.3%	0.6%
Write-off ratio	2.3%	1.1%	0.6%
Restructured loans	0.0%	0.0%	0.0%
ROE	18.7%	29.8%	39.4%
AROE	6.4%	9.6%	12.4%
Oper. Self-sufficiency (OSS)	123.4%	130.8%	146.1%
Fin. Self-sufficiency (FSS)	123.0%	123.4%	128.4%
Staff productivity (loans)	59	61	68
LO productivity (loans)	189	197	198
Operating expense ratio	26.4%	20.7%	17.3%
Funding expense ratio	2.2%	4.5%	5.8%
Provision expense ratio	0.0%	0.7%	0.6%
Portfolio yield	33.5%	33.5%	33.7%
Risk coverage ratio	274.6%	201.9%	261.5%
Cost of funds ratio	6.0%	7.4%	8.4%
Debt/Equity ratio	1.3	1.7	2.4

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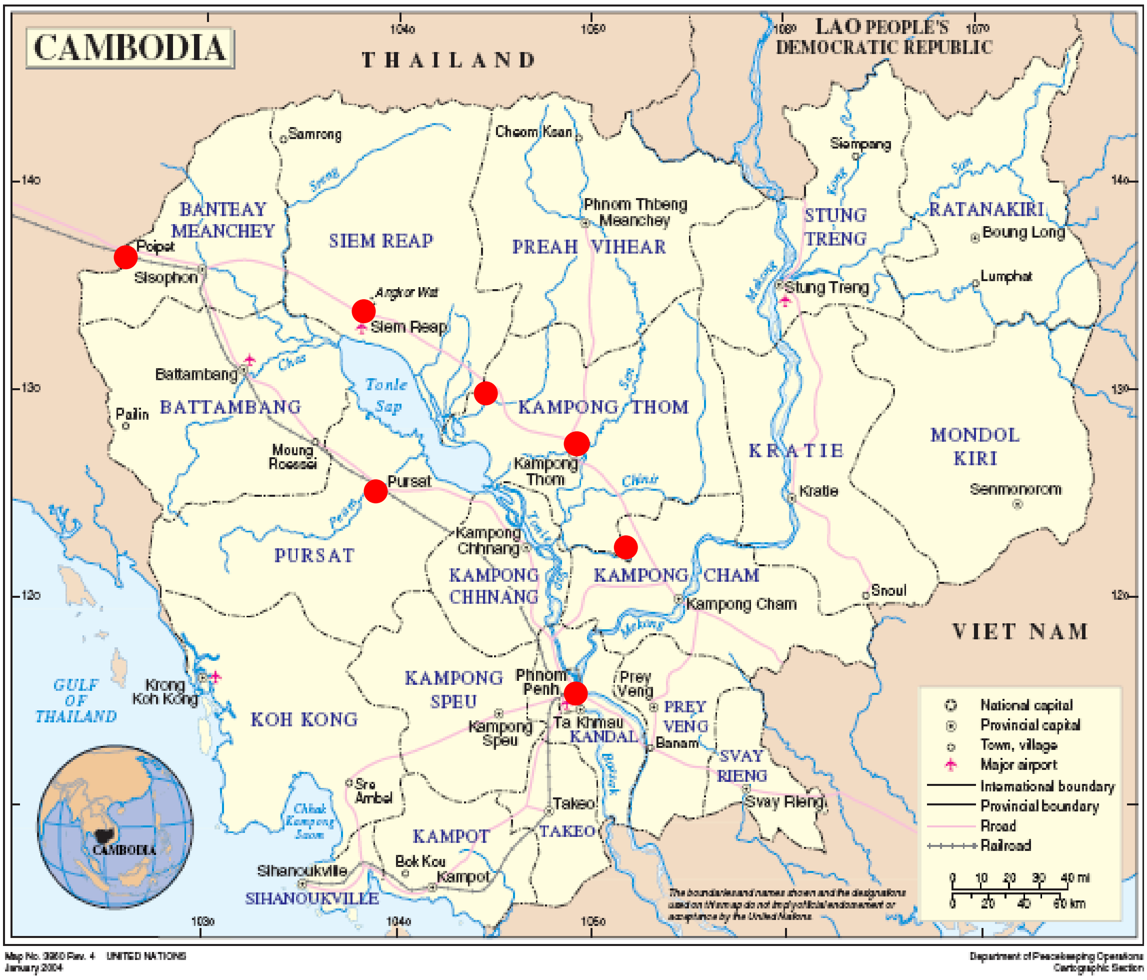
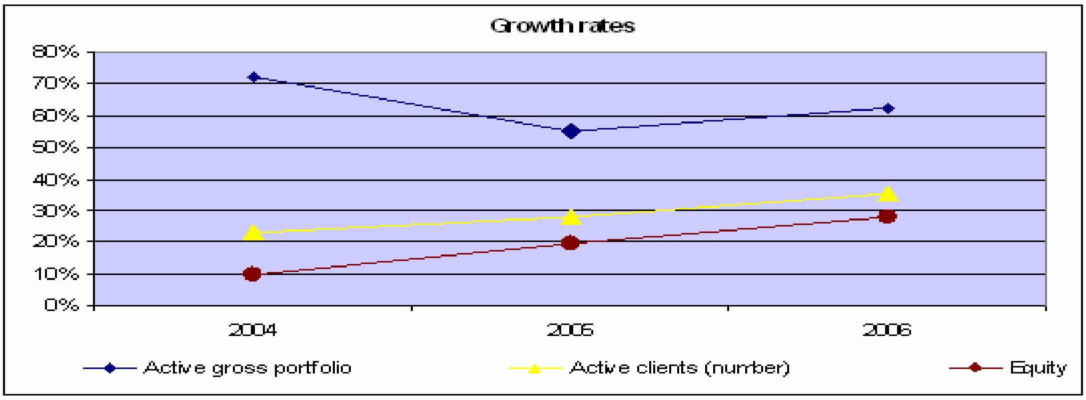
AREA	Risk factors	Relevance*
External environment	Increasingly competitive environment	Medium-high
	Lack of a credit bureau and exchange of clients information	Medium
	Not full availability of land titles	Medium
	Uncertainties related to savings mobilization	Medium-low
Governance, management and operations	Management members sit in the Audit Committee	Medium-high
	Overweight of management member within the BoD	Medium
	Low frequency of BoD meetings	Low
	Shortcomings in the MIS	Medium
	Staff capacity building in progress	Medium
	Control environment still to be strengthened	Medium
	Uncertainties linked to recent significant changes in policies and procedures	Medium-low
	Poor incentive scheme for LOs	Medium
	Relatively high staff turn over	Medium-low
	Lack of securities in documents storage	Medium
Financial products and asset quality	Limited development of savings products	Medium-low
	Ineffective tracking of client retention	Medium
Financial structure and ALM	Exposure to interest rate risk	Low
	Exposure to currency risk	Medium-low
Financial and operational results	Improvable staff allocation and productivity	Medium-low
Strategic objectives and future	Uncertainties linked to BoD decision on shareholders structure	Medium-high

* Relevance refers to the damage/loss brought about by negative events (associated to each risk factor) and to the probability that damage/loss eventually occurs.

Strengths	Opportunities
– Skilled and committed staff – Proactive governance – Flexible products – Good relationship with lenders	– Savings mobilization – Equity investors

HKL branches and satellites:





Final opinion
Over the period of analysis, HKL has been characterized by a continuous consolidation of its organizational and financial performance, steadily growing and strengthening its geographical penetration. HKL has improved its portfolio quality and increased its profitability levels overtime, also benefiting from economies of scale. Operating in an increasingly competitive environment, HKL offers flexible products and adjusts them to market conditions. HKL benefits from the dynamism of young personnel, even if for some departments and branch managers the capacity building process is still in progress. Senior management is skilled and committed, but their involvement in the governing bodies may result overweight and potentially generate conflicts of interest (they also sit on the audit committee). A contribution for offsetting this situation is expected to come from the step-in of new shareholders; nevertheless, uncertainties are still linked to the future balance within the shareholders composition. For what concerns operations, the strengthening of the MIS and audit system has still to be completed.

Benchmarking

The benchmarking analysis includes the comparison of HKL's performances with the *MicroBanking Bulletin* (MBB) database updated as of December 2005. Financial ratios considered within the benchmarking analysis do not fully correspond to the ratios calculated by *MicrofinanzaRating* presented within the present rating report (see Annex 3), as they are calculated according to the *MicroBanking Bulletin* (MBB) methodology[1].

Financial ratios	HKL	Asia Medium Non FI	Individual	High end target	Cambodian MFIs
Gross Loan Portfolio gross loan portfolio adj for standardised write-offs (US$)	5,933,866	3,961,878	8,959,428	18,631,924	4,426,465
Average Loan Balance per Borrower on per capita GNI Average loan balance per borrower/ GNI per capita(%)	112.3%	21.1%	61.4%	174.6%	42.5%
Portfolio at Risk> 30 Days oustanding balance of loans overdue>30days/gross loan portfolio (%)	0.6%	1.5%	2.3%	1.3%	0.6%
Adjusted Return on Equity AROE adj net operating income after taxes/avg tot equity (%)	10.1%	1.1%	5.9%	5.6%	5.6%
Portfolio yield Financial Revenue from Portfolio/ Adjusted Average Gross Portfolio	33.7%	34%	30%	24%	37.7%
Debt/ Equity Ratio adj.tot.liabilities/adj.tot.equity	2.4	2.9	3.9	4.6	0.7
Operating Expense/ Loan Portfolio (operating expense + In-Kind donations)/avg gross loan portfolio (%)	20.5%	21.4%	16.4%	11.8%	22.2%
Borrowers per Loan Officer n. of active borrowers/n. of loan officers	182	222	205	141	209

Asia Medium, Non FI, Gross Loan Portfolio (US$) 2 to 8 million, Voluntary Savings/ Total Assets < 20%

All figures are referred to the MicroBanking Bulletin database updated as of December 2005

Figures on Cambodia refers to the Benchmarking of Asian Microfinance 2005 issued by the MIX and include data from 9 MFIs

HKL appears to serve a higher target population than the Cambodian and regional peer group, which partly explains its lower productivity in terms of borrowers per loan officer. Operating expenses seem to be improvable, especially taking into consideration the size of the average loan and the lending methodology.

HKL shows a very good portfolio quality, in line with the national peer group and better than the Individual methodology peer group. The institution also shows good results in terms of profitability, as shown by the AROE. On the other hand, this difference is striking when compared to the regional peer group, with similar operating expenses, leverage and portfolio yield.

Portfolio yield is slightly lower than the Cambodian peer group.

[1] The MBB adjusts the financial data to produce a common treatment for the effect of: a) inflation, b)subsidies, and c) loan loss provisioning and write-off (see *MBB* , Appendix I: Notes to Adjustments and Statistical Issues).

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1. External Environment and HKL positioning

Institutional background

Hattha Kaksekar Limited (HKL) was established in **1996** as a NGO thanks to the **initial support of OCSD/OXFAM from Canada**. HK NGO started its microfinance program in the **Pursat province** providing financial services to the poor. In **2001**, in order to accomplish with the regulation issued by the National Bank on licensing MFIs, **HK NGO registered the limited liability company HKL**.

Over years HKL expanded geographically opening **7 branches and 21 sub-branches,** reaching an **outstanding portfolio** of almost **US$ 6 million**. In the last three years HKL has **consolidated its organizational and financial structure**, maintaining a very good portfolio quality and strengthening its performances. HKL portfolio is mostly financed by **commercial liabilities**, as a result of a positive relationship with international investors.

