Foreword of the Governor

The year 2009 has ended with an improved sentiment among policymakers and market participants over the prospects of the global economy and financial markets. The deep concerns and uncertainty caused by the turmoil in international financial markets in mid-2007, and which had major repercussions on economic activity worldwide during 2008 and in the first few months of 2009, seems to have abated. After a deep recession, global economic growth has turned positive. Decisive and wide-ranging public interventions in key advanced economies have allayed concerns about a systemic financial collapse and a global depression, while stimulative macroeconomic policies have shored up domestic demand across many other economies. Emerging and developing countries, notably in Asia, are recovering earlier than advanced economies. According to the IMF’s latest report on the global economy, global activity is forecast to expand by about 3 percent in 2010, after contracting by about 1 percent in 2009. Advanced economies are projected to expand sluggishly through much of 2010. Average annual growth in 2010 will be only modestly positive at about 1.2 percent, following a contraction of 3.5 percent during 2009. The emerging and developing economies’ real GDP growth is forecast to reach 5 percent in 2010, up from 1.7 percent in 2009. The rebound is driven by China, India, and a number of other emerging Asian countries. Economies in the ASEAN region are also expected to post solid growth of close to 4 percent in 2010, which will be helped by recovering commodity prices.

As far as our own economic situation is concerned, the global financial crisis and economic contraction has taken a heavy toll on the remarkable gains Cambodia made in recent years—achieving stable and robust economic growth, reducing fiscal and external current account deficits, and lowering unemployment and poverty, as its economy is highly dependent on a sustained international trade expansion and foreign capital inflow. Three of the four main drivers of growth—exports, tourism, and construction—have registered contractions while agriculture remains on a firm footing. The current global economic crisis has indeed led to a sharp fall in exports, while the capital and investment flow was reduced heavily, which has in its turn adversely affected the investment decisions by the domestic private sector, as the private sector continued to adjust to slack external demand and weak conditions in the property market. The IMF’s GDP projection indicated that the Cambodian economy may contract by 2.7 percent in 2009, with a modest bounce back in 2010 to a positive 4.2 percent.

With a prompt evaluation of the situation, the Cambodian Government initiated a rapid response and adjusted the orientation of the macroeconomic policy. On the fiscal front,
to help foster economic activities and sustain growth under the shadow of the global financial crisis and recession, the Government has acted counter-cyclically to prop up domestic demand, by introducing fiscal stimulus and expenditure rationalization with priority spending focusing toward improving social safety nets and providing alternative employment for vulnerable population segments, including those losing jobs in the affected export sectors. Priorities were also given to public investment in physical infrastructure and supporting growth in the agricultural sector.

With regard to the monetary and banking sector, the NBC has tried to adjust its monetary policy in a flexible manner in order to deal with inflationary developments and to address liquidity constraints in the system. The monetary policies were promptly modified from an appropriately tight monetary policy during the period that the economy was hit by the impact of rising global food and fuel prices in 2007-2008 to a moderately easy monetary policy in early 2009, in order to ensure that some liquidity strains in the economy did not escalate into systemic pressures, while the NBC’s role as the lender of last resort has been further enhanced. In the meantime, inflation has come down rapidly since the middle of this year and stayed at 5.3 percent until the end of the year. Furthermore, we remain committed to a floating exchange rate regime by letting exchange rates adjust to external realities while maintaining a comfortable level of the international foreign reserves. It is worthwhile to recall that during the episode of strong growth and capital inflow in 2007 and the first half of 2008, the exchange rate of the local currency was strong. However, the currency depreciated by about 1.8 percent year-on-year to the USD in 2009 following pressure from the global financial crisis as foreign investors pulled out the needed cash to meet their obligations abroad. The gross international reserves continued to increase, albeit at slower pace than a year ago, to reach 2,367.3 USD million at the year-end, a level that is sufficient to cover about 4 months of imports.

As far as the monetary and banking sector is concerned, the performance of the banking sector has been satisfactory, though challenging. Following an episode of stress, total banking system liquidity is gradually improving. The broad money supply (M2) has recovered to 36.8 percent year-on-year in December 2009, from a negative growth at the beginning of the year, reflecting the increase in customers’ deposits, with an annual growth rate of 38.3 percent in December 2009. Credit to the private sector remained low, mirroring banks’ prudent credit policy in the period of weak economic activity.

