Cambodia: Funding for Small and Medium-sized Enterprises (SMEs) I

Ex post evaluation report

OECD sector	240300 - Financial intermediaries in the formal sector	
BMZ project ID	2001 66 249 (2008 random sample)	
Project executing agency	Canadia Bank	
Consultant	GFA Consulting Group	
Year of ex post evaluation report	**2009**	
	Project appraisal (planned)	**Ex post evaluation (actual)**
Start of implementation	Q2 2003	Q3 2003
Period of implementation	24 months	27 months
Investment costs	EUR 2.5 million	EUR 2.5 million
Counterpart contribution	--	--
Financing, of which Financial Cooperation (FC) funds	EUR 2.5 million	EUR 2.5 million
Other institutions/donors involved	--	--
Performance rating	2	
• Relevance	2	
• Effectiveness	2	
• Efficiency	3	
• Overarching developmental impact	2	
• Sustainability	3	

Brief description, overall objective and project objectives with indicators

This project, 'Funding for Small and Medium-sized Enterprises (SMEs) I', supported the establishment of investment financing for SMEs. This was designed to contribute to the development of the financial system and of the SME sector. The executing agency is Canadia Bank, a private business bank, which received refinancing in the amount of EUR 2.5 million as a revolving line of credit.

As a supplementary measure, the bank received additional support of approximately EUR 0.5 million.

The overall objective was to contribute to the consolidation of the financial system and the development of the SME sector. The overall objective would be considered to have been achieved if: (a) the number of long-term loans issued after project completion was equal to, or greater than, the number issued during the project term, and (b) satisfactory returns on equity were evident in the companies which received funding. We believe indicator (a) was poorly defined, whilst (b) lacked a precise target level. The project objective was the lasting provision of long-term investment loans to meet the needs of the SME market.

Achievement of the project objective would be determined by the following indicators: (a) FC loan terms should be longer than three years; (b) the proportion of loans in default for interest and/or capital repayments overdue by more than 90 days should constitute less than 5% of the total loan portfolio; (c) amounts loaned under the project should range from a minimum of USD 10,000 to a maximum of USD 200,000; (d) the bank's return on equity should remain positive in real terms, and should at least match the interest on one-year fixed-term USD deposit accounts in Cambodia.

Project design / major deviations from original planning and their main causes

The FC funds were transferred in USD to Canadia Bank, the executing agency, on a ten-year term (with a three-year grace period) at variable market interest rates, and served as the initial finance for a revolving credit fund. Thereafter funds flowed back to the beneficiary, the Cambodian Ministry of Economy and Finance, which used them, together with the interest on counterpart funds, for the further development of the SME sector. Since the end-user loans are disbursed in USD and the Cambodian economy is extensively dollarised, neither the bank nor the final borrower was exposed to a serious foreign exchange risk.

Canadia Bank presides over a holding company, majority-owned by a Cambodian family. It is a universal bank, offering a broad spectrum of financial products. In recent years the bank has tightened risk management and strengthened its operational structure. Canadia Bank views SME development as one of its core businesses, both now and in the future.

Canadia Bank deployed the funds to provide long-term investment finance for SMEs, with individual loan values from USD 10,000 to USD 200,000. Interest was set close to market rates so that all costs could be covered. SMEs were defined as businesses with between 5 and 300 employees. Furthermore, only companies which had a majority Cambodian management and were predominantly owned by Cambodians would be eligible to receive credit. In addition to the standard negative list, the financing of estate agencies, trading operations and restaurants was excluded. Canadia Bank also provided financing for operational costs in appropriate cases.

Key results of the impact analysis and performance rating

The FC-supported financing offered by Canadia Bank was well received by the SME sector. Canadia Bank issued loans with an average term of 50 months and an average amount borrowed of USD 58,000.

The credit line was set up as a revolving facility with a ten-year term. The volume of credit outstanding is currently running at approx. 1.8 times the FC funds provided. Since the bank states that it has no further long-term refinancing funds available, it is reasonable to assume that the credit line has contributed to the consolidation of the financial system and the development of the SME sector.

In assessing the criteria for developmental success we have arrived at the following conclusions:

Relevance: The Cambodian Government consistently gives SMEs a high developmental priority, but the lack of adequate long-term finance provision constitutes a significant bottleneck, both now and for the future. There is little diversification in the upper levels of the Cambodian finance system. In particular, there are limited opportunities for long-term refinancing of the banking system, even today.