Political and macroeconomic context

Cambodia still suffers from the legacy of **20 years of civil unrest** (1970–90). During that period, a significant number of educated Cambodians fled the country, and government structures were not fully operational, if they existed at all. The **social and economic infrastructure of the country**, including the financial and banking sector, was **virtually destroyed by the Khmer Rouge** condemning the country to isolation. Today, with a **GDP per capita of US$ 460**, Cambodia is one of the poorest countries in the region: 40% of population lives below the national poverty line, and 20% of households are headed by a female.

Cambodia

Macroeconomic Indicators	Dec 2003	Dec 2004	Dec 2005	Dec 2006
Exchange rate in US$ (end of period)	3,984	4,027	4,112	4,057
Exchange rate variation	1.4%	1.1%	2.1%	1.8%
Inflation rate (end of period)	1.2%	3.9%	6.7%	5.8%
Deposit rate	2.0%	1.8%	1.9%	1.8%
Lending rate	18.5%	17.6%	17.3%	16.4%
Real GDP growth	10.0%	8.6%	6.2%	6.3%*
GDP per head (US$)	333	372	427	466

Source: International Finance Statistics, EIU; National Institute of Statistics (NIS) of Cambodia
* Estimates of World Economic Outlook, IMF

With the signing of the **Paris Peace Accords in 1991** and the establishment of the UN peacekeeping operations, Cambodia emerged from its isolation. Hundreds of international organizations initiated relief and development programs to help reconstruct the country.

Starting from **1999**, the government has been making progress on **economic reforms**. The US and Cambodia signed a Bilateral Textile Agreement, which gave Cambodia a guaranteed quota of US textile imports and established a bonus for improving working conditions and enforcing Cambodian labor laws and international labor standards in the industry. From **2001 to 2004, the economy grew at an average rate of 6.4%,** largely driven by an expansion in the **garment sector** and tourism. With the expiration of a WTO Agreement on Textiles and Clothing in January 2005, Cambodia-based textile producers were forced to compete directly with lower-priced producing countries such as China and India. Although initial 2005 GDP growth estimates were less than 3%, better-than-expected garment sector performance led the growth rate to stand at 6.2% in 2005, whereas for **2006 growth rate was expected to remain stable around 6.3%**.

Moreover, the Royal Government has succeeded in keeping **a manageable inflation rate over the past years**, annual average 3.9% and 5.8% in 2004 and 2005 respectively, when it registered an increase due to raised oil and foods prices.

In December 2004, official donors pledged US$ 504 million in aid for 2005 on the condition that the Cambodian government implements steps to reduce corruption in order to strengthen credibility and transparence in efficiently allocating public resources. From an economic perspective, Cambodia's **main challenge is the promotion of a sound environment where the private sector is able to create jobs to handle Cambodia's demographic imbalance[2].** The population lacks education and productive skills and the countryside suffers from lack of basic infrastructure. 75% of the population is employed in subsistence farming.

Microfinance sector

The **microfinance** sector in Cambodia **was initiated** in the early 1990s by few organizations through **donor-financed credit projects** (including GRET, World Relief, the Association of Cambodian Local Enterprise Development Agencies -ACLEDA- and CRS). Along the decade, such initiatives were transformed by donors, international implementing partners, and local stakeholders into a sector led by **profitable, regulated financial institutions**.

In September 2006, microfinance institutions have **total loans outstanding of US$ 75 million** provided to 419,000 clients and have **total deposits of US$ 2.4 million** (0.25% of total deposits in banks) mobilized from 141,051 customers, remaining a marginal activity (see below). The sector is rapidly growing, as loans outstanding increased by 37% in 2006.

Cambodia's microfinance is still benefiting from the support of the international community, especially the United Nations Development Program (UNDP), French Development Agency (AFD), Asian Development Bank (ADB) and other partners, for financial and operational development.

Currently, the microfinance sector in Cambodia is led by **ACLEDA Bank**, transformed from an NGO into a microfinance bank, and is followed by **17 licensed MFIs and 24 registered as rural credit operators**. Among these institutions, the **majority were transformed from NGOs**, while others were local private companies. In addition, a number of smaller NGOs and community-based organizations provide microfinance services.

No formal mechanism exists for MFIs **to exchange information** on borrowers while banks are in the process of launching their own credit bureau (even if just collecting information on bad debtors).

In order to meet their specific needs, licensed MFIs, legally represented by ABC (Association of Banks of Cambodia), established in 2004 the **Cambodian Microfinance Association (CMA)** which however is still not fully developed and operating.

Regulation and supervision

In November **1999** the National Bank of Cambodia (NBC) issued a **new law on banking and financial institutions**, followed in **2000** by a decree ('Prakas') **regulating** the **microfinance** industry by **licensing and registering major microfinance providers**. NGO and microfinance projects were given the opportunity to transform into formal financial institutions (limited liability company or cooperative), or simply to be registered when they do not qualify for licensing criteria. The new prakas (2000 and 2002) marked **a shift toward the commercialization of microfinance and its integration into the formal financial system** of Cambodia.

Registered and licensed MFIs are submitted to a set of regulatory and supervisory provisions, out of which the main are the following:

- **Licensing requirements:** a microfinance institution is required to be incorporated as a limited liability company or a cooperative. Minimum capital requirement for licensed MFIs is KHR 250 millions (US$ 60,800). The license needs to be renewed every 3 years. The annual license fee being KHR 1 million (US$ 243).
- **Supervision:** registered MFIs need to submit quarterly reports including: financial statements, breakdown of loans/deposits by sector and currency; loan classification and delinquency ratio and network of branches and offices. No on site supervision is required for registered MFIs, as supervision activities are concentrated on licensed MFIs. Licensed MFIs need to present monthly and annual reports including: audited financial statements,

[2] More than 50% of the population is below 20 year-old.

BOD annual report, statistics of staff and salaries; updated organization chart. Suspicious transactions should also be reported. Focus of off-site supervision is capital adequacy and loan performance, and a yearly on-site supervision is planned just for licensed MFIs (but in practice it is less frequent).

Up to now the NBC has proved to be flexible toward a growing microfinance sector, for instance softening the capital adequacy (from 30% to 20% of total assets). With regards to **savings mobilization**, the legal framework still lacks definition and MFIs operate in this respect in a vacuum, as it is tolerated that MFIs mobilize savings from their areas of operations, even if this leaves room for interpretation. So far no MFI has undergone any sanction and **the government is working on developing a specific regulation, in cooperation with ADB**.

HKL's market positioning

As of June 2006, HKL has a market share of approximately 1.8% of total microfinance borrowers (2.4%, when not considering ACLEDA), while its share of portfolio outstanding stands at 0.2% (9%, not considering ACLEDA).

Main competitors

Institution	N. of provinces	Products	Oustanding loan portfolio	N. of borrowers	Active interest rate
HKL	7	individual/solidarity/ savings	5,950,760	11,490	2-3% monthly for US$
PRASAC	12	individual/solidarity/ savings	13,647,202	78,476	3 - 3.5% monthly
CEB	5	individual/solidarity/ savings	8,621,168	11,982	3.5% monthly for Riel; 2% for US$
ACLEDA Bank	24	individual/savings	121,026,764	143,751	3 - 3.5% monthly
TPC	9	individual/solidarity/ savings	5,735,280	49,389	2.5% - 3% monthly/ 3% monthly
AMK	6	individual/solidarity/ savings	3,891,241	48,583	3% monthly
VFC	7	individual/solidarity/ savings	4,658,151	29,653	3% monthly
AMRET	12	individual/solidarity/ savings	13,277,129	122,891	2.75 - 3.5% monthly for US$; 3 - 3.5% monthly for Riel/ 3,5% monthly

HKL has developed its operations in rural and semi-urban contexts, especially consolidating and expanding its activities in the regions around the Lake. More recently, it is also consolidating its presence in urban areas, including Phnom Penh.

In recent years, **competition** on the microfinance market **has become more intense** due to the increasing number of practitioners and the inflow of available resources. This results into an increasing geographic overlapping, with previously specialized MFIs starting offering both individual and group loans in order to diversify their portfolios. In particular, this implies a growing competition in the market of **individual lending.**

On the other hand, as a consequence of this evolving market supply, there is a gradual change in the behaviour of clients that become more aware of the comparative benefits amongst different providers.

The combination of **higher competition** and **absence** of an **effective information exchange** brings about a risk of **overindebtedness** with potential negative impact on the portfolio quality of MFIs.

The **main competitive advantages** of HKL are the following:

- flexibility of the loan product in terms of repayment schedule tailored on the cash flow analysis, which also allows free principal prepayments;
- longer term for small loans;
- good product development and capacity to innovate.

HKL's **competitive disadvantages** include the use of compulsory saving (even if procedures may be flexible on that), while most competitors dropped it and HKL's limited experience in group lending.

Among HKL's main competitors are currently institutions like PRASAC, CEB and ACLEDA BANK PLC.

2. Governance and operational structure

Ownership and Governance

Hattha Kaksekar was established in 1996, after the spin-off from an OCSD/OXFAM project, started in 1994 to provide financial services to the poor in the province of Pursat. In order to comply with the regulation, the institution established **a limited liability company in 2001.** The initial paid-in capital worth US$ 77,850, subscribed by four shareholders (HK NGO, HK Staff Association, SIDI and an individual), was two years later increased up to more than US$ 250,000 thanks to the contribution of CORDAID. According to the current structure, **only the local HK NGO is influent shareholder**[3], while neither the international shareholders intend to overcome the threshold of 20%, even if they are committed to the consolidation of the institution, also through the opening-up of the capital to the participation of new shareholders.

Shareholders' structure		
	Amount in US$	%
HK NGO	128,550	49.86%
SIDI	51,450	19.96%
CORDAID	50,010	19.39%
HK Staff Ass.	25,320	9.82%
Mr. Dy Davuth	2,520	0.97%
TOTAL	257,850	100%

Board of Directors

Members	Charge	Background and current profession
ALKA COUET	Chairman	Ms. Couet has good experience in the financial and service market. She holds Masters of Business Administration and Masters of International Affairs. She Joined the Board of HK in November 2003, being a representative of SIDI.
HOUT IENG TONG	Member	Mr. Hout Ieng Tong is the General Manager of HKL. He is the founder of HK since 1996 and in the BoD he represents HK NGO. He has 13 year-experiences in Micro Finance and staff management.
IM VANDITH	Member	Ms. Vandith is the Deputy General Manager of HKL since 2002. She had attended many courses such as Project Planning, Monitoring and Evaluation for Micro-Finance Institution, Financial Analysis for Micro-Finance, Accounting.
TONY FERNANDES	Member	Mr. Tony Fernandes recently joined the BoD, as a representative of CORDAID.
DY DAVUTH	Member	He is a Cambodian private shareholder. He has wide experience in microfinance, having been working with AMRET. Currently, he is working for Build Bright University, a private university. He entered HKL BoD in 2004, becoming also Chairman of the Audit Committee.
SREY CHANTHY	Member	He joined the Board in 2003. Currently, he is a consultant for various donors and consulting firms, including Asian Development Bank, World Bank, SIDA, CIDA, DANIDA, USAID, Oxfam America, etc.

