



SmaKmmRkUhrBa@tkmCa

Cambodia Microfinance Association

Seminar on Cambodia's Microfinance amid the Global Financial Crisis

Topic

Products and Interest Rate

Date: 19th August 2009

Sim Senacheert, CMA's Director of the board

Contents

- What is Microfinance
- Services offered by MFIs:
 - Financial: Loans, savings
 - Non-Financial: Social intermediation, enterprise development, ...
- Loan type and characteristics:
 - Group Loan
 - Individual
- Deposits:
- Interest rate:
 - How to calculate the interest rate
 - Funding, trend of lending interest rate and borrowing rate,
- Challenges:

Introduction

- What is Microfinance?
 - Microfinance is a solution for the people (poor) who have small business, low income, lack of collateral, and lack of experience to access to financial services
 - Therefore, it is an economic development approach intended to benefit low-income people. It involves the provision of financial services to low-income clients
 - Microfinance is not simply banking. It is a development tool. Usually Microfinance are:
 - Perceiving as high risk operations because most of the client's inability to provide marketable collateral for loans
 - Occurring high operational costs due to small transactions
- What is the goal of Microfinance?
 - The sustainable economic development
 - To achieve outreach and viability. By reaching this goal, microfinance will be able to increase access to financial services to its clients over a long term.

Financial Products

- Financial services:
 - Credit
 - Deposits
 - Transfer (within network)
- Non-financial services:
 - Social intermediary
 - Microenterprise development

Microfinance Services

- What is Credit?

Credit is one of the important financial services provided by microfinance institution. Credit is borrowed funds with specified interest rate and term for repayment.

- What are the credit delivery method?

- Group-Based Lending:

- Is of the most popular microfinance lending method, it involves the formation of small groups of people who wish to borrow small loans
- Group-based lending targets majority of the people, who cannot provide the collateral requirements of most commercial banks
- One important feature of group- based lending is the use of peer pressure as a "collateral" substitute

- Individual Lending:

- Loans to individuals based on their ability to provide assurances of repayment, and some level of security (depending on the type of lending mechanisms, collateral may or may not be required)
- Lending based on personal knowledge of borrowers rather than on sophisticated feasibility analysis
- Use of informal collateral

