



Progress Report on Tranche Release

Program Number: 32431
Loan Number: 2185
October 2007

Cambodia: Financial Sector Program Loan I (Subprogram III)

CURRENCY EQUIVALENTS

(as of 10 August 2007)

Currency Unit	–	riel/s (KR)
KR1.00	=	\$0.000244
\$1.00	=	KR4,088

ABBREVIATIONS

ADB	–	Asian Development Bank
CAR	–	capital adequacy ratio
FIU	–	Financial Intelligence Unit
FSDS	–	Financial Sector Development Strategy
FSPL	–	Financial Sector Program Loan
GDP	–	gross domestic product
IMF	–	International Monetary Fund
KICPAA	–	Kampuchea Institute of Certified Public Accountants and Auditors
MFI	–	microfinance institution
NBC	–	National Bank of Cambodia
NSDP	–	National Strategic Development Plan
SEDP	–	Socioeconomic Development Plan
TA	–	technical assistance

NOTES

- (i) The fiscal year (FY) of the Government and its agencies ends on 31 December.
- (ii) In this report, "\$" refers to US dollars.

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I. INTRODUCTION

1. The development of Cambodia's financial sector before 2001 was characterized by liberal entry of banking institutions at a time when regulatory and supervisory capacity were weak. During that period, there was a rapid increase in the number of banks and financial institutions (state-owned, joint venture, and family-owned banks, and branches of foreign banks), almost half of which were technically insolvent. This led to a decline in public confidence in the sector. In 1999, the Government enacted a Law on Banking and Financial Institutions and requested assistance from the Asian Development Bank (ADB) to support the development of its financial sector. In response, ADB provided a comprehensive diagnostic review of the financial sector and this in turn led to a Financial Sector Blueprint for 2001–2010. The Blueprint was adopted by the Council of Ministers on 24 August 2001 as the official framework for Cambodia's financial sector over the next 10 years. To help implement the first phase of the Blueprint, ADB's Board of Directors approved the \$30 million Financial Sector Program Loan I (FSPL I)¹ in November 2001.

2. The overall objective of FSPL I is to promote the development of a sound, market-based financial system to enhance resource mobilization and support sustainable economic growth. FSPL I adopted a program cluster approach with three subprograms of \$10 million each to be processed sequentially upon completion of the preceding subprogram. FSPL I focused on: (i) establishing a legal and regulatory foundation for banking, insurance and commercial development; (ii) enhancing financial intermediation and public confidence by developing key information infrastructure and strengthening banking surveillance; (iii) laying the foundation for interbank and money markets; (iv) developing financial market infrastructure by establishing common accounting standards and enforcement mechanisms; and (v) establishing key institutions with appropriate capacity support. Loan proceeds from FSPL I have been used to finance the costs of projects directly linked to reforms in the financial sector.

3. Subprogram I was approved in November 2001 and completed by the end of 2002. Subprogram II was approved in November 2002 and completed in August 2005. Through subprograms I and II, the National Bank of Cambodia (NBC) was able to reconcile and revise old prudential regulations and issue new regulations, fully staff its on-site inspection unit, implement a corrective action system for all banks, introduce two anti-money-laundering regulations, establish a uniform chart of accounts for all banks, establish a credit sharing information system, set up a center for training NBC staff, develop regulations for licensing microfinance institutions (MFIs), establish a unit within the NBC for supervising MFIs, strengthen its off-site supervision capability, transform insurance agents into fully functional insurance firms capable of competing with the state-owned insurance company (Caminco), and establish a unit within the Ministry of Economy and Finance to supervise insurance business. Key legislation governing insurance, accounting, and commercial enterprises was adopted and the following draft bills were at various stages in the approval chain when subprogram II ended: negotiable instruments and payment transactions, commercial arbitration, government securities, secured transactions, anti-money laundering, insolvency, and private sector securities. Other institutions and associations established during subprogram II include the Bankers Association, a banking training institute, a national accounting council for standard development, and an institute for professional accountants and auditors.

¹ ADB. 2001. *Report and Recommendation of the President to the Board of Directors on a Proposed Program Loan Cluster to the Kingdom of Cambodia for the Financial Sector Program*. Manila.

4. Subprogram III,² built on the achievements of subprograms I and II and was approved on 29 September 2005 for SDR6,763,000 (about \$10 million), to be released in a single tranche. Its aim is to support the Government's continuing efforts to strengthen legal and regulatory foundations and to facilitate growth in financial and commercial activities, enhance banking infrastructure to promote and maintain principles of transparency and accountability, strengthen supervision of the insurance industry so as to make it more competitive, prepare the foundation for interbank and money markets, and assist the professional association of accountants to train its members to meet the required accreditation levels. The loan agreement was signed on 8 November 2005 and subprogram III became effective on 11 January 2006 with a closing date for implementation of 30 June 2007, extended to 30 September 2007.

5. An ADB technical assistance (TA) project³ supported the Government in implementing some of the policy actions proposed under FSPL I, subprogram III. The TA for \$500,000 was approved on 29 September and became effective on 11 November 2005, with a closing date of 31 March 2007, extended to 31 December 2007.

II. MACROECONOMIC AND FINANCIAL SECTOR ISSUES AND DEVELOPMENTS

A. Macroeconomic Development

6. Cambodia's economy has expanded strongly over the last decade, with gross domestic product (GDP) growth averaging 7.5% per annum, reaching a record high of about 13.5% in 2005. This impressive growth was largely driven by continued high export growth, albeit in one product (garments), healthy tourism receipts, robust construction activity, and moderate agricultural production. The annual inflation rate, represented by consumer prices, has remained within tolerable levels (single digits) and the exchange rate has been broadly stable. The macroeconomic environment has been reasonably well managed (Table 1). The poverty level (based on \$1 income per day) has been declining rapidly from about 47% in 1994 to 35% in 2004. Per capita household consumption has risen 32% in real terms since 2004 (estimated at \$500 per capita in 2006).

Table 1: Key Macroeconomic Indicators

Indicator	2001	2002	2003	2004	2005	2006
Real GDP Growth Rate (%)	7.7	6.5	8.5	10.0	13.5	10.8
Inflation Rate (average % annually)	0.3	3.3	1.2	3.9	5.8	4.7
Broad Money (% of GDP)	14.1	17.2	18.2	20.3	19.7	23.5
Fiscal Position (% deficit to GDP)	(5.2)	(6.3)	(5.9)	(4.7)	(3.4)	(1.5)
Current Account (% of GDP)	(8.8)	(9.5)	(10.6)	(8.2)	(9.4)	(7.2)
Foreign Reserves (months of imports)	3.1	3.4	3.3	3.0	2.8	2.8
GDP in Absolute Value (\$ million)	3,980	4,273	4,656	5,315	6,278	7,254
Exchange Rate (average)	3,924	3,917	3,979	4,019	4,097	4,107

GDP = gross domestic product.

Sources: National Bank of Cambodia, National Institute of Statistics, and Ministry of Economy and Finance.

7. To maintain strong economic growth, in May 2006 the Government adopted the third National Strategic Development Plan (NSDP III). This accords high priority to accelerating broad-based and across the board reforms in all sectors, to ensure rapid and orderly

² ADB. 2005. *Report and Recommendation of the President to the Board of Directors on a Proposed Loan and Technical Assistance Grant to the Kingdom of Cambodia for Subprogram III of the Financial Sector Program*. Manila.

³ ADB. 2005. *Technical Assistance to the Kingdom of Cambodia for Implementing the Financial Sector Program*. Manila (TA 4656-CAM).

development of the country. The Government has initiated steps to strengthen and broaden the base for growth, with a stronger focus on agriculture (including irrigation), governance and government capacity, trade and investment, reorienting capital outlays toward the development of rural areas, agro-industry, and small and medium-sized enterprises. The financial sector plays a significant and vital role in all these processes.

8. Fiscal performance continued to improve in 2006, with the overall deficit estimated at 1.5% of GDP (3.4% in 2005), narrowing the recent deficit sharply. Recurrent revenues grew strongly to 11.6% of GDP because of increased tax collections. The Government's Public Financial Management Reform Program, launched in December 2004, also started to yield results, with an increasing proportion of customs and tax revenues being collected through the banking system and a growing share of treasury payments to suppliers made by check instead of cash. Expenditures have risen less rapidly than receipts and accounted for 13% of GDP, reflecting growth in current spending related to higher outlays in social sectors, defense, and civil service salaries. As in the past, overall fiscal deficit was financed by concessional loans and grants.