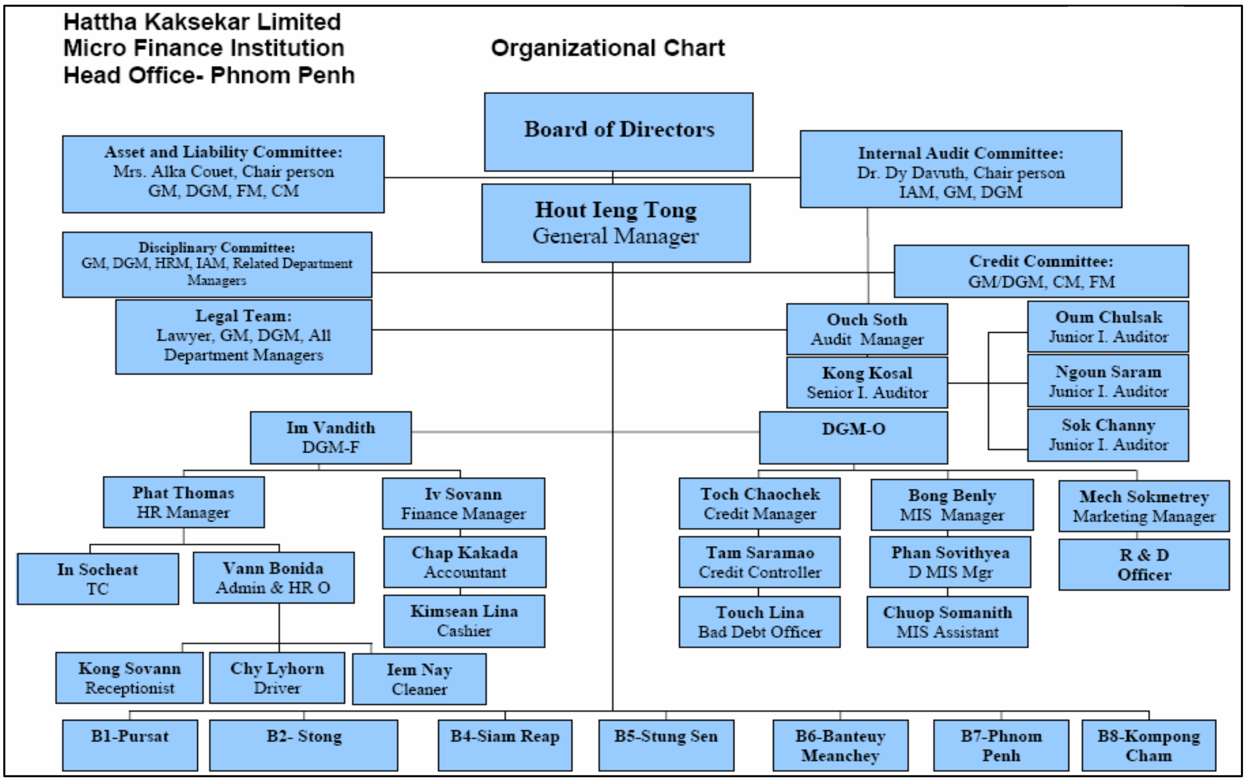
Indeed, in 2007, a significant inflow of share capital is expected, with **new international shareholders joining**, potentially interested in becoming **influent shareholders**. This **would change the overall equity structure**, with a drop in the relevance of the HK NGO (see Chapter 5). With respect to this, an **agreement has not been reached** yet within the current BoD, as the management members want the NGO to inject more capital in order to maintain its position in the new capital structure, while the current international shareholders oppose this increase, leaving space for uncertainty.

[3] More than 20%.

According to the drafted Business Plan (to be approved by the Board in March 2007), this capital increase should cover projected growth until 2009. In this view of expanding its capital base, HKL has started distributing dividends on its profits.

HKL is governed by a **Board of Director** composed of 6 members[4], both **internationals and locals**, ensuring a good rooting in the Cambodian context, and the composition includes expertise in the **financial, business and microfinance** sectors. The General Manager sits as representative of HK NGO and the Deputy General Manager as representative of the Staff Association, resulting in a strong presence and potentially an overweight of the **management members** within the Board, one of those representing the only influent shareholder (see above, more than 20%). A **better balance is expected to be acquired** with the entrance of the representatives of new shareholders. At the same time, the DGM has already decided to resign and will be soon replaced by another representative from the Staff Association. On the other hand, **minority shareholders are represented** in the Board and, at the moment, one independent member also sits in the Board.
BoD meetings are held physically **twice a year**, but **ordinary functioning and decision making** is guaranteed and strengthened by **virtual meetings** and more frequent meetings of committees including BoD members: ALCO, Audit Committee (see below), Credit Committee and Compensation Committee. Participation of BoD members with specific skills in these committees is also ensuring **capacity building** for HKL's personnel (in particular in Audit and AL committees). On the other hand communication flows are regular between management and non management members of the Board, also including supervision activities. The BoD composition is expected to be strengthened by the stepping in of new shareholders.

Organization and structure
HKL's **organizational structure** has been going consolidating over the years and appears now relatively mature. Up to date HKL operates through a network of 7 branches and 21 sub-branches in the province of Pursat, Stong, Siam Reap, Stung Sen, Banteuy Meanchey, Phnom Penh and Kompong Cham. In the last years, HKL has successfully worked for **streamlining its operations**



and reducing the geographical dispersion of its operations, with good results on its

[4] One local independent member resigned and was not substituted, in view of the change in structure.

performances. In particular, HKL managed to strengthen its penetration of the territory, exploiting the existing positioning but with little further expansion.

The **Head Office** is composed of a general direction, two sub-directions, finance and operations, and 6 departments (including Audit). At the time of the visit, the function of Deputy GM for Operations was covered by the Credit Manager, while the Deputy GM for Finance has an important role in supporting and assisting the GM. Some of the departments or their heads are still relatively new or inexperienced, still needing capacity building for ensuring autonomous functioning and **adequately supporting the institutional evolution** (e.g.: Audit, Marketing and HR). HKL's management and directors are aware and are working on that, also through the capacity building conducted by the institutional committees.
The head of Departments convene on a weekly basis for discussing operational and policy issues, while, following a **bottom-up approach,** planning activities also involve branch managers (and indirectly other staff).

HKL has adopted a **decentralized structure**. Especially in the past, this has not always corresponded to adequate levels of centralized control, originating episodes of fraud and not very conducive internal control environment. The institution has overtime been making efforts in this sense (see below). Branches prepare their own financial statements, budget and analysis of performances to be reported to the HQ.
In order to streamline operations and improve efficiency, branches are treated as separated cost centres and, in this perspective, also expansion through sub-branches and their functioning is more closely monitored.

Human Resources

Personnel	Dec 2004	Dec 2005	Dec 2006
Total	113	139	169
Loan officers	35	43	58
Other staff	78	96	111

As of December 2006, HKL staff included **169 employees[5], out of which 58 are loan officers**, for a quite low staff allocation ratio equal to 34.3% (Chapter 6).
HKL relies on experienced and skilled top management and young and dynamic personnel. Nevertheless, as already mentioned, the capacities of young management at the HO and of branch managers, also related to the decentralization of operations, need to be strengthened.
The HR department includes three different Units: Administrative, Training and HR. The **training** Officer is responsible for organizing in-house and external trainings based on evaluation of training needs collected every year during the staff appraisal. So far, training has been financed by donors but starting from 2007 HKL will allocate a dedicate budget (around USD 30,000).
It is worth noting that the initial training for loan officers and field staff currently seems to be too short and more focussed on marketing and promotion than financial analysis.
The HR unit mainly deals with recruitment, compensation and staff performance appraisal. Even without a formal carrier path, internal promotion and, more recently, staff rotation put seem to represent a good incentive for staff retention. On the other hand, the **perception exists that salaries are not fully in line with the microfinance market**, especially for loan officers, and this seems to be one of the main reasons for turnover of credit staff. For better measure this potential weakness, HKL, with the contribution of AFD, contracted a local company to perform a study on the remuneration level at financial institutions in Cambodia. A number of other benefits are available for HKL's staff.
On the other hand, the **incentive scheme for loan officers** seems to be **hardly effective**, especially due to its strict features (zero tolerance on delinquency) not frequent (quarterly) payments. A new bonus system is being currently designed the HR department.
Staff turnover has been high in the past and is still **relatively relevant**, especially among LOs (8.9% in 2006, with 9 LOs, 14.8% in 2005, with 13 LOs).

[5] 13 support staff.

Internal control and operational risk management

Having experienced problems related to fraud and misappropriations of funds, HKL spent many efforts in improving its Internal Control Environment, introducing also a **dedicated committee within the BoD**, which supports and monitors the work of the **Audit Department**. The **GM and DGM sit in the audit committee**, what is not advisable, as it constitutes a **limit to the independence of the audit function**.

Currently, the Audit Department is composed of 4 people and is planning to hire one more person. The **audit manager is new in this function** (since November 2006) and may still need support in order to strengthen his capacities. The **Annual Audit Plan** is approved by the BoD and the General Manager and in 2006 was almost fully fulfilled. The Internal Audit system includes regular audits, follow-ups and special investigations. **Regular audits are held twice a year in each branch** and mainly focus on portfolio. In 2006 28% of disbursed loans were checked, which represents a fair coverage of the credit transaction, especially important in an institution whose weaknesses in the internal control system resulted in cases of fraud**.**

Follow-ups are made to check the implementation of recommendations, while special investigations are dedicated to specific categories of loans.

The **internal auditor regularly reports to the Audit Committee**. The periodical reports are rather clear and complete.

The overall **internal control environment** has **improved** in the last years, but the institution still experiences weak implementation of the internal control procedures (e.g.: no segregation of booking and validating functions in the branch accounting, as BM should monitor but he is often busy with the operations).

Accounting and external audit

PriceWaterCooperHouse has been auditing HKL's financial statements for the last three years. The auditors have expressed an unqualified opinion on HKL's financial statements.
FS are prepared in accordance with the Cambodian Accounting Standards and guidelines issued by the Central Bank, widely in accordance with the IAS and IFRS. The Company maintains its accounting records in US$, which is its functional currency, as permitted by the law.

Management information system

The transition phase to its new loan tracking system **Microbanker Windows Version** (MBWin) ended in June 2006, with the MIS being installed and operating in all the branches. Undoubtedly this phase required a long process of improvement and adaptation to the institutional needs (especially in terms of internal and external reporting). So far, only two branches are entirely operating using MBWin, whereas the rest of the branches still **manage old clients manually.**

MBWin presents the **loan tracking system integrated with the accounting software** for all the branches. Moreover, HKL internally developed a software, **Support Loan Applications (SLA)**, for reporting purposes (also to made reports available in Khmer language), to better customize the system to the institutional needs. To date, HKL presents potential to produce **appropriate information** and relies on a **complete MIS manual and Users Manual**.
Nevertheless, the full appropriation of the new system is not completed, as there is still an overall **limited knowledge of the MIS in branches** and it seems that the monthly IT department's visits to the branches are not enough to solve all the problems and emerging difficulties. This results in **mistakes** and **reverse transactions** (that should be approved by the HO) and sometimes in temporary return to the Excel system at the branch level.

The system is not on-line and each branch works on a **different database**, while they are working on one single database to be implemented by mid-2007. Portfolio data are now manually consolidated on a monthly basis, while **a set of automatic reports is produced at branch level** (breakdowns by products, sectors, amounts, etc).

One of the main weaknesses of the MIS is related to the **consolidation of financial information of the branches.** This is due to the existence of different chart of accounts in some branches and implies the **manual consolidation** of accounting data. However, the institution is working on this and by mid-2007 should have fully automated systems.