The chain of effects assumed at appraisal — that long-term investment financing would strengthen the finance sector and promote SME growth — seems reasonable; and, in principle, it remains valid today, due to the underdeveloped state of Cambodia's finance and capital markets. The project design also accords with the current priorities of the Cambodian Government, as well as with the BMZ (Federal Ministry for Economic Cooperation and Development) guidelines on the development of financial systems and the promotion of private enterprise. At the time of project appraisal, 'economic reform and building a market economy' was a developmental focal point for the BMZ in Cambodia. These measures were a useful addition to other donors' projects (rating: 2).

Effectiveness: The project objective indicators — an average loan term of 50 months, a high-quality loan portfolio, and individual loan amounts between USD 10,000 and USD 200,000, together with a return on equity by the bank which was positive in real terms — were comfortably achieved. A further positive outcome should be noted: with 168 individual loans to date, and the revolving line of credit already established, results were achieved across a fairly broad spectrum. The partner bank released the credit line swiftly, with no major delays. We assess Canadia Bank's control of the project as good; the above average standard and comprehensive scope of reporting merit particular mention. With few exceptions, the loans were utilised to finance investment. We see it as positive that approx. 40% of borrowers were new customers to Canadia Bank.

During the course of the project it became clear that the SME sector has a requirement not only for long-term investment financing, but also an ongoing demand for working capital finance. This is evident from the relatively high proportion (35%) of loans which were repaid early, i.e. after one year (13%), after two years (9%) or after three years (13%). In many of these cases, credit may have been used to finance both long-term investments and working capital. Clearly, this does not correspond with the original purpose of the project; however, that should not be seen as purely negative from a developmental or SME perspective, since the overall range of financing facilities available to SMEs in Cambodia is not adequate in its scope.

The supplementary measure enacted between January 2004 and June 2006 had great significance for the changes required in Canadia Bank's organisational and operational structure. Since that time, the bank has implemented the additional organisational changes recommended by the consultant in his final report. The overall effectiveness of the supplementary measure is above average, and has been assessed as good (rating: 2).

Efficiency: Overall progress at Canadia Bank since project appraisal is seen as positive. This is particularly true of its institutional and organisational development. Measured on profitability, capital resources and efficiency, the bank ranks among the best in the country. The SME sector has become core business for the bank. The standard of the FC loan portfolio is excellent. However, within the bank's total credit portfolio, the portfolio at risk has deteriorated since project appraisal; at the end of 2008 it stood well above the market average of 5.8%. According to the bank, these differences are attributable, inter alia, to the fact that FC loans were granted (for reasons of reputation) on a more stringent basis. From a developmental standpoint, however, this argument is not acceptable, since the DC (Development Cooperation) funding has no effects beyond the refinanced line of credit.

Loans were granted to borrowers on normal market conditions, and at rates of interest which were positive in real terms. Interest on borrowings was negative in real terms in 2008 only, due to the high rate of inflation (close to 20%). According to Canadia Bank's calculations, the provision of credit to the SME sector has proved profitable. Overall, we judge the project's production efficiency as satisfactory.

In terms of allocative efficiency, it can be assumed that borrowers have made consistently good use of the loans provided. Canadia Bank has conducted its own ex post surveys with those SMEs that received finance, and identified an average return of 23% on the investments supported. This was confirmed in principle by field visits (rating: 3).

Overarching developmental impact: At the time of evaluation, a total of 168 loans had been disbursed with a combined value of approx. USD 9.76 million (EUR 7.39 million). Allowing for the additional FC funds provided under the subsequent project 'Funding for SMEs II' (BMZ no 2003 66 278), this equates to a multiplication factor of 1.8 on the total FC amount of EUR 4.09 million. According to Canadia Bank, in 2008 their commercial credit department issued further SME loans on terms of up to two years in the amount of approx. USD 40 million. Taking all this into account, it is reasonable to assume that the overall objective for the finance sector was achieved.