9. During 2006, merchandise exports expanded by an estimated 27%. Garments, which accounted for 72% of total exports, rose by only 20.7% in value terms, despite stronger volume growth. This was due to lower unit prices as a result of stiffer global competition. Exports of natural rubber also rose sharply, but from a low base. Imports increased at a lower rate than exports (by 20.3%). With little change from the 2005 level, the trade deficit was offset to some extent by growth in receipts from tourism, and the current account deficit (excluding official transfers) narrowed to 7.2% of GDP. The 2006 deficit was more than covered by concessional aid and inflows of foreign direct investment, leading to a larger overall balance of payments surplus. Gross international reserves of \$1.2 billion at the end of April 2007 provided about 2.8 months of import cover. External public debt was estimated at \$3.3 billion, or 46% of GDP, nearly 60% of which is owed to the Russian Federation and the United States. Debt to those countries is not being serviced while negotiations for debt relief are underway. The debt service ratio relative to exports of goods and services at end-2006 was low at 0.6% on a cash basis.

10. GDP growth is projected to be 9% in 2007 and 8% in 2008 following strong economic performance in 2005 and 2006. These strong growth forecasts presume that the Government will maintain fiscal discipline and continue public finance reform to strengthen revenue collection and increase outlays on social sectors and rural infrastructure. The pace of Cambodia's sustained growth will depend very much on capital inflows, domestic consumption, exports, and favorable weather. It will also depend on the speed and substance of banking reforms, and the soundness and viability of the financial system.

B. Government Strategy and ADB's Country Strategy and Program

11. Cambodia's first National Strategic Development Plan for 1996–2000 (NSDP I) marked the Government's first systematic approach to economic growth and poverty reduction, with the Government participating actively in the development process. The promotion of broad-based sustainable economic growth as a strategy for poverty reduction continued in subsequent NSDPs. Robust growth over the past decade and structural reforms have led to a steady decline in the overall incidence of poverty from an estimated 47% in 1994 to 35% in 2004. The gains have been widespread, but not uniform, with the incidence of rural poverty remaining stubbornly high at around 39%. Income disparities between rural and urban areas have increased. An important contributory factor is that economic growth has been narrowly based on clothing and tourism, both of which are urban industries, with weak links to the rural economy.

12. It was in the context of a falling, but still high, incidence of poverty, and a growing rural–urban divide that the Government prepared its third 5-year NSDP 2006–2010. The NSDP, approved by the National Assembly in May 2006, aims to operationalize the Government's Rectangular Strategy and to achieve the interim (2010) targets that the Government has in sight as it progresses towards its Millennium Development Goals. The Rectangular Strategy, adopted in July 2004, sets out the Government's reform agenda as a series of four interlocking rectangles with governance at its core. One of the four strategies focuses on the type of environment required to implement and promote economic growth through agriculture, infrastructure, private sector, and human resources development.

13. ADB's overarching goal in Cambodia is sustainable poverty reduction. In line with the priorities and strategies identified in the Government's Rectangular Strategy, the ADB country strategy and program⁴ focused on three strategic pillars: (i) broad-based economic growth through investments in physical infrastructure, development of the financial sector, support for greater regional integration, sustainable development of small and medium-sized enterprises, and investments in agriculture and irrigation; (ii) inclusive social development through basic education, empowering vulnerable groups such as women and ethnic minorities, control of communicable diseases, provision of rural water supply sanitation facilities, and community-based sustainable management and conservation of natural resources in the Tonle Sap basin; and (iii) good governance, through improvements in public financial management to enhance the development effectiveness of public expenditures and decentralization initiatives to strengthen local participation in government and improve public service delivery.

14. The country strategy and program specifically stated that ADB would continue its leading role in supporting financial sector development and that ADB's future involvement in the financial sector would depend on the outcome of the financial sector Blueprint update. The Blueprint update, now known as the Financial Sector Development Strategy (FSDS) 2006–2015, was approved by the Council of Ministers in February 2007. The FSDS states that financial sector development is not an end in itself; rather it is one aspect supporting the development and reduction of poverty in Cambodia. There are many things that need to be done to achieve this difficult goal, but there is general agreement that accelerating and diversifying growth is key and that financial sector development supports this objective. Reform and change are essential for growth. At the same time, expanding finance brings risks; hence, the context in which financial development occurs must be carefully considered. There needs to be a focus on prudential risk reduction, transparency, and the uniform application of rules and regulations.

C. Financial Sector

15. At present the formal financial system comprises the NBC, 16 commercial banks, six specialized financial institutions and two representative offices of foreign-based banks; 17 licensed and 26 registered MFIs; and five insurance companies. Cambodia has yet to establish bond or securities markets. The predominantly rural nature of the economy, high transaction costs, the inability of the real sector to put together bankable projects, and low creditor confidence have been the main reasons for the low level of formal intermediation and outreach within the sector, the slow development of non-bank financial institutions, and the limited range of products and services being offered. The financial crisis in the late 1990s, the adoption of the Banking and Financial Institutions Law and membership of the Association of Southeast Asian Nations (ASEAN) in 1999, and the World Trade Organization (WTO) in 2003 helped to provide a strong impetus for reform in the financial sector.

⁴ ADB. 2005. *Country Strategy and Program (2005–2009): Cambodia*. Manila.

16. Dominated by the banking system, Cambodia's financial sector has gone through major restructuring and reforms since the mid-1990s. A good example is the NBC-led relicensing program that brought about the closure of 16 non-viable banks in 2002, raised capital requirements for the remaining banks to \$13 million equivalent and set the minimum capital adequacy ratio (CAR) at 15% of risk-weighted assets. Privatization of the only state-owned commercial bank (the Foreign Trade Bank) was completed in 2005. Banks have been free to set their own interest rates since 1995. However, while banks are free to determine their own interest rates, the average annual interest rate spread is still high—it was 11.9% in 2006 (a decline from around 15% in 2001)—reflecting the banks' perception of high credit risks.

17. **Bank supervision has improved but the system is still vulnerable to shocks.** The capacity of the NBC for off-site supervision of banks has been upgraded and strengthened. Regulatory standards have been gradually improved and relevant prudential regulations added to maintain NBC's primary objective of enhancing the soundness of the banking system. All banks adopted a uniform chart of accounts in 2004 and began publishing annual audited financial reports in 2005. At the end of 2006, the Bank Supervision Department of the NBC published its second annual report providing a very detailed and comprehensive assessment of the banking system. These developments are evidence that the NBC is serious about market transparency and has made significant progress toward establishing a sound regulatory and efficient supervisory regime to enhance the integrity of the banking system. As reported at the end of 2006, the average CAR for all banks was 26% (32% in 2005), the overall ratio of non-performing loans to total net loans was 9.8% (8% in 2005), the loan to deposit ratio was 63% (60% in 2005), and the average return on assets was about 2.8% (1.8% in 2005).

18. **Shallow Financial Intermediation.** The financial sector has been growing from a very low base (Table 2). The M2/GDP ratio was about 21% at the end of 2006 compared with 13% in 2001. Credit to the private sector increased from 6.2% of GDP in 2001 to 12.3% in 2006 and total bank deposits to GDP was 18.2% in 2006, compared with 10.4% in 2001. There is increasing public confidence in the banking system as depicted by total deposits, which are growing by an annual average of 30% and bank assets which grew by an annual average of 27% between 2001 and 2006 (private sector credit increased by 52% in 2006). While growth in the banking system is facilitating economic development, the fast pace of growth requires strong supervision and surveillance to ensure banks are weighing all the risks properly. Lending is highly concentrated, with the leading five banks accounting for 67% of total lending at the end of 2006. However, competition is slowly picking up with some evidence of market segmentation emerging. There is no legal barrier for the entry of foreign banks and, as at the end of 2006, in eight of the commercial banks foreign owners were in the majority.

19. **Insurance is constrained by limited public awareness and weak coordination.** Progress in the insurance industry has been mixed. Insurance is still a new concept to most Cambodians and there has been little public awareness building by the industry as a whole. The enforcement of the three insurance products available locally (commercial vehicle, construction site and passenger vehicle liabilities) has been very weak and coordination between the ministries assigned to oversee their implementation (the Traffic Department and the Ministry of Interior) and the Ministry of Economy and Finance has been poor. The lack of capacity to provide underwriting, actuarial, loss adjustment, and fund management services, or effective supervision remains, while current accounting practices (statutory or otherwise) are inadequate. There is a need to introduce a risk-based capital framework. Revisions to the licensing framework, supervision approach and the legal framework for insurance businesses are important steps to put the industry on a sustainable path and they will require the strong support of the Ministry of Economy and Finance.