The current situation, where the transition phase has not been fully accomplished yet, leaves space for higher efficiency levels and improved reliability of data.

At the moment, **security** in terms of backups is satisfactory. Back-ups are made daily in the branches and then a weekly backup is sent to the HQ. Moreover, at the HQ backups are made in two copies (one copy kept inside the building and one outside). Passwords to access to computer system have to be changed every 40 days and every 90 days for MBWin, while for supervisors they need to be changed manually. An informal contingency plan exists.

3. Lending operations

Financial products and policies

HKL offers credit and savings products to micro and small entrepreneurs, **essentially through individual lending methodology**[6]. The products are offered in US$, Thai Bath and Khmer Riel, to better meet clients' needs in the branches of Banteuy Meanchey and Stong.

The credit products are mainly defined according to the amount offered, up to a maximum amount of US$ 3,000 and a maximum maturity of 24 months. Special loans amounting more than US$ 3,000 are also offered to good repeated clients (informally established to be kept below 10% of total portfolio).

Credit products

	Micro-loan	Small loan	Medium loan	Special loan
Credit methodologies	Individual loan and Group loan	Individual loan	Individual loan	Individual loan
Currency of the	KHR,THB, USD	USD	USD	USD
Type of interest	Declining balance	Declining balance	Declining balance	Declining balance
Average interest rate (%)	3.5%	2.5%	2.0%	2.0%
Commissions	0	0	0	0
Min. credit amount (US$)	50	1,000	2,500	3,000
Max credit amount for the first loan (US$)	na	na	na	na
Average credit amount (US$)	274	1,127	1,908	3,640
Min. loan maturity (months)	3	3	3	3
Max. loan maturity (months)	10	18	24	24
Average loan maturity (months)	7	11	14	14
Periodicity of interests payments	monthly	monthly	monthly	monthly
Periodicity of principal payments	monthly, balloon	flexible according to cash-flow	flexible according to cash-flow	flexible according to cash-flow
Collaterals / guarantees	land titles / building	land titles / building	land titles / building	land titles / building

Overall conditions appear to be quite flexible and able to adapt to the characteristics and needs of the clients, such as the introduction of ad hoc repayment schedule, tailored on the effective client's cash flow and repayment capacity.

Better conditions are offered to repeated clients in terms of amount disbursed and interest rate charged.

[6] HKL has started launching some group loans, but they remain marginal in its portfolio.

HKL products **diversification is limited**, but the flexibility shown by the existing products and conditions appear to counterbalance this potential constraint, also judging from the clients surveys conducted internally. To monitor market trends and customer satisfaction HKL Marketing Department carries out periodic customer surveys, interviewing existing and potential customers, with a focus on products tailoring.
In addition, HKL **is planning to introduce an insurance service by the end of 2007**. Besides, in 2007 interest rates in Bath and KHR will be lowered, in response to the complaints from clients.

Lending procedures
HKL's **disbursement process** can issue a loan in 3-5 days, in line with main competitors. Loan application and disbursement procedures are simple and do not require much paperwork and overall customer service seems to be satisfactory.
The evaluation of the client's ability to repay is assessed through the **analysis** of a **Business Plan, financial statements and cash flow** for one average month. **Family income** is also taken into consideration. Nonetheless, time for disbursement may be longer when the **branch managers re-assess the evaluation**. Branch managers usually check 60-70% of client analysis of new loan officers, 15% of clients for experienced loan officers and all special loans. This is a prudential procedure that, while slowing down the process, mitigates the **risk of abuse** involved in HKL's products flexibility, which requires strong training, adequate MIS and appropriate internal control environment. Currently, not all the branches of the institution present these characteristics, so that the **approval process has been delegated according to the different capacities of the branches** in order to also mitigate this risk, while sub-branches do not approve loans. The Branch Credit Committee, composed of the branch manager, the Chief of Credit Unit and the accountant, can approve loans up to US$ 3,000 (but differentiated according to the capacity of the branch). No physical meeting is required for the Credit Committee but the client file is individually assessed and approved by each person participating in the Committee and finally approved at majority. A common discussion with the participation of the loan officer lacks. Only loans bigger than US$ 3,000 are systematically approved by the HQ Credit Committee.

Disbursements and repayments are made in cash at branch and sub-branch offices. Each day the loan officer in the sub-branch travels to the branch to deliver the cash exceeding the daily cash limit of US$ 50. Some risks arise from **cash handling and transportation,** though the fact of operating through sub-branches guarantee a proximity service for clients living in scattered and remote areas.

During the all life of the loan, the credit officer, chief of credit unit and sporadically also the branch manager **monitor the client.**

In terms of **repayment policies**, HKL shows flexibility, offering balloon repayments for agricultural loans, monthly, semi-balloon and ad hoc repayment schedules for business loans. Moreover, clients are permitted to repay in advance without any penalties.
On the other side, penalties charged in case of late repayment are quite high. This certainly represents a strong incentive for clients to repay. Generally, procedures to recover delinquent loans are quite effective and usually assure repayments before reaching the lengthy judiciary process.

Collaterals and accessibility
In regards to collateral requirement, HKL, as well as its main competitors, requires land titles and building certificates. For this, it is worth to note that in Cambodia, the **use of land titles as collateral is still ineffective due to the scarcity of land title issued by the government** (only half of the land has an ownership record) and the high cost of registration. As a consequence, MFIs usually rely on the copy of the land certificate, which however can be used by clients for backing parallel loans from different institutions.

Savings and other banking services

Beside compulsory savings, HKL offers also two different savings products, sight and term deposits. Savers have the possibility to save in different currencies, the US$, the Thai BATH and the Khmer REAL. HKL savings products appear to be quite appealing in terms of interest rate offered. Nevertheless, **HKL capacity to mobilize savings is still limited.** Difficulties to attract deposits for MFIs are linked to a general lack of trust from the public and specific constraints of this institutional form (in terms of public image).

Savings products			
	Compulsory	Voluntary	Term Deposit
Currency	KHR, USD, THB	KHR, USD, THB	KHR, USD, THB
Min. interest rate (%)	NIL	0.5%	4.0%
Max. interest rate (%)	NIL	5.0%	11.0%
Min. accepted balance	Depend on loan size	10	50
Average balance	15	37	2,794
Term	Depend on loan term	Unlimited	3-12 month
Periodicity of interest repayments	NA	Monthly basis	Maturity basis
Penalty in case of anticipated withdrawal	NIL	NA	interest rate of voluntary is applied

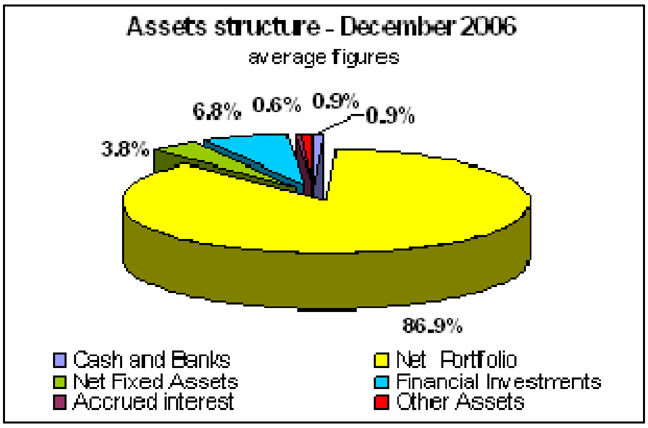
As of December 2006, the **average balance of savings is worth US$ 18**, with the bulk of savers economizing very small amounts and only very few clients saving quite high amounts in the form of term deposit (average balance US$ 2,794).

Compulsory savings represent 81% of total savings. Nevertheless, as they are one of the main reasons for complaints by clients, HKL started to be more flexible in this respect and is planning to eliminate it. On the other hand, not many efforts will be spent to promote voluntary savings and term deposits in the short-medium run.

4. Assets structure and quality

Assets structure

For the period December 2005 - December 2006 HKL average net portfolio represents 87% of the total assets, which is considered a **good level of concentration of resources in the core business, with no significant seasonal patterns.**



Average liquidity (cash and banks) has been maintained at a minimum level of 1%, however when considering the share of financial investments held by the institution, liquid assets reaches almost 8%. The largest share of investments is represented by savings accounts earning from 0.5 to 1.5%. The remaining part is given by a capital guarantee deposit held in the central bank, in accordance with NBC Prakas no. B700-006 requirement for microfinance institutions[7].

Net fixed assets remained stable on average at about 4%.

Portfolio structure

As of December 2006 HKL has an **outstanding portfolio worth almost US$ 6ml**, which **grew by 62%** in the last year, confirming its capacity to maintain a sustained growth for the last 3 years (72% in 2004, 55% in 2005).

For the last period the strongest growth was registered for micro-loans thanks to the decision of the Board to keep its focus on micro-lending, reversing the trend of 2005 that saw medium and special loans growing at a very fast rate. Nevertheless, as shown by the **constant increase in the average disbursed loan** (US$ 375 in 2003 and **US$ 629 in 2006**) HKL is defining its market niche towards the upper segment of the microfinance clientele, both following its own repeated clients and attracting new ones (**number of borrowers** grew by 35.6% in the last year). This is also confirmed by the increasing size of the average disbursed loan on the GDP per capita (136% as of December 2006) and by the fact that the institution overachieved its growth targets, though remaining slightly below in terms of number of clients.

Portfolio features	2003	2004	2005	2006
Gross outstanding portfolio (US$)	**1,377,150**	**2,372,294**	**3,671,126**	**5,950,760**
Micro-loan	933,827	1,151,351	1,534,689	2,544,774
Small loan	278,228	634,458	1,031,241	1,655,232
Medium loan	165,096	443,839	750,043	990,048
Special loan	0	142,646	741,971	760,706
Growth of active gross portfolio	1.0%	72.3%	54.8%	62.1%
Average disbursed loan amount (US$)	375	470	557	629
Av. disbursed loan size on per capita GDP	113%	126%	131%	135%
Number of active borrowers	5,372	6,620	8,475	11,490
Number of active loans to women	51.0%	54.7%	57.0%	65.0%
Drop-our ratio *	70.0%	53.3%	43.6%	43.3%

* According to HKL's definition

It is worth mentioning that, after revising its budget upwards, HKL suffered during 2006 a shortage of funds due to the late reception of funds from the Global Microfinance Facility. This situation was handled through a liquidity facility (Chapter 5).

[7] According to the Central Bank's Prakas no. B700-006 on "Licensing of Microfinance Institutions", each licensed MFI shall maintain an amount equal to 5% of its registered capital in a non-interest earning permanent account with the Central Bank.

81% of the HKL borrowers receive microloans (from US$ 50 to US$ 1,000), representing 43% of the total outstanding portfolio.
On the other hand, even if HKL informally decided to keep the share of special loans (over US$ 3,000) below 10%, as of December 2006 they represent almost 13% and just 1.8% of number of loans.

Decemeber 2006

Loan product	% of outst. portfolio	% number of credits	PAR >30 days	PAR > 30 weighted	PAR >1 day	PAR > 1 weighted
Micro-loan	42.8%	80.9%	0.48%	0.21%	0.54%	0.23%
Small loan	27.8%	12.8%	0.96%	0.27%	1.09%	0.30%
Medium loan	16.6%	4.5%	0.3%	0.06%	0.4%	0.07%
Special loan	12.8%	1.8%	0.4%	0.05%	0.4%	0.05%
TOTAL	100.0%	100.0%		0.58%		0.65%

HKL is in the process of **changing the internal definition of drop-out, in order to make its monitoring more consistent**. The institution also periodically conducts customer satisfactory surveys. Marketing campaigns are also carried out aimed at building a stronger institutional image, optimizing customer service and promote products.
Nevertheless, according to our formula and based on HKL's data on new clients, **drop-out ratio** seems to be extremely high (though decreasing). This may be distorted by a misbehaviour of loan officers, registering existing clients as new (especially when passing from the old to the new system) and is biased by the definition itself of drop-out of the institution (all existing clients not renewing loans within one month are considered drop-out). Retention rate needs to be carefully redefined and monitored in a more consistent way.