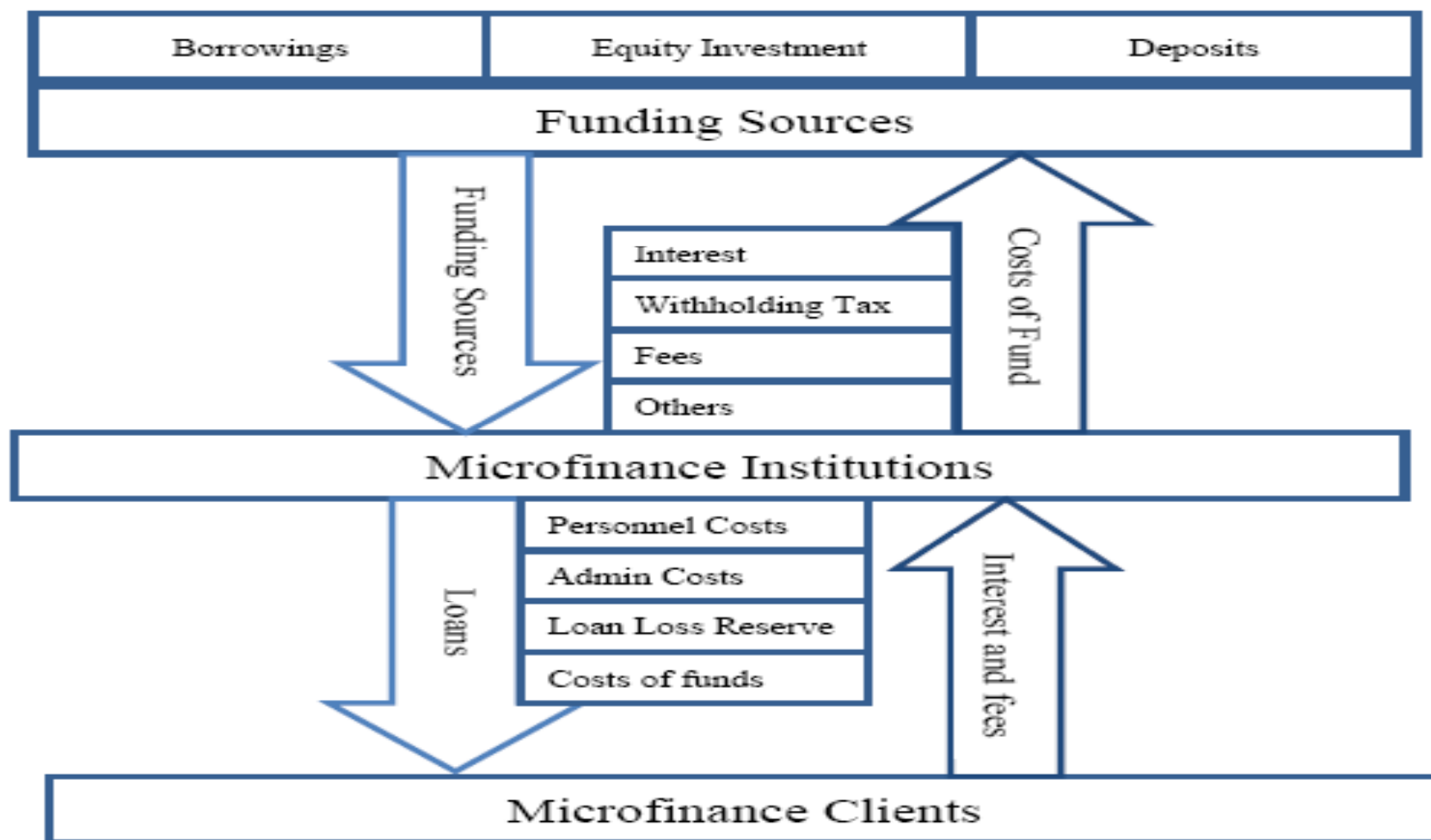
Summary Credit Products

Characteristics	Group Loan	Individual Loan
Target Clients	Traders, Street vendors, Small farmers, Service providers (hairdressers, rickshaw drivers), Artisans, Small producers (black smiths, tailors, etc.)	
Currency	KHR, USD, and THB	KHR, USD, and THB
Loan amount	USD5 - 225	\$35 to \$25,000
Loan term	4 to 12 months	4 to 24 months
Interest rate	3 % to 3.5% per month	1.6% to 3% per month
Purpose	For working capital, investment, consumption, health, emergency, purchasing machinery equipment, multi-business purposes	
Collateral	Group guarantee	Physical collateral +Personal guarantee