Overarching developmental effects may also be assumed to have taken place at those SMEs which received financing, since these SMEs demonstrate a satisfactory return on equity. The bank points out that the investments which were financed served to create a total of 1,377 new jobs, and to preserve 3,856 existing positions; our field visits have broadly confirmed the data collected by the partner bank. However, we do not consider that the number of jobs created or preserved is a suitable measure of the project's actual economic impact in the SME area. Since the majority of investments which were financed were made in sectors with growth potential, it is reasonable to assume that the project made a useful contribution to the sectoral diversification needed in the Cambodian economy. Overall, the impact on the Cambodian SME sector can be considered good (rating: 2).

Sustainability: Together with ACLEDA bank, Canadia Bank is one of the largest banks in the country, and was rated by the IFC in 2008 as one of the top three banks in Cambodia. Even allowing for the fall in portfolio quality and the possible need to increase write-downs, the level of capitalisation may well prove adequate. In view of the deterioration in the standard of the portfolio, provisions against possible loan defaults have been very finely calculated.

The bank's liquidity position has deteriorated steadily since 2004. Considering the very limited opportunities in the short term for refinancing on the interbank market, the fall in the bank's portfolio quality and the negative repercussions for the Cambodian banking system expected from the international financial and economic crisis, we view the bank's present liquidity position as a difficulty.

Canadia Bank views SME financing as one of their core businesses, both now and in the future. Since refinancing is, for the most part, highly dependent upon short-term deposits and on long-term refinancing options (which have so far been lacking), the scope for continuing to issue loans in the long term remains severely limited.

Based on the data collected by the executing agency, the results of field visits and the very high standard of the FC loan portfolio, it is safe to assume that, in general, the SME investments have been managed sustainably. This may be constrained by the bank's overall earnings ability, in view of the quality deterioration in the bank's overall loan portfolio. The bank states that it will use the experiences gained from the FC-financed issue of SME loans to raise the overall standard of the portfolio in the longer term (rating: 3).

Having considered all the foregoing risks and effects, we have arrived at an overall evaluation of the project's developmental impact as good (rating 2).

General conclusions and recommendations

The objective indicators for portfolio quality which were selected for the FC portfolio should also be considered for the bank's overall portfolio. This is the only way to ensure an accurate depiction of the desired ongoing structural and institutional effects of FC involvement.

Notes on the methods used to evaluate project success (project rating)

Projects are evaluated on a six-point scale, the criteria being relevance, effectiveness (outcome), "overarching developmental impact" and efficiency. The ratings are also used to arrive at a final assessment of a project's overall developmental efficacy. The scale is as follows:

1 Very good rating that clearly exceeds expectations

2	Good rating fully in line with expectations and without any significant shortcomings
3	Satisfactory rating – project falls short of expectations but the positive results dominate
4	Unsatisfactory rating – significantly below expectations, with negative results dominating despite discernible positive results
5	Clearly inadequate rating – despite some positive partial results the negative results clearly dominate
6	The project has no positive results or the situation has actually deteriorated

A rating of 1 to 3 is a positive assessment and indicates a successful project while a rating of 4 to 6 is a negative assessment and indicates a project which has no sufficiently positive results.

Sustainability is evaluated according to the following four-point scale:

Sustainability level 1 (very good sustainability)

The developmental efficacy of the project (positive to date) is very likely to continue undiminished or even increase.

Sustainability level 2 (good sustainability)

The developmental efficacy of the project (positive to date) is very likely to decline only minimally but remain positive overall. (This is what can normally be expected.)

Sustainability level 3 (satisfactory sustainability)

The developmental efficacy of the project (positive to date) is very likely to decline significantly but remain positive overall. This rating is also assigned if the sustainability of a project is considered inadequate up to the time of the ex post evaluation but is very likely to evolve positively so that the project will ultimately achieve positive developmental efficacy.

Sustainability level 4 (inadequate sustainability)

The developmental efficacy of the project is inadequate up to the time of the ex post evaluation and an improvement is very unlikely. This rating is also assigned if the sustainability that has been positively evaluated to date is very likely to deteriorate severely and no longer meet the level 3 criteria.

The overall rating on the six-point scale is compiled from a weighting of all five individual criteria as appropriate to the project in question. A rating of 1 to 3 indicates a “successful” project while a rating of 4 to 6 indicates an “unsuccessful” project. In using (with a project-specific weighting) the five key factors to form an overall rating, it should be noted that a project can generally only be considered developmentally “successful” if the achievement of the project objective (“effectiveness”), the impact on the overall objective (“overarching developmental impact”) and the sustainability are considered at least “satisfactory” (rating 3).