HKL's portfolio is well distributed among branches. Instead, more than 90% of the total PAR of the institution is concentrated in the branch of **Banteuy Meanchey**, on the border with Thailand, located in an economically dynamic area, but exposed to riskier activities and clients.

Decemeber 2006

Branch	outstanding portfolio (US$)	% of outst. portfolio	% number of credits	PAR > 30 days	PAR > 30 weighted
Pursat	863,926	14.5%	18.7%	0.29%	0.04%
Stong	929,113	15.6%	23.4%	0.09%	0.01%
Siam Reap	1,481,028	24.9%	16.2%	0.01%	0.00%
Stung Sen	661,238	11.1%	16.2%	0.37%	0.04%
Banteuy Meanchey	1,097,704	18.4%	14.0%	2.55%	0.47%
Phnom Penh	735,375	12.4%	8.5%	0.11%	0.01%
Kompong Cham	167,292	2.8%	2.9%	0.0%	0.0%
Head Office	15,083	0.3%	0.1%	0.0%	0.0%
TOTAL	5,950,760	100%	100%		0.58%

Almost half of the outstanding portfolio is invested **in trading activities (49.5%),** whereas the remaining part of the portfolio is quite diversified, including **productive** (agriculture, 13%; transportation, 9.6%, etc.) and non **productive purposes** (consumer loans, 10%).
No information about distribution of delinquency by sector is available on the MIS, which is not yet fully customized.

Decemeber 2006

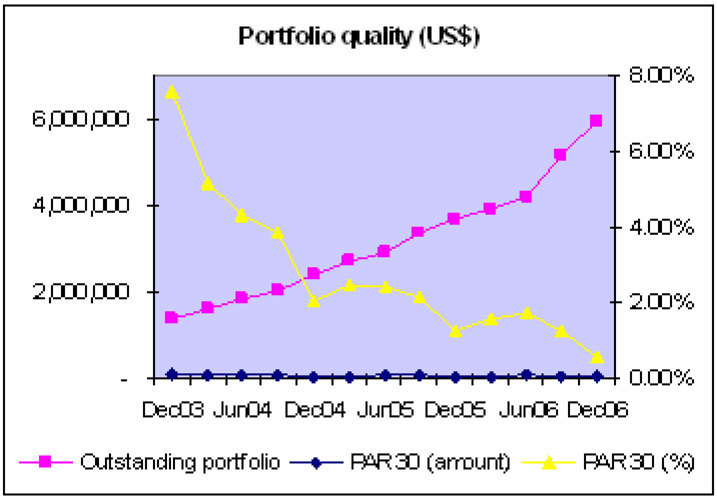
By sector	outstanding portfolio (US$)	% of outst. portfolio	% number of borrowers
Agriculture	768,105	12.9%	26.3%
Trade and Commerce	2,945,549	49.5%	39.5%
Services	390,869	6.6%	5.0%
Transportation	569,287	9.6%	7.6%
Construction	353,230	5.9%	3.0%
Consumer loans	595,260	10.0%	12.3%
Other	328,460	5.5%	6.3%
TOTAL	5,950,760	100%	100%

Loan portfolio quality

Portfolio Quality Indicators	2003	2004	2005	2006
Consolidated PAR30	**9.47%**	**2.07%**	**1.26%**	**0.58%**
31-60	1.23%	0.49%	0.52%	0.11%
61-90	0.16%	0.08%	0.07%	0.02%
91-180	6.62%	1.05%	0.38%	0.17%
181-365	0.37%	0.07%	0.21%	0.13%
>365	1.09%	0.37%	0.08%	0.15%
Arrears rate (> 1 day)	8.4%	1.7%	0.8%	0.5%
Restructured portfolio	0.0%	0.0%	0.0%	0.0%
Provision expense ratio	3.5%	0.0%	0.7%	0.6%
Loan loss reserve ratio	12.8%	5.7%	2.5%	1.5%
Risk coverage ratio (30 days)	135.2%	274.6%	201.9%	261.5%
Write off ratio	3.56%	2.27%	1.1%	0.64%

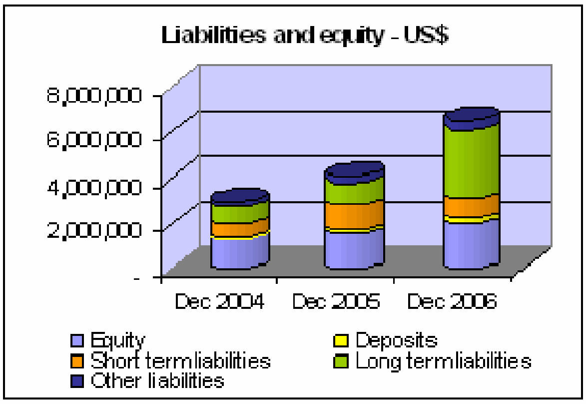
As of December 2006, HKL shows a **satisfactory portfolio quality**, which steadily improved over the years. PAR30 was 9.5% in 2003 continuously decreased, reaching 0.58% as of December 2006. This improvement may be in part due to constant portfolio growth. As it is visible in the graph, portfolio quality follows seasonal patterns, corresponding to recovery efforts and write-offs at the end of each year.

Parallel to this improvement, **write-off ratio** also steadily decreased, having partially absorbed the previous delinquent loans. By the way, according to a strict policy, HKL only writes off after the delinquent loan has reached its maturity.



HKL's delinquency structure does not present significant concentration in older aging brackets.
This level of portfolio quality is the result of a strict policy of the institution, which include the fact that loan officers gain their bonus only with a zero PAR 30.
With a **262% risk coverage ratio**, the institution confirms its prudential approach.

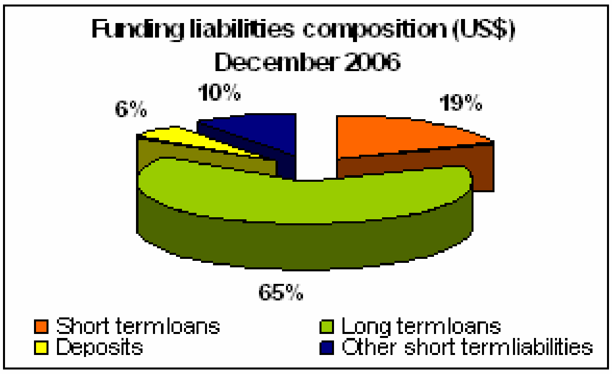
5. Financial structure and ALM



In the past three years HKL has continuously raised its **access to external funding**, keeping strong growth rates constantly over 60% (it grew by 81.5% in 2006). Over the years, HKL has increasingly leveraged its equity, reaching a **2.36 debt / equity as of December 2006** but still leaving room for further increase. The bulk of its liabilities is represented by medium-long term loans, almost all in US$. On the other hand, the institution is continuously **increasing its equity base**, through the capitalization of profits. In the last **two years the institutional capital has steadily grown**, maintaining an appropriate **capital adequacy ratio (28.9% as of December 2006).** Currently HKL is negotiating with **two more equity investors**, for a further issue of shares to feed its equity of fresh financing.

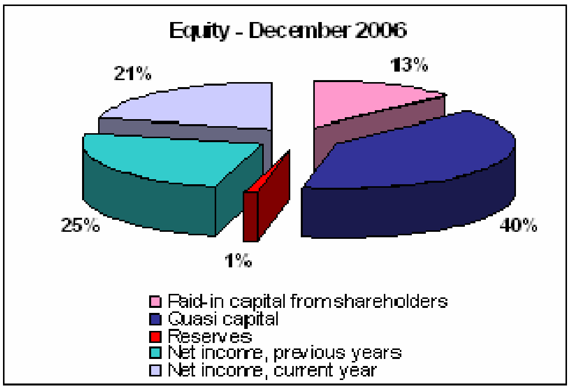
Liabilities and equity structure

As of December 2006, **total liabilities are worth US$ 4.6 million**. Out of this, around **65%** are due in the **medium-long term**. HKL has a **good diversification** of funding resources, including borrowings from the **Asian Development Bank / Rural Development Bank, Symbiotics,** the **Global Microfinance Facility** and other international investors (see Annex 5). On the other hand, **access to local resources is still very limited** for microfinance institutions. In particular, local banks tend to require strong real estate collateral, which MFIs in general can hardly provide.



HKL capacity to mobilize savings is still limited and deposits has maintained a stable level of **5-6%** of total funding liabilities over the last three years, being composed mainly by compulsory savings and, secondarily, term deposits. This is partly due to a combination of lack of public trust and the preference of public for banks rather than MFIs and legal constraints (e.g.: MFIs are not allowed to make money transfers). However, HKL strategy from 2007 will focus more on the attraction of voluntary savings.

On the other hand, also based on the customer surveys, the institution, now already quite flexible in collecting compulsory savings, is planning to eliminate this product and to push through adequate marketing supports, voluntary savings.



HKL **equity**[8] **has been steadily growing in the last two years** (20% in 2005 and 28% in 2006) mainly based on **retained earnings**, accounting for 46% of the total equity, as of December 2006.
Paid-in capital from shareholders amounts at more than US$ 250,000 (13% of the equity), half of it being held by the HK NGO and the rest almost equally divided between SIDI and CORDAID and a residual 10% held by the staff association.

[8] HKL equity is registered in KHR and not using the functional currency which is Dollars.

40% of HKL equity has been contributed in the form of **quasi-capital** by HK NGO[9].

Based on the financial results the institution, **dividends** will be distributed to shareholders for the first time in 2007. Though not yet approved by the BoD, dividends to be distributed should represent 10% of net income.

HKL capitalization policy, currently mostly based on retained earnings, in 2007 would be characterized by new equity investors stepping in. Overall, the participation of new shareholders would change the equity structure and the **relative weight of existing shareholders**. On the other side, within the governing body there are still uncertainties and discussions over the future preferable equity structure (chapter 2).
The opportunity of transforming into a bank is also considered for long-term (after 2011)

<u>Assets and Liabilities Management</u>
HKL's assets and liabilities management is not very sophisticated, even if it seems **adequate to the legal requirements of the NBC and internal needs of the institution**. HKL also relies on an **Assets and Liabilities Committee** (ALCO) composed of the General Manager, the Deputy General Manager, the Operational Manager, the Finance Manager and a member of the Board. The ALCO Committee meets on a quarterly basis, but more frequently if needed. Since 2003, a technical consultant from SIDI is supporting the institution also on financial management.

HKL **does not present any significant maturity mismatch risk.** Current ratio amounts to 2.07 as of December 2006, increasing over the last year from 1.25. As shown in the table above, the institution does not present any negative cumulative net position, thanks to the combination of a mostly short-term portfolio and liabilities over one year.