To maintain financial stability, the NBC has also closely monitored the banking sector. It has further tightened and enhanced its banking supervision and paid particular
attention to the banks’ solvency and liquidity conditions. Safeguarding the stability of the banking system, which is still in the early stages of development compared to many other economies, remains a priority of the NBC. The central bank has been very active in recent years in taking steps to improve banking supervision; recent efforts have included a focus on strengthening loan classification standards, improving bank licensing procedures and the formulation of bank resolution plans for troubled banks, should they be needed. The recent crisis has also prompted reform in the legal framework, in particular to provide for a better framework for sound banking operations and an effective exit policy. Thus, an amendment of the existing banking law has been prepared and submitted to the Council of Ministers for review. To promote a money and interbank market, the NBC has securitized the fixed certificate of deposits held by banks and issued a regulation supporting repo operations. Going forward, the NBC will consider any regulatory and supervisory measures aimed at strengthening risk management practices and policies at the banks to strengthen enabling institutions to better anticipate, manage and ultimately withstand adverse economic conditions and market trends.

During the year, NBC also continued to actively support the expansion of microfinance services. This was done, among other ways, through facilitating MFIs’ access to voluntary deposits from the general public, enhancing the provision of credit to MFIs from domestic commercial banks, providing necessary support for MFIs’ capacity building and the inclusion of MFIs in the Credit Information Sharing System.

Another project which should help banks in Cambodia play a more active role in the economy is the development of the National Payments System, which will serve as a channel of inter-sector, inter-industry and inter-company financial resource flows, thus promoting economic growth. With the support from private stakeholders and development partners, the NBC has made efforts to introduce institutional arrangements, operational mechanisms, inter-related IT infrastructure.

Within the NBC itself, organizational development and improvement is ongoing. Among the ongoing activities is the effort to provide better central banks’ services through strengthening our branch network. So far the work to revive and strengthen our branches has proceeded smoothly and effectively as planned. The NBC’s internal audit and risk management capacity has also been steadily enhanced. Following a series of actions to build an institutional framework and develop rules and procedures to guide internal auditing activities, the audit process has been started in various areas, with satisfactory results so far.
Various other measures have been also implemented in order to provide better and more efficient central bank services to banks and the Government; these include an improvement in the quality and in the supply and distribution of banknotes in circulation, a more efficient organization and development of the information system to support central bank operations, and active participation in the implementation of the second phase of the Public Financial Management Reform agenda of the Government.

Besides this, actions to develop the skills of NBC staff were accelerated, with the help of external technical assistance. A special effort has been made with respect to banking supervision, which we would like to serve as a benchmark for other activities.

Before concluding, I would like to stress an important lesson from the recent global crisis. While Cambodian banks have been spared the full impact of the financial crisis, in the years ahead they will be operating in an environment that is likely to have changed as a result of the dynamic domestic banking sector, the development in the domestic financial market, and the ongoing international economic integration and financial globalization. There are thus major tasks ahead of us, including revitalizing the growth potential that was damaged by the crisis, generating sustainable and balanced growth and promoting a sound, adaptable and innovative banking system. The NBC needs to strengthen itself to be able to play a vital role in contributing to sustainable economic and achieving financial stability.

As Governor of the NBC, I would like to thank the Royal Government of Cambodia and all partners with the Government for their support and collaboration, to thank development partners for their friendship and assistance to the NBC, and to thank all NBC officials and staff for their dedication and hard work. Building a healthy banking system that functions effectively through financial intermediation, obtains confidence from the public and contributes actively to economic development is a great challenge. It requires more effort and strong will and patience from all stakeholders. NBC truly hopes that all the relevant parties will continue to actively support it in the efforts to promote and strengthen Cambodia’s banking system.

Governor
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Introduction

For over a year, the global environment has changed significantly. Last year, the challenge of the Royal Government of Cambodia and the NBC was to strike the right balance between containing inflation and promoting economic growth in light of inflationary pressure arising from high and volatile international commodity and oil prices. This time, the authorities face greater challenges, namely those arising from a volatile financial and economic environment, and thus requiring more sophisticated and unconventional policy responses.