20. **A rapidly-growing microfinance subsector faces financial resource constraints.** Banking activities in rural areas, although not fully developed, are improving, and MFIs provide most of the formal financial services available (mostly credit). With ADB's support, NBC has successfully developed a regulatory framework for MFIs and implemented the licensing and registration process. The microfinance subsector is expanding rapidly, with total assets growing by about 80% in 2006, and the assets of a number of individual institutions expanding by 200% annually. Despite this growth, a large part of the country is not covered by formal financial institutions. As such, it is important for NBC and Ministry of Economy and Finance to identify the areas requiring policy and regulatory changes that would further expand services, products, and savings mobilization (directly or indirectly).

Table 2: Key Financial Data

Indicator	2001	2002	2003	2004	2005	2006
M2/GDP (%)	13.0	15.6	16.5	18.6	18.7	20.8
Average CAR (%)	58.0	49.0	41.0	34.0	32.0	26.0
Private Sector Credit/GDP (%)	6.2	6.3	7.3	8.6	9.4	12.3
Total Deposit/GDP (%)	10.4	12.7	13.3	15.2	14.8	18.2
NPL/Total Loan (%)	8.0	15.0	14.0	10.0	8.0	9.8
Average Return on Assets (%)	0.6	1.1	0.9	1.2	1.8	2.8
Average Interest Spread (%)	15.0	14.0	13.3	12.9	12.0	11.9
Total Assets of Five Largest Banks/Total Assets (%)	59.0	70.0	69.0	67.0	63.0	67.0
Total Deposits of Five Largest Banks/Total Deposits (%)	75.0	84.0	82.0	79.0	70.0	71.0
Number of Licensed and Registered MFIs	0.0	30.0	34.0	38.0	39.0	40.0
Total Number of MFI Borrowers ('000)	410.0	328.0	265.0	322.0	368.0	471.0
Total Amount of MFI Loans (\$ million)	35.9	51.3	32.6	40.9	49.2	92.2
Number of Insurance Firms	1.0	1.0	4.0	3.0	3.0	3.0
Total Insurance Premium (\$ million)	3.6	5.5	8.8	10.1	10.8	13.0

CAR = capital adequacy requirement, GDP = gross domestic product, M2 = a broad money supply measure, MFI = microfinance institution, NPL = nonperforming loan.

Sources: National Bank of Cambodia and Ministry of Economy and Finance

D. ADB's Development Experience

21. The key lessons from FSPL I and associated TA projects in the sector include the following.

- (i) **The need for a long-term perspective.** The adoption of a medium-term blueprint for the financial sector meant that the Government had a set of long-term objectives as an anchor to guide and shape medium-term policy design and implementation. The in-built flexibility and changes in the underlying policy environment facilitated the recent update of the Blueprint and its acceptance by the Government in February 2007 as the FSDS 2006–2015. The close consultative process involving the Government, ADB and other donors, strengthened the Government's ownership and increased the potential for involvement by donors.

- (ii) **Lead role in the sector.** ADB has established a lead role in the sector through its involvement in the development of the financial sector Blueprint (2001–2010) and its update (FSDS 2006–2015). This has enabled effective policy dialogue with the Government and built the Government's trust of ADB's commitment to the sector. The other partner providing consistent long-term support to the sector is the International Monetary Fund (IMF), through a poverty reduction and growth facility (PRGF) program that concluded in 2003 and several ongoing TA projects. ADB and the IMF consult closely to ensure complementarity.
- (iii) **Long-term partnership requires flexibility in design.** Financial sector reforms are complex and involve major changes to the legal and regulatory framework, institutional arrangements, financial infrastructure, and human capacity. Sufficient time must be allocated to program implementation and there must be design flexibility. The use of the program cluster approach under FSPL I provided the opportunity to refine the proposed policy actions for succeeding subprograms to reflect the Government's achievements, changes in the policy environment, and lessons learned from the previous subprogram.
- (iv) **Substantial TA resources required.** Under FSPL I, the Government adopted legal, policy, and institutional measures, many of which were relatively new concepts and therefore required extensive coordination and consultation to ascertain stakeholders' understanding, acceptance and implementation of the new measures. Substantial TA support was necessary to ensure that best practices were incorporated and then consolidated throughout the implementation period to achieve intended results.
- (v) **National and commune council elections.** Implementation of FSPL I, subprogram II was delayed by almost 2 years following the national general election of 2003 and the subsequent 1 year delay in forming the new Government. Subprogram III was delayed by 3 months because of the Commune Council election in April 2007. Both elections (commune and national) affected the passage of the draft laws targeted by FSPL I through the Council of Ministers and the National Assembly. This is a lesson for program design as the next national general election has been scheduled for July 2008.
- (vi) **Awareness of emerging risks.** The transition from a centrally-controlled to a market-led economy changes the rules of the game and creates new forms of risk. The presence of international banks, the offer of more sophisticated services to depositors and the increase in lending demonstrate the increasing confidence that investors have in Cambodia's financial system. However, with these encouraging developments come new risks and challenges, the awareness of which must be strengthened in both public and the financial sectors. New ways for mitigating risks must also pursued.
- (vii) **Strong anticorruption initiatives.** Previous decades of conflict and isolation have resulted in weak governance and perceived high levels of corruption, as demonstrated, for example, by the Transparency International (TI) Corruption Perceptions Index, which shows perceived corruption levels in Cambodia to be high (though comparable to those in many other developing countries in the Asia and Pacific region). The speedy implementation of changes often increases institutional risks and opportunities for corruption. FSPL I reforms were designed

to deter or minimize the impacts of corruption, and to encourage the Government to act on cases of malfeasance.

III. PROGRAM IMPLEMENTATION

A. Status of Policy Actions for Tranche Release

22. The Government has demonstrated its commitment to financial sector reform by carrying out actions in a number of key areas, in line with the objectives of FSPL I, subprogram III. The design and monitoring framework (with indicators for development impact) is in Appendix 1 and the detailed status of implementation of policy conditions is presented in Appendix 2. The Government's successful implementation of all 12 policy actions associated with the release of the single tranche under subprogram III is summarized below.

B. Review of Progress in Implementation

1. Development of the Banking Subsector

a. Development of the Banking Subsector Infrastructure

23. **Secured Transactions Law Adopted by the National Assembly.** Following formal approval by the Council of Ministers on 10 June 2005, the draft law was submitted to the National Assembly, together with a letter signed by the Prime Minister, in July 2005. The underlying purpose of the Secured Transactions Law is to facilitate growth in the economic sector by making credit available, through secured transactions, to all types of Cambodian businesses. The creation of a legal framework that allows a creditor to take security interest over a debtor's movable property is the key to small and medium-sized enterprises (SMEs) that do not own land and buildings but require access to readily available, cheap and long-term credit. Committee number 2 of the National Assembly took time to review the provisions of the draft Secured Transactions Law and to and harmonize them with the draft Civil Code. The Secured Transactions Law was finally adopted by the National Assembly on 5 April 2007, endorsed by the Senate on 25 April 2007, and the Royal Kram was issued on 24 May 2007. The Ministry of Commerce has included the Secured Transactions Law in its on-going public dissemination program throughout Phnom Penh and other provinces.

24. **Public Registry for Secured Transactions.** The main objective of the online filing registry, a major advance in Cambodia, is to reduce the involvement of civil servants in the registration and collection of fees. This will enhance priority claims on securities and provide public access to information on secured chattels and their owners. The Ministry of Commerce approved a time-bound action plan for establishing the registry in May 2005. ADB provided TA to improve the legal infrastructure in the financial sector⁵ by designing and establishing the online filing registry for secured transactions and procuring hardware and software. The design of the system for an online filing registry was completed in 2004 and procurement began in 2005. All the hardware, system software, and application software have been procured, installed, and tested. The domain name www.setfo.gov.kh has been registered at Ministry of Post and Telecommunication (MPTC). Two filing office staff have been appointed and trained and a contract with an internet service provider came into effect in October 2006. A contract was

⁵ ADB. 2001. *Technical Assistance to the Kingdom of Cambodia for Improving Legal Infrastructure in the Financial Sector*. Manila (TA 3661-CAM).

signed with ACLEDA Bank to collect online filing fees. The Online Filing Registry was officially launched by the Ministry of Commerce in September 2007.