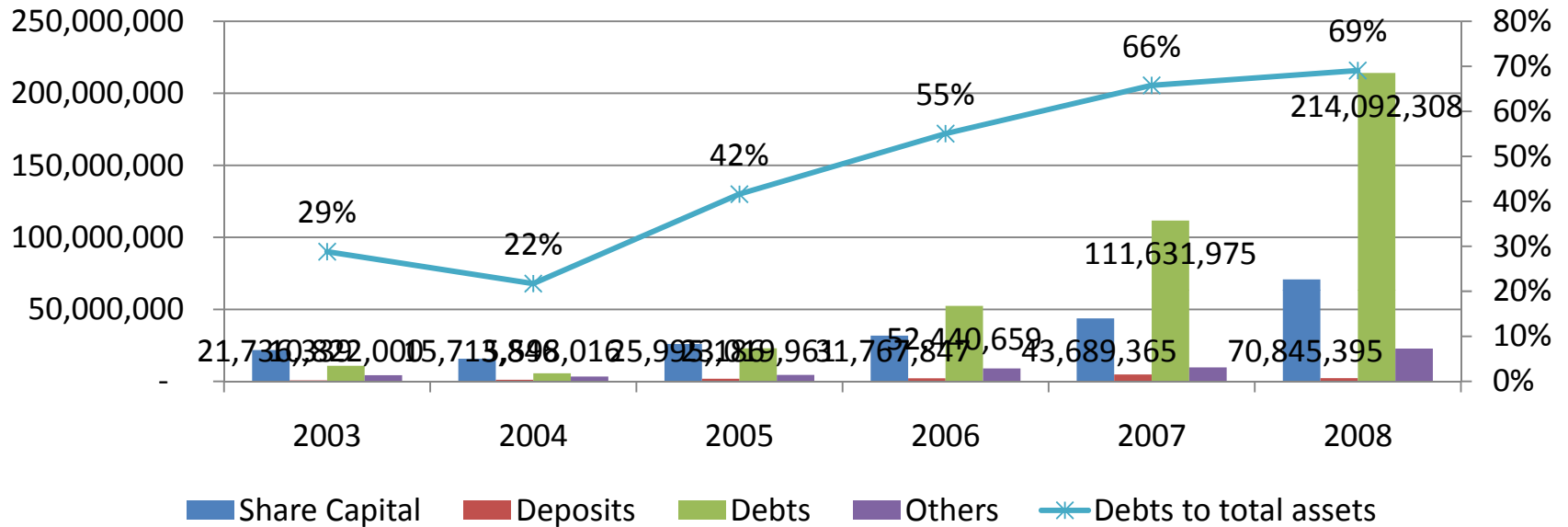
How Microfinance services are used by the clients?

- To respond to economic opportunity: By having loan, **Start or expand business.**
- To invest in the future: **By making deposit client can save for their future needs, the money is safe and generates income through interest earned.**
- To protect against bad times: By having loan or savings, the clients can manage risks better, can protect assets , and can absorb loss better.
- **If they use microfinance services in the right way, their living standard will be upgraded, family economic will improve so that contribute to country economic development,**

Funding Sources and Interest Rate



Funding Sources



- The main sources of funds:
 - Share capital
 - Debt Financing
 - Deposits

How to Set the Interest Rate

1. Formula

Simple method:

Interest Rate = Funding Costs + Loan Loss Provision + Operating Costs + Costs of Capital

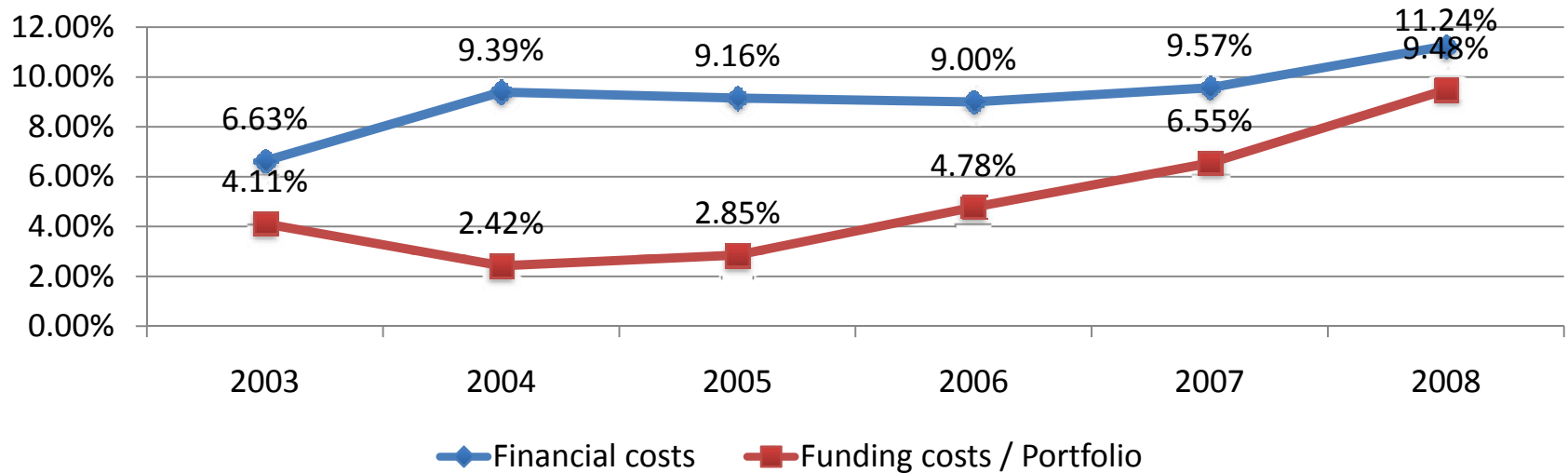
Standard method:

Interest Rate = (Funding Costs + Loan Loss Provision + Operating Costs + Costs of Capital)/(1 - Loan Loss Provision)

2. Definitions

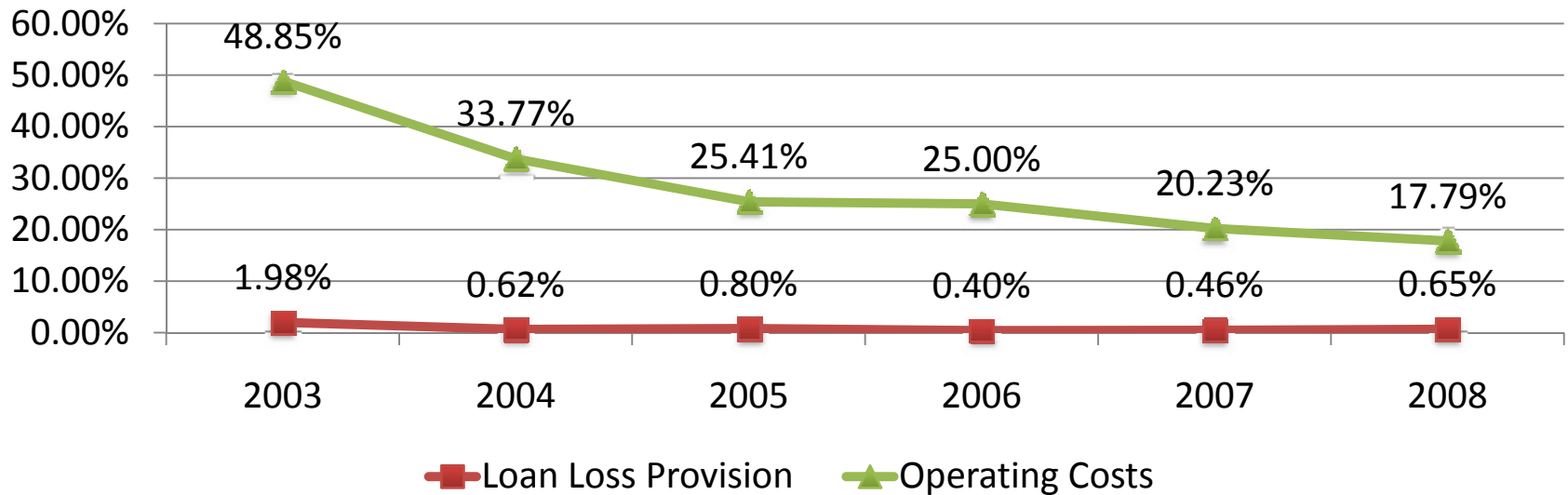
- Costs of Funds: All financial expenses paid to lenders and depositors and other related costs
- Operating costs consist of personnel costs, rental, transportation, other admin costs
- Loan loss provision is the reserves to prevent the bad loans
- Costs of capital is the required return from the investment

Costs of Fund



- The financial costs includes:
 - Interest
 - Fee (upfront, front-end, annual monitoring fee)
 - Withholding tax (14%)

Operating Costs and LLP



- Operating costs consist of personnel costs, rental, transportation, other admin costs
- Loan loss provision is the reserves to prevent the bad loans

Set the Interest Rate

1. Simple method:

Interest Rate = Funding Costs + Loan Loss Provision + Operating Costs + Costs of Capital