	< 30 days	31 to 90 days	91 to 180 days	181 to 365 days	1 to 5 years	Other
Assets	**882,795**	**1,289,350**	**1,608,370**	**1,501,313**	**1,269,988**	**14,247**
Cash and banks	296,807	178	0	0	0	14,247
Investments	0	0	0	0	0	0
Outstading portfolio	585,988	1,289,173	1,523,568	1,464,969	996,179	0
Net fixed assets	0	0	0	0	273,809	0
Other assets			84,803	36,344		
Liabilities	**-**	**597,325**	**773,841**	**776,594**	**2,462,220**	**-**
Deposits	0	77,152	128,587	51,435	0	0
Loans	0	472,198	508,251	588,157	2,325,218	0
Other liabilities	0	47,975	137,002	137,002	137,002	0
Net position	**882,795**	**692,025**	**834,530**	**724,719**	**-1,192,232**	**14,247**

Liquidity management is relatively efficient, despite suffering from not full automatization. This is decentralized at a branch level, where cash-flow projections are weekly prepared, while the HO Financial Department monthly consolidates the cash flows for the whole structure to also determine transfers among branches. This may be enough for an institution not just marginally collecting savings. These projections may be affected by the fact that HKL experiences some level of pre-payments in its lending portfolio.
In 2006, due to the **late disbursement of a borrowing** HKL was to receive from the Global Microfinance Facility, the institution had a shortage of liquidity, which was solved by using an **overdraft facility** made available by the Rural Development Bank. Through this facility, HKL has access to a maximum amount of US$ 200,000[10].

[9] This represents a subordinated debt not repayable as long as the HKL sticks to its original mission and activities. On this amount, HKL is paying an annual 1%.
[10] For maximum 3 months, at an interest rate of 9% p.a. (and an administration fee of 1%).

Over the years, **liquidity has been maintained at rather low levels**. Cash and banks, on average during the whole 2006 accounted for 0.93%. However, if taking into consideration also the share of short-term investments, average liquid assets raise to 6.5%.

HKL is **assets sensitive** for all time brackets up to 1 year. Subsequently, its exposure to **interest rate risk** is formally mitigated by the fact that HKL's lending portfolio carries fixed interest rates. Nevertheless, maturity patterns of most portfolio and competitive pressures confirm that HKL is exposed to **potential decrease in active interest rates**. On the other hand, 30% of HKL borrowed funds bear variable interest rates linked to Libor.

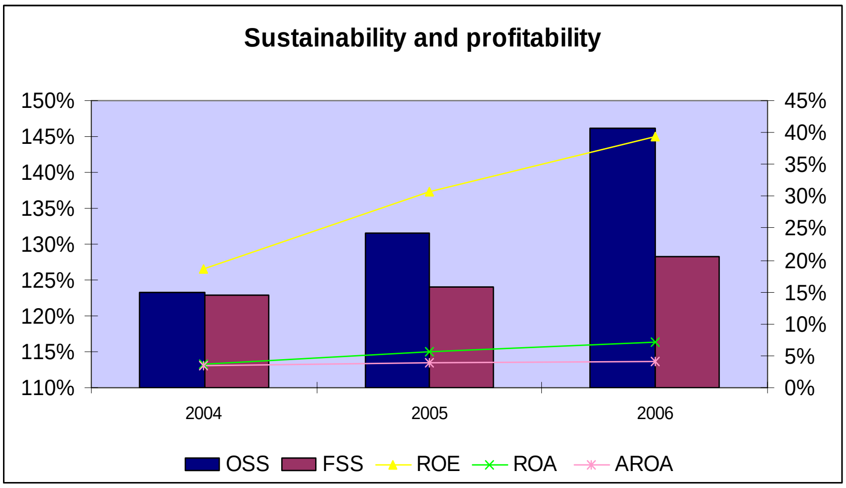
Decemeber 2006

US$	US$*	Other currencies	Local currency
Assets	**5,914,582**	**346,966**	**304,514**
Cash and banks	303,306	1,660	6,265
Financial assets	0	0	0
Portfolio	5,224,961	342,997	291,918
Fixed assets	273,809	0	0
Other assets	112,506	2,309	6,331
Liabilities	**4,082,231**	**457,565**	**70,184**
Loans	237,448	15,562	4,163
Other liabilities	3,388,373	441,911	65,848
Grants	456,410	92	173
NET POSITION	**1,832,351**	**-110,599**	**234,330**

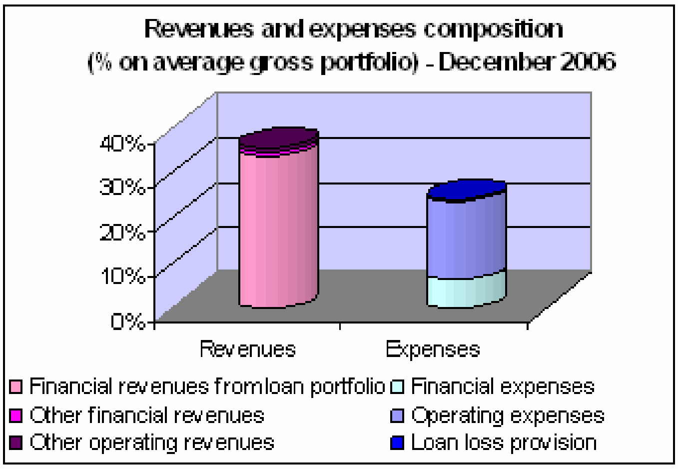
*Exchange rate: KHR / US$: 4,057
**Exchange rate: KHM / BATH 36.40

According to regulation of **the National Bank of Cambodia**, HKL is allowed to hold maximum total open position in foreign currencies of 15% on net worth, and 5% for each currency.
A monthly report on **foreign currency exposure is monthly due to NBC**. As of December 2006, in a downwards trend from previous months, **HKL breaches this requirement** with a short open position on Baht of 5.6%.
HKL's functional currency is US Dollar. As of now, the **share capital of the institution is registered** in Riel (despite the possibility exists to convert it into Dollars), potentially generating capital in Riel shrinking in case US$ devaluates against Riel.
Taking into account the functional currency of the institution, **open position in Riel** should also be monitored, as it carries a potential currency risk as portfolio in Riel is financed in USD by 11.5% of net worth.

6. Financial and operational results



HKL presents **very positive results in terms of profitability and sustainability**, maintaining positive trends.
As of December 2006, **ROE and ROA are respectively 39.4% and 7.2%**, showing a steady 30% increase from 2005, while the trend seems to be **stabilizing down from the rapid evolution of the previous years** (ROE and ROA passed respectively from 18.6% to 30.6% and from 3.7% to 5.6% from 2004 to 2005). This rapid evolution reflects a phase of institutional changes and a significant **scaling-up and intensification of operations** (assets grew by 122% from 2004 to 2006). Over the same period, **OSS**[11] increased from 123% in 2004 to 131.5% in 2005 up to **146% in 2006**.



Adjusted results, mainly impacted by in-kind subsidies[12], reduce compare to non-adjusted performances, with AROE standing at 12.4%, AROA at 4% and FSS at 128.4% for 2006. These adjustments mostly impact the last period of analysis, which still shows an **upwards but slowed-down trend** and mainly due mainly due to important investment done through donations.

A significant role in HKL's better performance in terms of profitability is linked to **efficiency levels** improving overtime. In 2006, HKL shows a satisfactory **operating expense ratio of 17.3%,** down from 26.4% in 2004 and the cost per borrower shows the same decreasing trend. This result stems from a combination of expanding scale of operations while geographically intensifying them, as already mentioned.

Positive effects on the efficiency levels should also come from **increased staff allocation** and **productivity,** in terms of both loan officers and staff. In particular, with a number of new loan officers joining in the last year, caseload by loan officer still shows potential of increase. On the other hand, the portfolio amount managed by loan officer shows a smooth upwards trend, reflecting an increasing average loan.
For what concerns staff allocation, this low level is also due to a **relatively heavy branch structure**, required by a decentralized organizational structure and the strengthening of the internal control system, while the already mentioned intensification of activities in the same area has gradually improved the situation overtime.

[11] Operational and financial self-sufficiency (OSS and FSS) do not include taxes unlike ROA and ROE. This is because we consider the first two ratios as a comparable measure of the sustainability of the MFI without taking into consideration external factors like taxes
[12] Including: technical assistance from SIDI consultant, training of the staff abroad, MIS, technical study on labour market.

Portfolio yield has maintained stable over the last three years at 33.7%, not suffering of the effects of increasing competition. By the way, HKL is already a portfolio yield by 4 points lower than the Cambodian benchmark (MBB data), positioning itself in the low-end of competitors in terms of interest rates applied.
With a significant increased access to external sources of funds, HKL shows a growing **financial expenses ratio**, standing at 5.8% in 2006 (up from 2.2% in 2004). Parallel to this, the institution also knew an increasing commercialization of its funding resources, confirmed by a **cost of funds ratio** augmented from 6% in 2004 to 8.4% in 2006, fairly in line with market rates.

Provision expenses are negligible, reflecting the constant improvements in portfolio quality. HKL applies NBC policy of provisioning for loan impairment.

Financial Indicators	2003	2004	2005	2006
Operating expenses ratio (aver. gross portf.)	31.3%	26.4%	20.7%	17.3%
Staff allocation ratio	29.2%	31.0%	30.9%	34.3%
Loan officer productivity (loans)	173	189	197	198
Loan officer productivity (amount)	44,424	67,780	85,375	102,599
Branch productivity (amount)	229,525	474,459	611,854	850,109
Cost per loan lent	68	57	58	54
Cost per borrower	67	82	82	79
Funding expense ratio	1.0%	2.2%	4.5%	5.8%
Provision expense ratio	3.5%	0.0%	0.7%	0.6%
Portfolio yield (gross portfolio)	31.6%	33.5%	33.5%	33.7%

To maintain profitability levels achieved overtime, HKL should first of all be able to counterbalance the upwards trend in funding costs deriving from increasing access to external funds and the possible downwards push in active interest rates. For doing this, the institution can still improve its performance in terms of productivity and, in part, efficiency of the system, by further **streamlining processes and technology implied, increasing the staff allocation,** etc.

7. Strategic objectives and financial needs

General guidelines for future evolution

The main features of the projected institutional, operational and financial evolution of HKL are disclosed in the draft of the Business Plan 2007-2011.

In 2005 **HKL achieved most of the planned results and performances** set in its strategic document, especially in terms of growth of financial and portfolio indicators.

The **Business Plan is rather complete and detailed** in describing HKL future steps toward the planned evolution and contains a comprehensive analysis of the external sector. The financial projections included in the Business Plan are drafted by the Financial Manager and the Operational Manager, after having gathered all the necessary information from branch managers (responsible for the projections of their own branch). The BoD participates in the planning activity driving HKL to maintain a growth rate in line with the sector (around 40% in 2007), lower than that experienced in the last years. This draft is expected to be approved by the BoD in March 2007.

HKL's main strategic goals for 2007 and for the coming years are the followings:

- → To capitalized its structure thanks to the entry of two new international shareholders in its equity;
- → To maintain a rather stable portfolio growth, expanding to new market in Buttambang, Kampong Chhnang, Takeo and in Kampot;
- → To develop new products tailoring them to clients' needs, especially introducing an insurance component and eliminating the compulsory savings;
- → To maintain portfolio at risk up to maximum 1%;
- → To maintain and streamline efficiency, improving staff productivity;
- → To promote savings mobilization in order to reach the target of 15% of total liabilities in 2011.