25. **Financial Intelligence Unit (FIU).** The policy condition required the NBC to form a precursor to the FIU and to undertake the preparatory work required for the establishment of an FIU when the anti-money laundering law was approved. Under the TA on implementing the financial sector program (footnote 3), ADB provided consulting support to help establish the precursor to the FIU in June 2005 with a staff of six under the Bank Supervision Department of NBC. Training workshops on anti-money laundering in general, procedures to assess suspicious transactions reports, roles of compliance officers at banks and financial institutions, and anti-money laundering assessment were conducted jointly by NBC and AUSTRAC throughout 2005 and 2006. The anti-money laundering/CFT law was adopted by the National Assembly in May 2007 and the formal establishment of the FIU is underway.

b. Commercial Law Development and Capacity Building

26. **Law for Commercial Arbitration adopted by the National Assembly.** The draft law was submitted to the National Assembly, together with the Commercial Enterprises Law in 2004. At the committee level of the National Assembly, discussions to harmonize the procedures and key provisions of the draft law with the draft Civil Procedures Law took some time before the law was adopted by the National Assembly in March 2006. The law provides the legal basis for dispute resolution alternatives for small commercial transactions. ADB provided technical assistance (footnote 3) to help develop the implementing sub-decree and assist the Ministry of Commerce in establishing the National Arbitration Center.

27. **Submission of the Draft Insolvency Law to the National Assembly.** The law was drafted in 2002 with IMF support and submitted to the Council of Ministers in 2003. Considerable time was required for Ministry of Commerce and the Ministry of Justice to ensure coherence and consistency of the draft insolvency law with the draft civil code prior to its passage through the plenary session of the Council of Ministers. The draft law was endorsed by the Council of Ministers on 17 August 2007 and submitted to the National Assembly thereafter. It provides the legal basis and procedures for administering insolvent corporations.

28. **Dissemination of Commercial Laws via the Internet.** With budget support from the Ministry of Economy and Finance, the Ministry of Commerce established a website (www.cambodiacommerciallaws.com) and, in December 2005, posted all approved commercial laws. In addition to the dissemination of commercial laws through the internet, the Ministry of Commerce has held road shows in the provinces to raise public awareness of the new commercial laws.

29. **Commercial Law Curriculum Based on the New Commercial Laws.** The Ministry of Commerce has carried out workshops and seminars in the provinces on topical areas of commercial and financial law through a team of trainers and lecturers. A training program targeting mid-level legal drafters, arbitrators, judges and other key Government officials and legal trainers and lecturers is being carried out. A compact disc containing training modules based on existing commercial laws has been developed by Ministry of Commerce. Under the previous TA project (footnote 3), ADB provided consultancy support to help the Ministry of Commerce work with law institutes so a commercial law curriculum based on the new commercial laws could be used to train judges, lawyers, and legal and clerical staff. Three legal institutions have been selected to develop this curriculum. The commercial law curriculum for

the 4-year Business Degree Program has been adopted and the teaching of the program is expected to commence in the September 2007 semester.

2. Development of the Insurance Subsector

a. Strengthening the Capacity of the Regulator

30. Prudential Regulations to Enhance Solvency, Liquidity, and Corporate Governance. Under the previous TA (footnote 3), ADB provided consultancy support to help the Ministry of Economy and Finance review, update, and implement prudential regulations to enhance solvency, liquidity, and corporate governance requirements and to support the insurance regulator. At the conclusion of the consultancy assignment, ministerial *prakas*⁶ covering corporate governance, solvency and liquidity were issued in March 2007.

b. Promoting Private Sector Involvement in the Insurance Subsector

31. Restructure Caminco. A policy condition requires the Ministry of Economy and Finance to implement the key actions of the plan to restructure Caminco, as agreed with ADB, with a view to the Government divesting itself of its shares at the earliest opportunity. The restructuring plan was approved by the Senior Minister of Economy and Finance in August 2005. Under the TA (footnote 3), ADB provided consultancy support to help the ministry implement key activities of this plan and divest the Government's shares at the earliest opportunity. A three-member board audit committee was established in December 2005 and has been functioning since 2006. A 3-year business plan (including a training plan for 2006 and a marketing strategy) was developed and adopted by the board of Caminco in December 2005. The implementation of the plan has been monitored closely by Caminco's management team since 2006. Accounting policies and internal procedures to enhance financial disclosure by Caminco have been approved and implemented. In preparing for the privatization of Caminco, a long-list of 20 international firms was put together, following which a shortlist was prepared by an inter-ministerial privatization committee. Invitations for expressions of interest were sent out and three firms responded. Each signed a confidential agreement and was provided with an information memorandum with a request that formal proposals be made by 7 February 2007. Two of the three firms (from New Zealand and Singapore) later informed Caminco Management that they were no longer interested in pursuing a due diligence study. The third firm, Prudential Insurance, requested an extension by 1 month and has not made further contact since 7 March 2007. The Caminco Board assumed that Prudential Insurance was no longer interested in pursuing its bid and it has decided to continue with the internal restructuring of Caminco and focus on building its market share before re-visiting the need for an international strategic partner.

3. Development of Interbank and Money Markets

a. Legal Framework for Money Market Development

32. Law on Negotiable Instruments and Payment Transactions Adopted by the National Assembly. The draft law was submitted to the National Assembly with a letter from the Prime Minister in January 2005. The law was adopted by the National Assembly in March 2006 providing the legal basis for further developing the payments system, introducing new negotiable instruments, and promoting the development of a money market.

⁶ Khmer name for regulations and/or instructions issued by Government ministers or Governor of the NBC.

33. **Implementing Regulations for the Law on Negotiable Instruments and Payment Transactions.** With technical support from the IMF, NBC drafted the implementing regulations for this law. Four regulations were prepared: (i) on the control of systemic risks, (ii) on the operation of settlement accounts, (iii) on payment clearing systems, and (iv) on licensing of money service businesses. With the exception of the last regulation, the *prakas* covering the first three regulations were issued in December 2006. NBC required more time for consultation with affected stakeholders before issuing the fourth regulation. Under the TA (footnote 3), ADB helped NBC to disseminate the new law and its implementing regulations.

4. Development of Accounting and Auditing Practices

a. Support to Develop the Technical Capacity of Professional Members of the Kampuchea Institute of Certified Public Accountants and Auditors (KICPAA)

34. **Scholarships for the Technical Development of Professional KICPAA Members.** The Government has been providing 70 scholarships a year since 2003 to train candidates to reach the KICPAA accreditation level. The Ministry of Economy and Finance continued to provide allocations for the 70 scholarships in the 2006 and 2007 recurrent budgets. New criteria and administrative procedures for the competitive selection of scholarship candidates, which were formulated by the National Accounting Council/KICPAA and approved by the Senior Minister of Economy and Finance in April 2006 are currently being implemented. Public announcements of the scholarships are made before the beginning of each semester to enable open competition.

IV. CONCLUSIONS

35. The commitment to successfully implement subprogram III of the FSPL I by the Government agencies concerned was clearly evident throughout the implementation period, despite periodic shortages of qualified staff. There was clear ownership of the overall program and demonstration of a clear understanding by the Government of its role in developing the financial sector under FSPL I as well as ownership of the individual measures in subprogram III (which had been jointly agreed to by the Government and ADB). Given the significant progress in implementing the overall program and full compliance with all 12 tranche conditions, the release of the single tranche is justified.

V. THE PRESIDENT'S DECISION

36. In view of the solid progress made in implementing the Financial Sector Program Loan I subprogram III, and the Government's compliance with all 12 conditions for the single tranche, I am satisfied with the overall implementation of the Program and I note that the conditions for the release of the tranche have been fulfilled. In accordance with the established procedures, the release of the single tranche in the amount of SDR6,763,000 equivalent under FSPL I subprogram III, will be effective not less than 10 working days from the date of circulation of this progress report.