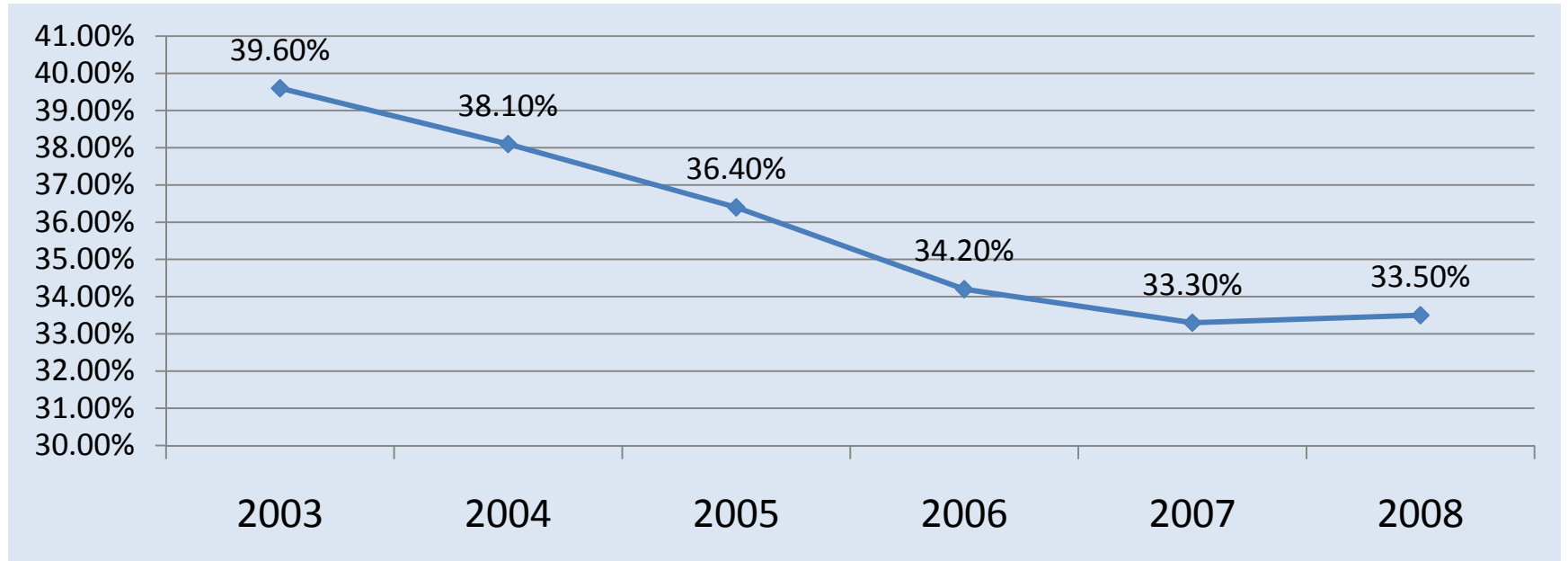
Components	Annual Rate
a) Funding Costs	9.48%
b) Loan Loss Provision	0.65%
c) Operating Costs	17.79%
d) Required Profit	5.58%
e) Interest Rate (e=a+b+c+d)	33.50%

2. Formal method:

Interest Rate = (Funding Costs + Loan Loss Provision + Operating Costs + Costs of Capital)/(1 - Loan Loss Provision)

$$(9.48\% + 0.65\% + 17.79\% + 5.55\%)/(1 - 0.65\%) = 33.72\%$$

Interest Income



Conclusion

- Lowering interest rate leads MFI to:
 - No sustainability
 - Mission drift
- MFI should fix the interest rate high enough to cover all financial costs and operating costs
- Use microfinance in both services: Credit loan and saving deposit

Conclusions - I may delete this slide

- Microfinance is the key breaking poverty cycle.
- During this crisis time needs a strong support from all stakeholders such as client, local authority, creditor, investor and public sector.
- Client should responsible to repay their debt on time and accurate.
- Microfinance operator should operates business in transparency manner and applying customer care concept.
- Use microfinance in both services: Credit loan and saving deposit.