It is now evident that we are not immune to the ongoing global financial and economic crisis, which has repercussions on a small, open economy like Cambodia that is highly integrated with the world economy through trade and capital inflows. Despite the fact that there has been generally no damage to the household balance sheets, the macroeconomic conditions remain fragile. Cambodia’s dependence on external capital inflows and exports (particularly garments), which have shown declines since the last quarter of 2008 as a result of the world financial crisis, is a matter of continuous concern. Revenue from international visits was down slightly. Garment exports declined by 23.4 percent in 2009 compared to 2008. Net foreign direct investment fell by 35.2 percent.

Facing such a situation, fiscal stimulus packages and expansionary monetary policies were introduced with a commitment to limiting the impact of the crisis as much as possible. Yet, downside risks on growth remain significant, which requires coordinated efforts among all institutions and more efficient utilization of resources.

These circumstances also present challenges for the domestic banking system, and in addressing them it is important to recognize the implications for the economy at large. Safeguarding the stability of the banking system, which is still in the early stages of development compared to many other ASEAN economies, remains a priority of the National Bank of Cambodia. The central bank has been very active in recent years in taking steps to improve banking supervision. Recent efforts have included a focus on strengthening loan classification standards, improving bank licensing procedures and the formulation of bank resolution plans for troubled banks, should they be needed. While there have been some liquidity strains in the economy, the NBC has taken steps to ensure that these do not escalate into systemic pressures. The central bank continues to take a conservative approach to monetary management, which will allow Cambodia to weather the present global financial crisis.
I. Macroeconomic Developments

1. Prices and Exchange Rate Movements

1.1. Retail Prices and Inflation

After having increased significantly in the first half of 2008 and having reached a peak in May, inflation in Cambodia, as measured by the consumer price index, showed a steep decline in the following months of the year. This declining trend continued into 2009 when the year-on-year inflation rate turned negative for the first time in March. The disinflation sustained until nearly the end of 2009. The reversal in the inflation trend was brought about by the sharp deceleration in global economic activity, while commodity prices turned down, sharply so in the case of oil. In addition, as the global financial meltdown adversely affected capital flows into Cambodia and the country’s real estate market, local demand pressure also eased. The base year effect of the past swings in the consumer prices was also an important factor for the drop in the year-on-year inflation rate.

Chart 1: CPI All Items
( Index: 2006 = 100 )
Nevertheless, as the financial turmoil began to calm, global economic conditions improved, and the medium-term prospect for the world economy began to appear favorable, oil prices in the international market started to pick up gradually again from the beginning of 2009, although by year’s end were still well below the highs reached during mid-2008. Local oil prices have followed the trend abroad. As a result of a pass-through of high international energy costs to consumers’ charges combined with the weak US dollar, the inflation rates turned positive in annual terms in November and December.

**Chart 2: Year-on-Year Change of CPI All Items**

As shown in Chart 2, the negative inflation rates moved continuously upward in the second half of 2009, when the year-on-year inflation rose from a low of -5.7 percent in May 2009 to a positive rate of 5.3 percent in December 2009. By comparison, the rate of the year-on-year inflation in December 2008 and 2007 was 12.5 percent and 14.0 percent, respectively.

The twelve-month moving average rate of inflation was negative at 0.7 percent as of the end of the review year.

Sectoral analysis of the Consumer Price Indices indicated that the inflationary pressure was pronounced in a number of subgroups, such as Transport, Miscellaneous Goods...
& Services, and Alcohol Beverages & Tobacco, and which posted an increase of 11.9 percent, 11.3 percent, and 10.3 percent, respectively, in December 2009 compared to the same period of last year. This was followed by changes in the subgroups of Education (8.9 percent), Health (5.8 percent), and Furnishings & Household Operations (4.8 percent). Change in subgroup of Restaurants & Hotels ranked eighth with a rate of 3.8 percent, a substantial decline against the change a year ago. Meanwhile, changes in the subgroups of Clothing & Footwear and Housing, Water & Electricity were also moderate compared to last year’s increase, both up by 2.6 percent and 2 percent, respectively.