12 Appendix 1

Design Summary	Performance Indicators/Targets	Results Achieved	Monitoring Mechanisms	Assumptions and Risks
Impact Develop a sound, market-based financial system to support resource mobilization and sustainable economic growth	Increased M2/GDP ratio	M2/GDP 2006: 20.8% (2004: 18.6%)	Economic reports, official statistics	
	Increased financial assets/GDP ratio	Total private sector credit/GDP 2006: 12.3% (2004: 8.6%)	ADB review missions	
	Increased capital adequacy and bank profitability	CAR 2006: 26% (2004: 34%) Average ROA 2006: 2.8% (2004: 1.2%)		
	Reduced level of nonperforming assets	NPL 2006: 9.8% (2004: 10%)		
	Tightened interest rate spread	Average interest spread 2006: 11.9% (2004: 12.9%)		
	Diversified financial services	Deposit services now include debit and credit cards		
	Enhanced rural financial services	Number of MFI borrowers 2006: 471,000 (2004: 322,000)		
	Diversified insurance products	The three compulsory non-life categories now include marine cargo and fire		
	Increased interbank market activities	Not much development as most banks are highly liquid		
	Legal basis for capital market development established	Several commercial laws enacted and being implemented	Official copies of laws, decrees, regulations, etc. from NBC and Ministry of Economy and Finance	

Design Summary	Performance Indicators/Targets	Results Achieved	Monitoring Mechanisms	Assumptions and Risks
Outcome 1. Enhance banking intermediation, public confidence, and capacity building 2. Establish legal and regulatory framework for insurance development 3. Lay foundation for the development of interbank and money markets 4. Create an enabling environment for capital market development 5. Develop financial infrastructure	Strengthened banking supervision Core information infrastructure and safety net developed Human capacity in public and private sectors strengthened Strengthened insurance supervisory system and prudential regulations strengthened Private sector development in the insurance sector Development of compulsory insurance enforcement and monitoring mechanism Establishment of basic legal framework for inter-bank/ money markets Establishment of legal system Establishment of accounting and auditing standards and enforcement mechanism	Bank supervision unit now fully staffed and functioning with hands-on training provided by ADB consultants Uniform chart of accounts for banks adopted CBS established with short and medium-term training programs offered Supervision unit established at Ministry of Economy and Finance and staff trained State-owned insurance firm restructured as a first step in the privatization process Monitoring mechanism established and adopted Negotiable instrument and payment transactions law enacted with implementing regulations adopted Commercial arbitration law and secured transactions law enacted 15 accounting and 10 auditing standards (internationally based) adopted and being implemented	Reports of various financial institutions ADB review missions	Assumptions The Government's financial sector strategy is implemented Macroeconomic stability continues Political commitment to undertake the reforms continues NBC, Ministry of Economy and Finance, Ministry of Commerce and all stakeholders remain committed Capacity to undertake the reforms is present Implementation of governance reforms is as specified in the Governance Action Plan

Design Summary	Performance Indicators/Targets	Results Achieved	Monitoring Mechanisms	Assumptions and Risks
Subprograms A. Subprogram I 1. Banking subsector a. Strengthen bank supervision and prudential regulations	<p>NBC to reconcile old prudential regulations with new ones and issue clarifying guidance to commercial banks</p> <p>NBC to fully staff the on-site inspection division of the Banking Supervision Department, in a way that is acceptable to ADB</p> <p>NBC to adopt a formal procedure for soliciting comments from the private sector on proposed revisions to laws, regulations, procedures, and policies affecting banking subsector</p> <p>NBC to adopt surveillance and inspection procedures, including standardization of reports submitted by commercial banks. Unless specified otherwise in the NBC regulations, these procedures are also to be applied to licensed MFIs</p> <p>NBC to adopt a prompt corrective action system for commercial banks, acceptable to ADB. A similar system to be applied to licensed MFIs with modified capital adequacy standards</p>	<p>Fully implemented in 2002 with periodic updates since then</p> <p>Fully implemented in 2002 with on-going training provided</p> <p>Being implemented since 2002</p> <p>Fully implemented since 2002. Separate prudential regulations have been issued for MFIs</p> <p>The system was adopted in 2002 and initial implementation required technical support</p>	<p>Official copies of effective prudential regulations and the clarifying guidance</p> <p>Official copies of organization chart of the Banking Supervision Department, job descriptions, and NBC decision regarding staff appointment</p> <p>Official copy of the procedure for soliciting comments from the private sector</p> <p>Official copy of the surveillance and inspection procedures</p> <p>Official copy of NBC regulations on prompt corrective action system</p>	<p>NBC is committed to the reform</p> <p>NBC is willing to communicate with the private sector</p>

Design Summary	Performance Indicators/Targets	Results Achieved	Monitoring Mechanisms	Assumptions and Risks
<p>b. Capacity building</p> <p>2. Insurance subsector Establish supervisory and regulatory framework for insurance development</p> <p>3. Money/interbank markets Create interbank market arrangements</p>	NBC to adopt an anti-money laundering regulation. Unless specified otherwise in the NBC regulations, this regulation should also be applied to licensed MFIs	Two key regulations <i>Know Your Customer</i> and <i>Reporting Suspicious Transactions</i> were adopted in 2002	Official copy of the anti-money laundering regulation	NBC and FTB management are committed to these activities
	NBC to establish a CBS as a subsidiary of NBC with separate management and accounts	CBS has been established and is operating its own budget sourced from trainees	Official copy of the NBC decision to establish CBS as a subsidiary	
	NBC to ensure that FTB management adopts a comprehensive staff training program, including accounting, risk management, asset/liability management, and a management information system	Staff training program was adopted in 2002 followed by the privatization process which was completed in 2005	Confirmation letter from FTB management with official copy of the training program and budget approved by FTB board	
	Ministry of Economy and Finance to establish an insurance supervisory unit	Insurance supervisory unit established within Ministry of Economy and Finance in 2002	Official copy of the Ministry of Economy and Finance regulation to establish the insurance supervisory unit; Official copy of personnel announcement	Ministry of Economy and Finance is committed to the process. Capacity is built in the insurance supervisory unit
	Ministry of Economy and Finance to ensure issuance of a subdecree to implement the Insurance Law	Implementation of the sub-decree began in 2002	Official copy of the subdecree	
	NBC to recognize bankers association as a self-regulatory organization	Bankers association operating independently since 2002	Official copy of the articles of association approved by NBC	NBC and the commercial banks are committed to the process
	Approved articles of association must include provisions for the	Articles of association adopted; work on establishing a CISS	Confirmation letter from NBC with official copy of document	Collaboration of NBC and commercial banks

Design Summary	Performance Indicators/Targets	Results Achieved	Monitoring Mechanisms	Assumptions and Risks
4. Accounting and auditing and legal infrastructure	establishment of interbank market arrangements, arrangements for sharing credit information among the members of the bankers association, and a banking institute for private bank staff	has commenced. Banking institute established and fully operational after ADB provided initial technical support. The institute has since been taken over by MPDF	establishing the interbank markets working group	
	NBC and the bankers association to establish a working group to establish interbank market arrangements, arrangements for sharing credit information among the members of the bankers association, and a banking institute	On-line CISS launched in August 2006 and banking institute established in 2002		
	Ministry of Economy and Finance to submit to the National Assembly a draft law on corporate accounts, their audit, and the accounting profession	Accounting law enacted in 2002	Official copy of the draft law on corporate accounts, their audit, and the accounting profession submitted to the National Assembly	The Government is committed to establishing and enforcing the accounting standards
	Ministry of Economy and Finance to adopt IAS and ISA to be applied upon the adoption of the law on corporate accounts, their audit, and the accounting profession	15 accounting and 10 auditing standards (internationally based) adopted and implementation started	Confirmation letter from Ministry of Economy and Finance to adopt IAS and ISA	The Government is committed to the reform
	Ministry of Commerce to submit to the National Assembly a draft law on commercial enterprises	Draft commercial enterprises law submitted to the National Assembly and adopted in May 2005	Copy of the draft law on commercial enterprises submitted to the National Assembly	