The following table synthesizes the main results reported in HKL 's financial projections:

Projected key figures (US$)	Actual 2006	Forecast 2007	Forecast 2008	Forecast 2009	Forecast 2010	Forecast 2011
Outstanding portfolio	5,950,760	8,448,119	11,417,602	15,424,904	20,869,561	28,204,167
Net outstanding portfolio	5,859,876	8,298,542	11,160,706	15,077,844	20,399,996	27,569,573
Number of active borrowers	11,490	18,778	27,726	37,515	48,570	57,710
Portfolio growth	62%	42%	35%	35%	35%	35%
PAR>30	0.58%	1.78%	1.74%	1.7%	1.67%	1.61%
Equity	1,956,082	3,025,774	3,656,467	4,679,660	6,286,780	8,860,759
Equity growth	27.9%	54.7%	20.8%	28.0%	34.3%	40.9%
Debt/Equity	2.4	1.9	2.3	2.5	2.5	2.3
Deposits	257,174	336,186	627,968	1,079,743	1,773,913	2,820,417
Borrowers per LOs	182	159	163	165	163	165

Source: Draft of the Business Plan 2007-2011 (draft version, not approved by the BoD)

Even if the institution initially presented a more aggressive scenario, the Board decided to bring it back to the more conservative hypothesis.

The projections are accurate, comprise different scenarios and take into consideration several variables which could affect HKL performances. A sensitivity analysis is undertaken applying different active interest rates.

Financial needs

The financial needs to sustain the planned growth for 2007 are worth US$ 3 millions, out of which US$ 1.8 ml would come from existing lenders and the rest from new investors. Almost US$ 1ml is expected to come from new shareholders, the rest will come mostly from commercial liabilities,

while the contribution from the mobilization of savings should be limited (around 5%. It is 4% as of December 2006).
With regards to its financing, HKL is already negotiating with various international lenders; some having already a long term relationship with the institution and others new (Global Microfinance Facility (GMF), Microcredit Enterprise (MCE), Alterfin, Norfund and Microfinance Alliance).
On the other side, access to local banks is still very limited for microfinance institutions, as they tend to require strong real estate collateral, which MFIs can hardly provide.

HKL's **investors base is satisfactory,** being composed by a wide spectrum of different actors, mainly lending at commercial rates. At the same time, HKL is not planning to dramatically increase its financial leverage but rather prefers to keep it at around 2.5.

8. Details of the risk factors and final opinion

According to our analysis, the main **risk factors** of HKL are the following:

AREA	Risk factors	Relevance*	Main measures implemented and/or to implement in the short term	Observations
External environment	*Increasingly competitive environment*	Medium-high	HKL is constantly monitoring competition and is working to adjust the conditions (pricing and processing) of its lending products to those offered by competitors	In the last year HKL focussed more on micro-loans.
	Lack of a credit bureau and exchange of clients information	Medium	Banks are currently developing a project in this sense.	This situation worsens the risk of overindebtedness in a competitive environment. A credit bureau is not foreseen for microfinance sector in the short run
	Not full availability of land titles	Medium	HKL is working with a lawyer to make their access to land titles more effective	Land titles are not available all over the areas of operations.
	Uncertainties related to savings mobilization	Medium-low	HKL is flexible in the compulsory savings while it is promoting voluntary savings.	The legal framework within which MFIs are allowed to collect savings still lacks definition. Uncertainties are also linked to lack of trust from the public, public image of MFIs compared to banks and operational constraints
Governance, management and operations	*Management members sit in the Audit Committee*	Medium-high	-	GM and DGM sitting on the Audit Committee constitute a limitation to its independence
	Overweight of management member within the BoD	Medium	DGM is expected to exit the Board, while their weight will be counterbalanced by stepping in of new shareholders	Currently both the GM and the DGM participate in the BoD
	Low frequency of BoD meetings	Low	Virtual meetings and meetings of the committees more frequently happen, in order not to slow down decision-making	-
	Shortcomings in the MIS	Medium	IT department working on MIS development.	Poor knowledge of the system at branch level. Manual consolidation of accounting data.
	Staff capacity building in progress	Medium	-	Some Head of Departments, branch managers and in general branch staff need more training to develop adequate skills for their positions. Given the level of decentralization of the branches, BM would need to improve their managerial skills
	Control environment still to be strengthened	Medium	HKL is continuously working on improving its internal control.	Lack of implementation of some control procedures (e.g. segregation of duties, etc.)
	Uncertainties linked to recent significant changes in policies and procedures	Medium-low	-	Different application of policies and procedures in different branches.
	Poor incentive scheme for LOs	Medium	HKL is working to change it	The current incentive scheme is ineffective (e.g. too strict, not frequent)
	Relatively high staff turn over	Medium-low	-	Especially among loan officers
	Lack of securities in documents storage	Medium	-	HKL keep all clients files in simple cabinet, not fireproof

AREA	Risk factors	Relevance*	Main measures implemented and/or to implement in the short term	Observations
Financial products and assets quality	*Not fully competitive time for disbursment*	Low	-	The practice of re-assessing clients' assessments impact on the time for disbursement.
	Limited development of savings products	Medium-low	In the next coming years HKL will be promoting and developing more voluntary savings products.	The current legal framework is not yet clear for MFIs regarding savings mobilization and this lengthen the whole process.
	Ineffective tracking of client retention	Medium	-	Drop-out results difficult to calculate and monitor adequately, based on available data
	Weak enforcement procedures	Medium	-	Generally enforcement procedures in Cambodia are quite lengthy and bureaucratic.
Financial Structure and ALM	*Exposure to interest rate risk*	Low	-	Due to maturity patterns of portfolio and competitive pressure
	Exposure to currency risk	Medium-low	Regular monitoring	-
Financial and operational results	*Improvable staff allocation and productivity*	Medium-low	HKL has worked on that	That would allowed to counterbalance a relatively heavy back-office structure
Strategic objectives and future evolutions	*Uncertainties linked to BoD decision on shareholders structure*	Medium-high	-	There is still disagreement among the Board members on the composition and relative weight of HKL's local and international shareholders

Annex 1 - Financial statements

HKL			
Balance sheet (US$)	***2004***	***2005***	***2006***
ASSETS			
Cash and bank deposits	114,421	34,955	46,940
Short term financial assets	399,021	291,996	250,044
Net outstanding portfolio	2,237,619	3,577,783	5,859,876
Gross outstanding portfolio	2,372,294	3,671,126	5,950,760
Performing portfolio	2,323,252	3,624,895	5,916,004
Portfolio at risk > 30 days	49,042	46,231	34,756
(Loan loss reserve)	134,675	93,343	90,884
Accrued interest	15,747	8,846	95,794
Other short term assets	76,181	33,953	23,801
Total short term assets	**2,842,989**	**3,947,533**	**6,276,456**
Long term financial assets	13,747	13,747	14,247
Net fixed assets	86,276	154,635	273,809
Other long term assets	19,209		1,552
Total long term assets	**119,232**	**168,382**	**289,608**
Total assets	**2,962,221**	**4,115,915**	**6,566,064**
LIABILITIES and EQUITY			
LIABILITIES			
Sight deposits	3,364	25,536	15,685
Short time deposits	-	-	33,529
Short term loans	594,180	1,121,208	879,678
Other short term liabilities	228,149	299,843	458,983
Total short term liabilities	**825,693**	**1,446,587**	**1,387,876**
Long term time deposits	94,063	144,787	207,959
Long term loans	766,734	995,525	3,014,147
Other long term liabilities	-	-	-
Total Long term liabilities	**860,797**	**1,140,312**	**3,222,106**
Total liabilities	**1,686,490**	**2,586,899**	**4,609,982**
EQUITY			
Paid-in capital from shareholders	257,850	257,850	257,850
Donated equity	-	-	-
Quasi-capital	777,641	777,641	777,641
Reserves	4,030	9,692	23,241
Total retained earnings	236,210	483,833	897,350
Net income, previous years	123,409	225,164	479,602
Net income, current year	112,801	258,669	417,748
Total equity	**1,275,731**	**1,529,016**	**1,956,082**
Total liabilities and equity	**2,962,221**	**4,115,915**	**6,566,064**

Annex 1

HKL			
Income Statement (US$)	**2004**	**2005**	**2006**
Interest & commissions received on loans	619,791	1,004,533	1,542,687
Financial revenue from investment	436	1,300	3,493
Other financial revenues	638	-	31,013
A) Financial revenue	620,865	1,005,833	1,577,194
Interest paid on borrowings	41,026	133,254	262,984
Interest paid on savings	113	537	779
Other financial expenses	7,344	17,474	26,751
Inflation adjustment	-	-	-
B) Financial expenses	48,483	151,265	290,514
Gross financial margin (A - B)	572,382	854,568	1,286,680
Loan loss provision	413	21,397	27,008
Net financial margin	571,969	833,171	1,259,672
Other operating revenue	42,685	32,303	42,110
Personnel expenses	266,983	325,371	445,894
Administrative expenses	221,979	295,595	344,698
C) Operating expenses	488,962	620,966	790,592
Net operating income	125,692	244,508	511,190
Extraordinary revenue	645	2,349	1,824
Extraordinary expense	-	-	-
Net income before donations, before tax	126,337	246,857	513,014
Taxes	47,334	64,118	143,983
Net income before donations	79,003	182,739	369,031
Donations in cash	34,234	70,545	123,305
Revenue not from the operations	-	-	-
Expenses not from the operations	-	-	74,588
Net income	113,237	253,284	417,748

Annex 2 - Financial statement adjustments

The financial statements in Annex 1 are the result of **standard reclassification of audited financial statements for 2004 and 2005. For 2006, internal financial statements** are used. They are expressed in US Dollars (US$) being the Dollar the functional currency of the institution.

Financial statements have been adjusted by *Microfinanza Rating* to allow a comparison with other institutions which use a different logic of presentation of the information and to evaluate the level of sustainability of the institution with market conditions.
The main adjustments normally are:

- → adjustment for the accrued interest on delinquent loans
- → elimination of subsidies (donations in kind[13] and soft loans[14])
- → provisions are calculated with a standard formula[15]
- → adjustments for inflation
- → adjustments for write-off[16]

The main adjustments applied for the period of analysis are related to in-kind subsidies. The cumulative effect of all this adjustment reduces the net income in the period.

Adjustments (US$)	2004	2005	2006
Reversal of accrued interest on non-perf loans	-	-	-
Subsidized cost of fund adjustment	1,405	63	-
- Interest rate used (national currency)	13.2%	13.0%	12.3%
- Interest rate used (foreign currency)	5.1%	7.0%	8.3%
Inflation adjustment	-	-	3,716
Loan loss provision adjustment	-	-	-
In-kind subsidy adjustment	-	47,624	149,671
Total variation of net income	1,405	47,687	153,387

[13] Donations in kind are valorized and added to operational expenses.
[14] In the income statement it is registered the value of the difference between financial costs of the institutions and financial cost evaluated at the market rate. In particular, in the case of loans in local currency, it is considered 75% of the average lending rate in the national market (IFS Line 60P). In the case of loans denominated in foreign currencies (US$ and Euro), it is considered the average value of LIBOR 1 year plus 3%.
[15] Provisions are calculated according to the following formula:

Portfolio:	1-30 days	10%	Restructured loans	0-30 days	50%
	31-60 days	30%		>31 days	100%
	61-90 days	50%			
	>90 days	100%			

[16] Loans past due more than 180 days are written-off.