Design Summary	Performance Indicators/Targets	Results Achieved	Monitoring Mechanisms	Assumptions and Risks
B. Subprogram II 1. Banking Subsector a. Develop banking subsector infrastructure and safety net	<p>NBC to adopt a guideline for the arrangements for sharing credit information among the members of the bankers association; NBC and the bankers association to establish such arrangements</p> <p>NBC to adopt a uniform chart of bank accounts and disclosure rules for the commercial banks consistent with IAS</p> <p>NBC to apply the uniform chart of bank accounts and disclosure rules for the commercial banks, consistent with IAS, to the Rural Development Bank, and to other specialized banks</p> <p>Ministry of Commerce to submit to the National Assembly a draft secured transactions law</p> <p>Ministry of Commerce to adopt a plan to establish a public registry for secured transactions acceptable to ADB</p>	<p>MOU to establish a CISS signed by all commercial banks in 2004 and an on-line CISS launched in August 2006</p> <p>NBC <i>prakas</i> issued in December 2002 requiring all banks to adopt the uniform chart of accounts</p> <p>Uniform chart of accounts adopted by all banks in December 2004 and audited financial statements made publicly available since 2005</p> <p>Draft secured transactions law submitted to the National Assembly in July 2005</p> <p>Ministry of Commerce adopted the plan in May 2005 and design of an on-line registry commenced</p>	<p>Official copy of the guideline</p> <p>Official copy of a uniform chart of accounts and disclosure rules for banks</p> <p>Official copy of the clarifying regulation to apply the uniform chart of bank accounts and disclosure rules for the commercial banks to the Rural Development Bank and other specialized banks</p> <p>Official copy of the draft secured transactions law submitted to the National Assembly</p> <p>Confirmation letter of adoption of the plan from Ministry of Commerce and official copy of plan to establish a public registry</p>	<p>NBC is committed to activities</p> <p>Minimizing costs of non-compliance</p> <p>Ministry of Commerce is committed to the reforms</p>
b. Capacity building	NBC to ensure that CBS establishes a central banking course for NBC professional staff, including a mandatory	CBS began preparation of the courses in October 2002 and launched the programs in July 2003	Confirmation letter from NBC, and official copy of the CBS curriculum	NBC is committed to systematic capacity building

Design Summary	Performance Indicators/Targets	Results Achieved	Monitoring Mechanisms	Assumptions and Risks
2. Insurance Subsector	training program for entry-level professional staff			
a. Establish framework for compulsory insurance	Ministry of Economy and Finance, in consultation with related ministries, to adopt interministerial regulations for development of compulsory insurance	Three inter-ministerial <i>prakas</i> on motor vehicle third-party insurance, construction workers, and passenger transport liability adopted in 2002	Confirmation letter from Ministry of Economy and Finance, and official copy of the compulsory insurance regulations	Capacity is built in the insurance supervisory unit
b. Promote private sector development	Ministry of Economy and Finance to establish a joint venture between the state-owned insurance company and a private insurance company	No private investor expressed interest so Government agreed to restructure the state-owned insurance company	Official copy of the joint venture agreement and articles of incorporation	
3. Interbank/Money Markets	NBC to submit to the National Assembly a draft law on negotiable instruments and payment transactions	Draft law submitted to the National Assembly in January 2005	Official copy of the draft law on negotiable instruments and payment transactions submitted to the National Assembly	NBC is committed to the reform.
4. Accounting and Auditing System and Legal Infrastructure	Adoption of a law on corporate accounts, their audit, and the accounting profession	Law passed by the National Assembly in July 2002	Official copy of law on corporate accounts, their audit, and the accounting profession; and official copy of the official gazette announcing the adoption	Ministry of Economy and Finance has the capacity to enforce IAS and ISA.
	Ministry of Economy and Finance to adopt a subdecree to apply IAS and ISA to all companies (including insurance companies) incorporated in Cambodia, and to establish a national accounting council to set and interpret standards	Subdecree for the establishment of the National Accounting Council adopted in March 2003 and members of the Council appointed the same month	Official copy of the subdecree	Compliance costs for the private sector are manageable.
	Adoption of a law on commercial enterprises	Law on commercial enterprises enacted in May 2005	Copy of the law on commercial enterprises, and copy of the official gazette announcing the	Ministry of Economy and Finance is committed to the reform.

Design Summary	Performance Indicators/Targets	Results Achieved	Monitoring Mechanisms	Assumptions and Risks
	Ministry of Economy and Finance to establish an association of accountants and auditors including: (a) adopting a code of ethics that complies with the requirements of the International Federation of Accountants, and; (b) establishing committees on education and ethics within the association	Sub-decree to create the KICPAA adopted in March 2003. KICPAA and its by-laws formally established in February 2004	adoption Official copy of the articles of association for the association of accountants and auditors Official copy of code of ethics	
C. Subprogram III 1. Development of the Banking Subsector a. Develop banking subsector infrastructure	Adoption of a secured transactions law by the National Assembly Ministry of Commerce to establish a public registry for secured transactions NBC to form a unit and undertake the preparatory work needed to establish a financial intelligence unit responsible for anti-money laundering and combating the financing of terrorism	Secured Transactions law adopted in May 2007 Ministry of Commerce launched the on-line filing registry in September 2007 Precursor to the FIU was established in June 2005 with 6 staff members under the Bank Supervision Department	Official copy of the secured transactions law, and a copy of the Royal <i>Kram</i> promulgating the law Ministerial <i>prakas</i> to establish the public registry and confirmation by Ministry of Commerce of its commencement: (i) NBC confirmation that the precursor to the FIU is established, the mandate of the unit and staff terms of reference. (ii) Documentation for the FIU indicating: organization chart; staff terms of reference; budget allocation; procedures to capture and report on suspicious transactions and know your customer; training and public awareness programs	Ministry of Commerce is committed, committee number 9 of the National Assembly endorses the draft law, and the National Assembly has the required quorum to approve the law without delay NBC is committed to the reform

Design Summary	Performance Indicators/Targets	Results Achieved	Monitoring Mechanisms	Assumptions and Risks
b. Commercial law development and capacity building	Adoption of a law for commercial arbitration by the National Assembly	Adopted in March 2006	Official copy of the approved law on commercial arbitration and a copy of the Royal Kram promulgating the law	Ministry of Commerce is committed, Committee 9 of the National Assembly endorses the draft law, and the National Assembly has the required quorum to approve the law without delay
	Submission of an insolvency law to the National Assembly	Draft insolvency law submitted to the National Assembly in August 2007	Letter from the Ministry of Commerce confirming approval of the draft insolvency law by the Council of Ministers and submission to National Assembly, and a copy of the approved draft insolvency law with the accompanying letter from the Prime Minister or authorized person to the National Assembly	
	Ministry of Commerce to ensure dissemination of commercial laws via the Internet	Webpage established and all commercial laws uploaded in December 2005	Letter from Ministry of Commerce confirming the webpage address and list of commercial laws that have been uploaded	
	Ministry of Commerce to work with the relevant law institutes to develop commercial law curricula based on the new commercial laws for training judges, lawyers, and legal clerical staff	Curriculum for commercial law program adopted by the 3 selected legal faculties in May 2007	Copy of the approved commercial law curricula and confirmation from Ministry of Commerce that training programs have been adopted and are being implemented	
2. Development of the Insurance Subsector a. Strengthen capacity of the regulator	Ministry of Economy and Finance to review, update, and implement appropriate prudential regulations to enhance solvency, liquidity, and corporate governance requirements and support technical assistance (TA) to the insurance regulator	Prudential regulations formally approved by the senior Minister of Economy and Finance in March 2007	Progress reports of consultant(s), copies of prudential regulations and internal procedures approved by the Economy and Finance Minister and 6-monthly progress report from Ministry of Economy and Finance on their implementation	Ministry of Economy and Finance is committed to the reform

Design Summary	Performance Indicators/Targets	Results Achieved	Monitoring Mechanisms	Assumptions and Risks
b. Promote private sector involvement in the insurance sector	Ministry of Economy and Finance to implement the key actions of the plan to restructure Caminco, as agreed with ADB with a view to divest Government's shares at the earliest opportunity	Restructuring plan approved in August 2005 and implementation commenced in December 2005 Divestment of shares was not successful. Internal restructuring continues with the intention to grow market share and profitability	Copy of the approved restructuring plan and Ministry of Economy and Finance letter confirming its implementation and completion of key activities as follows: financial model to be approved by the Board and adopted; enhanced financial disclosure and reporting requirements to be approved by the Board and implemented; evaluation of existing staff finalized and approved by the Board; training needs assessment report; training program developed and being implemented; and annual business plan for 2006 approved by the Board	The Government is committed to the reform
3. Development of Interbank and Money Markets Legal framework for money market development	Adoption of a law on negotiable instruments and payment transactions by the National Assembly NBC to draft and adopt implementing regulations for the law on negotiable instruments and payment transactions	Law adopted by the National Assembly in September 2005 Three implementing regulations adopted in December 2006	Official copy of the approved law on negotiable instruments and payment transactions, and a copy of the Royal Kram promulgating the law Copy of the NBC <i>prakas</i> and/or regulations for implementing the law on negotiable instruments and payment transactions	NBC is committed, committee number 2 of the National Assembly endorses the law, and the National Assembly has the required quorum to approve the law without delay The Government is committed to the reform
4. Development of Accounting and Auditing Practices a. Capacity support to develop professional members for the KICPAA	Ministry of Economy and Finance to ensure financial support for at least 70 scholarships a year for the development of professional members of the KICPAA	Ministry of Economy and Finance continues to annually sponsor 70 scholarships with awardees selected on a competitive basis	(i) Confirmation letter from Ministry of Economy and Finance of the continuation of the annual budget allocation for 70 scholarships per year (2006 and 2007 fiscal years) to train local candidates to reach the KICPAA accreditation	Ministry of Economy and Finance is committed to the reform

Design Summary	Performance Indicators/Targets	Results Achieved	Monitoring Mechanisms	Assumptions and Risks
			<p>requirements</p> <p>(ii) selection criteria for scholarship candidates and administrative procedures for scholarship selection to be developed by the KICPAA in consultation with Ministry of Economy and Finance and adopted</p> <p>(iii) public announcements issued by KICPAA calling for nominees for the 70 scholarships in 2006 and 2007</p>	
<p>D. Technical Assistance Outcome</p> <p>Improve the capacity of the executing and implementing agencies to implement the policy reform activities under subprogram III</p>	<p>Enhance confidence in banking through an improved payment system, on-site supervision, and surveillance.</p> <p>Deter money-laundering activities.</p> <p>Enhance confidence in the insurance market and safeguard policyholders.</p> <p>Enhance understanding of the new commercial legislation and ensure timely application.</p>	<p>TA support has helped on-site supervision of selected banks, initial work in setting up the precursor to the FIU within NBC's banking supervision unit, public awareness workshops to explain the purpose and objectives of newly approved laws and the development of the implementing subdecrees</p>	<p>Published annual audited financial reports of banks</p> <p>Reports to the financial intelligence unit on suspicious transactions</p> <p>Consultants' reports</p> <p>ADB review missions</p> <p>Acceptance of the commercial law training modules by local legal institutions</p> <p>Number of reported commercial cases being successfully resolved</p>	<p>NBC is committed to the reform</p> <p>Ministry of Economy and Finance and Department of Financial Industry are committed to the reform</p> <p>Political will continue to approve key commercial legislations and enhance the judiciary functions to resolve commercial disputes</p>

Design Summary	Performance Indicators/Targets	Results Achieved	Monitoring Mechanisms	Assumptions and Risks
Outputs and Activities a. Supervision of banks and payment system b. Supervision and commercialization of the insurance subsector c. Application of commercial laws	Staff trained in the application of procedures for on-site supervision of banks	Completed in July 2006	Progress report from consultants	NBC is committed to the reform
	Public awareness, acceptance, and application of the approved law on negotiable instruments and payment transactions	Implemented in November 2006	Published bank reports Reports from NBC	
	Financial intelligence unit established	Completed in July 2006	ADB review missions	
	New and revised prudential regulations for insurance	Completed in May 2007	Progress reports from consultants	Ministry of Economy and Finance and Department of Financial Industry are committed to the reform
	Procedures for insurance supervision and training provided to the staff on their application	Completed in April 2007	Published reports of insurance companies	
	Restructured Caminco with part of the Government shares divested	Completed in April 2007	Reports from Ministry of Economy and Finance and Caminco	Ministry of Economy and Finance and Caminco are committed to the reform
	Training materials on commercial law courses acceptable to local legal faculties	Completed in May 2007	Report from Ministry of Commerce ADB review missions	Ministry of Commerce and the legal faculties are committed to implementing training
	Commercial disputes being resolved amicably	Work is still on-going. Draft subdecree with the Council of Ministers		

Design Summary	Performance Indicators/Targets	Results Achieved	Monitoring Mechanisms	Assumptions and Risks
Inputs	Advisory TA of \$0.5 million from ADB funds and \$0.15 million from the Government to implement key reform activities under subprogram III. The TA will provide 15.5 person-months of international and 14 person-months of domestic consulting services.		Signed TA letter Progress report from consultants ADB review missions Feedback from implementing agencies	Recruitment of qualified and experienced consultants is timely Implementing agencies take full ownership of the reform activities

ADB = Asian Development Bank, CAR = capital adequacy requirement, CBS = Center for Bank Studies, CISS = credit information sharing system, FTB = Foreign Trade Bank, GDP = gross domestic product, IAS = international accounting standards, ISA = international standards for auditing, KICPAA = Kampuchea Institute of Certified Public Accountants and Auditors, NBC = National Bank of Cambodia, NPL = nonperforming loan, M2 = a broad money supply measure, MFI = microfinance institutions, ROA = return on assets.

^a The program framework as approved by the Board of Directors in November 2001 and subprogram II, updated and approved by the Board of Directors in November 2002.

DETAILED POLICY MATRIX
LOAN 2185-CAM: SUBPROGRAM III OF THE FSPL I

Tranche Condition	Actions Taken	Supporting Documents Received
A.1. The National Assembly to adopt a secured transactions law	<p>The Ministry of Commerce submitted the draft Secured Transactions Law to the National Assembly in July 2005. JICA, in a letter dated 20 October 2006 to the chairman of Committee No. 2 of the National Assembly, expressed its concern with the draft law in relation to the draft civil code. The ADB Review Mission of November 2006 met with JICA to clarify its concerns and explain the need to have the draft law adopted by the National Assembly. JICA then reviewed the filing registry and expressed satisfaction with the system, the proposed fee structure and how it would cater to the requirements of the general populace. JICA then undertook to submit a letter to Committee No. 2 regarding these subsequent findings. Following the meeting with JICA, the mission met with the vice-chairman and other members of Committee No. 2 and explained the background to ADB's involvement in the Secured Transactions Law. JICA followed up with a series of letters to Committee No. 2 and the Ministry of Commerce proposing further discussion on the draft Secured Transactions Law and the draft civil code. The Ministry of Commerce received a letter from the National Assembly dated 16 January 2007 proposing a meeting between the Ministry of Commerce and JICA to address JICA's concerns. On 30 January 2007, the Senior Minister of Commerce met with JICA to discuss its concerns and explain the need to get the draft Secured Transactions Law adopted by the National Assembly as it would signal Cambodia's commitment to meeting an obligation to WTO. Following this meeting, Ministry of Commerce submitted an official letter to Committee No. 2 asking them to table the draft Secured Transactions Law at the plenary session of the National Assembly. The draft Secured Transactions Law was cleared by Committee No. 2 for discussion at a plenary session of the National Assembly on 21 March 2007. The Secured Transactions Law was finally adopted by the National Assembly on 5 April 2007 and endorsed by the Senate on 25 April 2007. The Royal Kram was issued on 24 May 2007.</p> <p>Completed: May 2007</p>	<p>Official copy of the secured transactions law, and a copy of the Royal Kram promulgating the law.</p>
A.2. Ministry of Commerce to establish a public registry for secured transactions	<p>All the required technologies have been procured and installed, including hardware, system software and application software. The domain name www.setfo.gov.kh has been registered at Ministry of Post and Telecommunication. Two filing office staff have been appointed and trained. Initial training of ACLEDA Bank staff who will be collecting filing fees has been held and user documentation prepared. Training of the major end users in Phnom Penh (primarily bank loan departments) has been done. Application software of Secured Transactions Filing Office system is being tested by a local IT consultant and by filing staff, and bugs that have been reported to the software development company will be fixed. The contract with the internet service provider came into effect on 1 October 2006. Online filing registry is ready for launching pending the issuance of the ministerial <i>prakas</i>. The other inter-ministerial <i>prakas</i> covering the fees for the filing registry was discussed with Ministry of Economy and Finance in early August 2007 and the <i>prakas</i> was formally issued in September 2007.</p> <p>Completed: September 2007</p>	<p>Ministerial <i>prakas</i> to establish the public registry and confirmation by Ministry of Commerce of its commencement.</p>