Annex 3 - Financial ratios

HKL (US$)	2004	2005	2006
PROFITABILITY			
Return on Equity (ROE)	18.7%	29.8%	39.4%
Adjusted Return on Equity (AROE)	6.4%	9.6%	12.4%
Return on Assets (ROA)	3.8%	5.4%	7.2%
Adjusted Return on Assets (AROA)	3.4%	3.8%	4.0%
Operational self-sufficiency (OSS)	123.4%	130.8%	146.1%
Financial self-sufficiency (FSS)	123.0%	123.4%	128.4%
Profit Margin	18.9%	23.6%	31.6%
LOAN PORTFOLIO QUALITY			
Portfolio at risk (PAR30)	2.07%	1.26%	0.58%
Arrears rate (> 1 day)	1.7%	0.8%	0.5%
Restructured loans	0.0%	0.0%	0.0%
Provision expense ratio	0.0%	0.7%	0.6%
Loan loss reserve ratio	5.7%	2.5%	1.5%
Risk coverage ratio (30 days)	274.6%	201.9%	261.5%
Write-off ratio	2.3%	1.1%	0.6%
EFFICIENCY AND PRODUCTIVITY			
Staff allocation ratio	31.0%	30.9%	34.3%
Loan officer productivity (loans)	189	197	198
Loan officer productivity (amount)	67,780	85,375	102,599
Staff productivity (loans)	59	61	68
Staff productivity (amount)	20,994	26,411	35,212
Branch productivity (amount)	474,459	611,854	850,109
Operating expenses ratio (average gross portf.)	26.4%	20.7%	17.3%
Operating expenses ratio (average assets)	23.3%	18.3%	15.4%
Cost per loan lent	57	58	54
Cost per borrower	82	82	79
Personnel expenses ratio (average gross portf.)	14.4%	10.9%	9.7%
Admin. expenses ratio (average gross portfolio)	12.0%	9.9%	7.5%
ASSETS/LIABILITIES MANAGEMENT			
Portfolio yield (gross portfolio)	33.5%	33.5%	33.7%
Funding expense ratio*	2.2%	4.5%	5.8%
Cost of funds ratio*	6.0%	7.4%	8.4%
Adjusted provision for inflation (av. gross port.)	0.0%	0.0%	0.1%
Current ratio	1.96	1.25	2.07
Liquidity over total assets	3.9%	0.8%	0.7%
Debt/equity ratio	1.32	1.69	2.36
Capital adequacy ratio	43.1%	37.1%	29.8%

* exchange rate variations are not included in the calculation of the ratio

OUTREACH			
Average disbursed loan size	470	557	629
Average disbursed loan size on per-capita GDP	126.19%	130.51%	134.94%
Percentage of active borrowers women	54.7%	57.0%	65.0%

GROWTH (amount in US$)			
Growth of active gross portfolio	72.3%	54.8%	62.1%
Growth of active borrowers	23.2%	28.0%	35.6%
Growth of total assets	90.5%	38.9%	59.5%
Growth of staff	11.3%	23.7%	24.7%
Growth of funding liabilities	797.8%	56.8%	81.5%
Growth of operating expenses*	23.6%	27.0%	18.5%
Growth of equity	9.7%	19.9%	27.9%

Annex 4 - Definitions

	Description of the ratio	Formula
Profitability	**Return on equity (ROE)**	Net income before donations / Average equity
	Adjusted return on equity (AROE)	Adjusted net income before donations / Average equity
	Return on assets (ROA)	Net income before donations / Average assets
	Adjusted return on assets (AROA)	Adjusted net income before donations / Average assets
	Operational self-sufficiency (OSS)	(Financial revenue + Other operating revenue) / (Financial expenses + Loan loss provision expenses + Operating expenses).
	Financial self-sufficiency (FSS)	(Adjusted financial revenue + Other operating revenue) / (Adjusted financial expenses + Adjusted loan loss provision expenses + Adjusted operating expenses)
	Profit margin	Net operating income / operating revenue
Portfolio quality	**Portfolio at Risk (PAR30)**	Portfolio at Risk > 30/ Gross portfolio
	Provision expense ratio	Loan loss provision expenses / Average gross portfolio
	Loan loss reserve ratio	Accumulated reserve / Gross portfolio
	Risk coverage ratio (>30 days)	Accumulated reserve / Portfolio at risk >30 days
	Write-off ratio	Write-off of loans / Average gross portfolio
Efficiency and productivity	**Staff allocation ratio**	Loan officers / Total staff
	Loan officer productivity – Borrowers	Number of active borrowers / Number of loan officer
	Loan officer productivity – Amount	Gross portfolio / Number of loan officer
	Staff productivity – Borrowers	Number of active borrowers/ Number of staff
	Staff productivity – Amount	Gross portfolio / Number of staff
	Operating expenses ratio	Operating expenses / Average gross portfolio
	Cost per borrower	Operating expenses / Number of borrowers
	Administrative expenses ratio	Administrative expenses / Average gross portfolio
	Personnel expenses ratio	Personnel expenses / Average gross portfolio
Financial management	**Portfolio Yield (gross portfolio)**	Interest income from portfolio / Average gross or net portfolio
	Cost of fund ratio	Interest expenses on funding liabilities / Period average funding liabilities
	Funding expense ratio	Interests and fee expenses on funding liabilities / Average gross portfolio
	Current ratio	Short term assets / Short term liabilities
	Debt/Equity ratio	Liabilities / Equity
	Capital adequacy ratio	Total equity / Total assets
Outreach	**Average disbursed loan size**	Amount issued in the period / Number of issued loans
	Average disbursed loan size on per-capita GDP	Average disbursed loan size / Per-capita GDP

Other definitions:

Funding liabilities: Liabilities that finance the loan portfolio and the cash investments necessary to manage the loan portfolio

Operating expenses: Personnel expenses + Administrative expenses

Recovery from write-off ratio: Income from write-off (payments received from loan already written-off) / Average gross portfolio

Restructuring of delinquent loans: includes rescheduling loans (extending the term of the loan or relaxing the schedule of required payments) and refinancing loans (paying off a problem loan by issuing a new loan).

Annex 5 - Guidelines of reporting and accounting

Financial statements

HKL's financial statements are audited by the Cambodian affiliate of PriceWaterhouseCoopers Limited and reflect the IFRS standards.

Loan loss provision and write-off

Classification	% provision
Standard loans	0%
Sub-standard loans	10%
Doubtful loans	30%
Loan losses	100%

HKL is following the standard classification of loans according to NBC's Directive (Prakas) No. B-02-186 dated 13 September 2002 on loan classifications and provisions. Standard and sub-standard loans refer to portfolio overdue of respectively 30 and 60 days; doubtful loans and loan losses also take into consideration the duration of the loan. Short term loans fall in the category of doubtful loans if they are more than 60 days past due, while long term loans are included in the same category if they are more than 180 days past due. Loans are classified as losses, when short term loans are overdue more than 90 days past due and long term loans more than 360 days. Reports on provision are prepared and submitted to the National Bank every month.

HKL writes off loans entirely matured, that have been provisioned 100% and checked by the internal auditor, based on the decision of the Board of Director. Loans that have been written off are tracked separately on a write-off list and remains under the responsibility of the loan officer for its recovering.

HKL does not allow restructuring of loans.

Insider loans

HKL recently introduce the possibility for the staff to receive a loan. Conditions are 1.5% interest rate monthly declining, for a maximum term of 24 months and for a maximum amount of 6 salaries. Overall internal loans should not represent more than 3% of the outstanding portfolio.

Donations

HKL received donations mainly from the AFD (ended in 2006) and GTZ (ended in 2003) and some supplementary support from the Asian Development Bank, MAF and other national and international donors.

Donations received (US$)

Year	Amount	Destination	Source
2005	5,000	Direct grant for operating expenses, (e.g. management and training/TA costs)	Department of Fishery
	21,000	Direct grant for operating expenses, (e.g. management and training/TA costs)	MAF
	20,266	Direct grant for operating expenses, (e.g. management and training/TA costs)	ADB
Sub-total	**46,266**		
2006	4,620	Grant loan capital	SC
Sub-total	**4,620**		
TOTAL	**50,886**		

Details of funding liabilities

The debt position of the institution, as of December 2006, is detailed in the following tables.

Source	Currency (in which the loan is due)	Outstanding Balance (US$)	Outstanding Balance Short term (US$)	Outstanding Balance Long term (US$)	Agreement, kind of product and collateral
RDB-ADB	US$	500,000	250,000	250,000	Uncollateralized credit agreement, at libor + 4%
Alterfin	US$	650,000	0	650,000	Credit baked by fixed assets, at libor + 4.5%
Cordaid	US$	328,373	137,526	190,847	Uncollateralized credit agreement, at 6% i.r.
MAF	KHR + THB	127,152	127,152	0	Uncollateralized credit agreement, at 10% i.r.
SIDI	US$	280,000	240,000	40,000	Uncollateralized credit agreement, at 8% i.r.
OIKOS	US$	130,000	0	130,000	Uncollateralized credit agreement, at 6% i.r.
GMF	US$	750,000	0	750,000	Uncollateralized credit agreement, at 9.5% i.r.
Symbioties	US$	750,000	125,000	625,000	Uncollateralized credit agreement, at 9.8% i.r.
NOVIB	THB	378,300	0	378,300	Uncollateralized credit agreement, at 10.5% i.r.
TOTAL		**3,893,825**	**879,678**	**3,014,147**	

Source	Loan amount (US$)	Disbursement date	Maturity date	Principal repayments	Interest repayments	Interest rate
RDB-ADB	1,000,000	01/01/02	01/01/08	2 times/year	Monthly	LIBOR + 4
Alterfin	650,000	20/12/06	26/12/07	2 times/year	2 times/year	LIBOR + 4.45
Cordaid	500,080	13/11/03	13/11/09	2 times/year	3 times/year	6.00%
MAF	250,000	13/09/04	13/07/07	2 times/year	Quarterly	10.00%
SIDI	300,000	21/12/04	31/12/08	2 times/year	2 times/year	8.00%
OIKOS	130,000	30/03/05	30/03/15	2 times/year	Yearly	6.00%
GMF	750,000	03/05/06	01/05/09	2 times/year	Quarterly	9.50%
Symbioties	750,000	26/11/06	26/05/08	2 times/year	Yearly	9.75%
NOVIB	378,300	28/09/06	31/08/09	2 times/year	Yearly	10.50%

Annex 6 - Rating Scale

Rating grade	Definition
AAA	Extremely strong capacity to meet its financial obligations. Excellent operations. Very stable and highly unlikely to be adversely affected by foreseeable events.
AA	Very strong capacity to meet its financial obligations. Very good operations. Stable and unlikely to be adversely affected by foreseeable events.
A	Strong capacity to meet its financial obligations. Very good operations. Stable even if it could be affected by major internal or external events.
BBB	Adequate capacity to meet its financial obligations. Good operations. Quite stable even if it could be affected by significant internal or external events.
BB	Limited vulnerable capacity to meet its financial obligations. Adequate operations. Quite stable even if it could be affected by internal or external events.
B	Partially vulnerable capacity to meet its financial obligations. Sufficient operations. Not completely stable and vulnerable to internal or external events.
CCC	Vulnerable capacity to meet its financial obligations. Basic operations. Potentially unstable and vulnerable to external or internal events.
CC	Highly vulnerable capacity to meet its financial obligations. Poor operations. Potentially unstable and vulnerable to external or internal events.
C	Very high vulnerable capacity to meet its financial obligations. Very poor operations. Unstable and very vulnerable to external or internal events.
D	Not able to meet its financial obligations. Insufficient operations. Very unstable and completely vulnerable to external or internal events.

The rating grade can be corrected with a + or – sign, which implies a slight positive or negative variation respect to the main grade.