Tranche Condition	Actions Taken	Supporting Documents Received
<p>B.3. Ministry of Commerce to ensure dissemination of commercial laws via the internet</p> <p>B.4. Ministry of Commerce to work with the relevant law institutes to develop and adopt commercial law curricula based on the new commercial laws for training judges, lawyers, and legal clerical staff</p>	<p>The Ministry of Commerce has established a web site (www.cambodiacommerciallaws.com) and uploaded all the approved commercial laws. Completed: December 2005</p> <p>Ministry of Commerce has undertaken workshops and seminars in specific topical areas of commercial and financial law. Short-term and long-term public dissemination approaches are being pursued at the central as well as at the provincial levels. A series of intensive short-term workshops and seminars have been and will continue to be provided for those already engaged in commercial work. A team of trainers and lecturers has been touring provinces to offer training workshops. A compact disc containing training modules based on existing commercial laws has been developed. Three law institutes have been selected to develop a commercial law curriculum. The commercial law curriculum for a 4-year business degree program has been developed and formally adopted by each selected institute. The program will start in the next academic year (September 2007). Completed: May 2007</p>	<p>Letter from Ministry of Commerce confirming the webpage address and list of commercial laws that have been uploaded</p> <p>Copy of the approved commercial law curriculum and confirmation from Ministry of Commerce that training programs have been adopted and are being implemented</p>
<p>C.1. Ministry of Economy and Finance to review, update, and implement appropriate prudential regulations to enhance solvency, liquidity, and corporate governance requirements, and support technical assistance to the insurance regulator</p>	<p>Ministerial <i>prakas</i> on defining solvency for insurance companies issued in April 2005; Ministerial <i>prakas</i> on accounting guidelines for insurance companies issued in April 2005; Ministerial <i>prakas</i> on motor vehicle stickers under compulsory insurance issued in January 2006. Letter issued requesting all insurance companies to provide their monthly bank statements to Department of Financial Industry sent on 27 December 2005. Workshop to discuss the draft subdecree on life insurance and micro insurance with assistance from Nomura Research Institute held on 2 February 2006. International and national consultants began work early in May 2006. Draft prudential regulations covering solvency, liquidity and corporate governance have been prepared by the insurance supervision consultants pending approval by the Ministry of Economy and Finance for their issuance. The March 2007 mission discussed with Ministry of Economy and Finance the urgency of getting the draft regulations (<i>prakas</i>) approved by the Senior Minister of Economy and Finance and the <i>prakas</i> was subsequently approved on 21 March 2007. Copies of the approved <i>prakas</i> covering corporate governance, solvency and liquidity were provided to the ADB mission. Completed: April 2007</p>	<p>Progress reports of consultant(s), copies of prudential regulations and internal procedures approved by the Senior Minister of Ministry of Economy and Finance and 6-monthly progress report from Ministry of Economy and Finance on their implementation</p>
<p>D.1. Ministry of Economy and Finance to implement the key actions of the plan to restructure Caminco, as agreed with ADB with a view to divest the Government's shares at the earliest opportunity</p>	<p>A restructuring plan, developed with assistance under ADB TA was approved by the Board of Caminco and endorsed by the Senior Minister of Ministry of Economy and Finance in August 2005. Key activities began with ADB TA assistance, some of which were completed in December 2005. A financial model has been developed and tested and staff have been trained in its application. A three-member board committee was established in December 2005 and has been functioning throughout 2006. A 3-year business plan was developed and adopted by the Board of Caminco (December 2005). This included a training plan for 2006 and a marketing strategy and has been monitored closely by Management throughout</p>	<p>Copy of the approved restructuring plan and Ministry of Economy and Finance letter confirming its implementation and completion of key activities as follows: financial model to be</p>

Tranche Condition	Actions Taken	Supporting Documents Received
	<p>2006. Staff evaluation and training needs assessment have been finalized and a training coordinator appointed. Proposed improvements to the accounting policies and internal procedures to enhance financial disclosures of Caminco have been approved and implemented. An information memorandum was issued to three international insurance companies requesting their formal proposal by 7 February 2007. Two firms informed Caminco management that they were no longer interested in pursuing a due diligence. Prudential Insurance requested an extension by 1 month and has not made further contact since 7 March 2007. The Caminco Board assumed no further interest by Prudential Insurance and has decided to continue the internal restructuring of Caminco and to focus on building its market share before re-visiting the invitation to engage an international strategic partner.</p> <p>Completed: April 2007</p>	<p>approved by the Board and adopted; enhanced financial disclosure and reporting requirements to be approved by the Board and implemented; evaluation of existing staff finalized and approved by the Board; training needs assessment report; training program developed and being implemented; and 3-year business plan and budget for 2006 approved by the Board</p>
<p>E.1. The National Assembly to adopt a law on negotiable instruments and payment transactions</p> <p>E.2. National Bank of Cambodia to draft and adopt implementing regulations for the law on negotiable instruments and payment transactions</p>	<p>The draft law was submitted to the National Assembly with a letter from the Prime Minister dated 18 January 2005. The law was adopted by the National Assembly on 19 September 2005 and the Royal Kram issued on 24 October 2005.</p> <p>Completed: November 2005</p> <p>ADB provided technical support to help NBC disseminate the new law and implementing regulations. A series of public awareness workshops covering 150 participants from banks, NBC, academic institutions and government agencies were held in November 2006. With IMF TA, the NBC has drafted four regulations: (i) on the control of systemic risks, (ii) on the operation of settlement accounts, (iii) on payment clearing systems, and (iv) on licensing of money service businesses. The <i>prakas</i> covering the first three regulations were issued on 4 December 2006. NBC will require more time for consultation with affected stakeholders before issuing the fourth regulation.</p> <p>Completed: December 2006</p>	<p>Official copy of the approved law on negotiable instruments and payment transactions, and a copy of the Royal Kram promulgating the law</p> <p>Copy of the NBC <i>prakas</i> and/or regulations for implementing the law on negotiable instruments and payment transactions</p>
<p>F.1. Ministry of Economy and Finance to ensure financial support for at least 70 scholarships a year for the development of professional members for the KICPAA</p>	<p>A new intake (the sixth) for ACCA accreditation qualifications at CPA level has been selected and classes began in February 2006. 50 of the 70 participants were civil servants and the remaining 20 were from the private sector on full scholarships. New criteria and administrative procedures for competitive selection of scholarship candidates were formulated by NAC/KICPAA and approved by the Senior Minister of Economy and Finance in 2006. Allocations for 70 scholarships were included in the 2006 and 2007 Government budgets. A copy of the public announcements issued in 2005 for the 2006 intakes provided</p>	<p>(i) Confirmation letter from Ministry of Economy and Finance of the continuation of the annual budget allocation for 70 scholarships per year (2006 and 2007 fiscal</p>

Tranche Condition	Actions Taken	Supporting Documents Received
	to ADB. The draft public notice for the 35 students for the first semester of 2007 has been reviewed by the Mission and was published in December 2006. Completed: December 2006	years) to train local candidates to reach the KICPAA accreditation requirements (R), (ii) competitive selection criteria for scholarship candidates and administrative procedures for scholarship selection to be developed by the KICPAA/NAC in consultation with ADB and adopted by Ministry of Economy and Finance, (iii) public announcements issued by KICPAA/NAC calling for nominees for the 70 scholarships in 2006 and 2007
i. Ministry of Commerce to establish a mediation/arbitration centre for resolution of commercial disputes	Ministry of Economy and Finance has endorsed funding for the establishment of the center but requires the Ministry of Commerce to identify a suitable piece of land for the new building for the centre. A draft subdecree containing the roles, functions and power of the center is being developed by Ministry of Commerce with assistance from the international consultant under ADB TA. It is expected to be tabled at the Council of Ministers in October 2007. Expected completion date: November 2007	Subdecree to establish the arbitration center and confirmation by Ministry of Commerce of its commencement.
ii. The National Assembly to adopt the law on government securities	The draft law has been reviewed by the Council of Ministers and was approved on 16 June 2006. It was adopted by the National Assembly in November 2006 and the Royal Kram issued in January 2007. Completed: January 2007	Official copy of the approved law on government securities, and a letter from Ministry of Economy and Finance confirming its adoption by the National Assembly

ACCA = Association of Chartered Certified Accountants, ADB = Asian Development Bank, CPA = certified public accountant, FIU = financial intelligence unit, IMF = International Monetary Fund, IT = information technology, JICA = Japan International Cooperation Agency, KICPAA = Kampuchea Institute of Certified Public Accountants and Auditors, NAC = National Arbitration Center, NBC = National Bank of Cambodia, PMLFT = prevention of money laundering and financing of terrorism, (R) = documents provided to ADB Mission, TA = technical assistance, WTO = World Trade Organization.