The Food & Non-alcoholic beverages index, which accounts for 44.8 percent of the overall CPI basket, increased by 5.4 percent in December 2009, with major food categories, such as cereals, poultry, meat, fish, fruits and vegetables, registering significant price increases. The rise in the Transport subgroup, on the other hand, reflected the increases in the prices of gasoline, diesel, motor oil, as well as transportation costs. Local premium gasoline pump prices accelerated from 2,930 KHR per liter in December 2008 to reach a new high at the end of 2009 of 4,000 KHR per liter (a nearly 33 percent increase).

The remaining two subgroups among the twelve total groups shaping the consumer basket in the country, Communication, and Recreation & Culture, registered declines of -6.9 percent, and -1.5 percent, respectively.

Analysis of the movement of other measurement of inflation indicates that the path followed by the inflation excluding food mirrored that of the overall changes in the CPI. Non-food inflation slowed down rapidly in the second half of 2008, after hitting the highest rate in May at 21.9 percent. It eased further throughout 2009 and turned negative in March to October, before regaining momentum in the last two months of the year. By the end of December, the year-on-year non-food inflation returned to 5.2 percent, compared with the 6.7 percent posted for the same period of the previous year, and against the annual overall inflation rate of 5.3 percent. This suggested that the prices of the non-food items were the major causes of the recent high of inflation.

At the same time, inflation excluding transport posted an annual rate of 6 percent, while non-food and non-transport inflation was just 6.8 percent at end of December 2009. This again implies that the prices of fuel and transport are also an important source of inflation.
Statistics on the contributions of the respective subgroups to the year-on-year change in the CPI showed that domestic food items contributed 2.4 percentage points, about 45 percent of the total inflation for the month. Transport items contributed around 1.5 percentage points, accounting for 27 percent of the total observed price increases. The contributions of other major subgroups, such as Restaurants & Hotels, Housing, Water & Electricity, Health, Clothing & Footwear, Furnishings & Household Operations, and Education, were positive, but relatively small, whereas Communication subgroups showed a negative contribution.

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<th>Sep-09</th>
<th>Dec-09</th>
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<tr>
<td>Food</td>
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<td>Others</td>
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<td>1.0</td>
<td>1.1</td>
<td>0.8</td>
</tr>
<tr>
<td>CPI</td>
<td>12.3</td>
<td>-0.5</td>
<td>-4.7</td>
<td>-2.3</td>
<td>5.3</td>
</tr>
</tbody>
</table>
1.2. Exchange Rate Movements

1.2.1. The Exchange Rate of KHR Against the US Dollar

Considering the bilateral average exchange rate of the Cambodian riel relative to the US dollar, which is the simple average of the daily exchange rate over the period under review, the local currency weakened somewhat against the US dollar during the year. The annual average exchange rate for 2009 was recorded at KHR 4,154 per US dollar, compared to KHR 4,065 to USD 1.00 for 2008, an annual change of about KHR 90 or 2.2 percent.

There were large fluctuations in the movements of the daily exchange rates over the course of the year under review, with the low-end and the high-end rate posting at KHR 4,107 and KHR 4,250 against the US dollar for a difference of KHR 143. As shown in the chart below, the local currency experienced remarkable stability during the first fourth months of the year under consideration, moving within a narrow range around the rate of KHR 4,118 per US dollar, the average rate of this four-month period. However, partly due to seasonal influences, the local currency weakened from mid-May up until late October, where it averaged KHR 4,183 per US dollar. Going into the later period of the year, the increased demand for the national currency during the harvest season drove up the value of the riel,
when the average rate for the last two months of the year slowed down to KHR 4,172 to a US dollar.

The KHR closed the year at 4,181. This was a depreciation of 1.8 percent on the end-period exchange rate for 2008, compared with to a depreciation of 2.7 percent recorded in the previous year. The drop in the value of the KHR in 2009 was a result of a pressure from the global financial crisis as foreign investors pulled out the needed cash to meet their obligations abroad. The weakness in the current account of the BOP and the increase in the Government’s spending in local currency associated with the stimulus package may also have contributed.

### Chart 5: Trend of Riel Exchange Rate Against US Dollar

![Chart 5: Trend of Riel Exchange Rate Against US Dollar](image)

1.2.2. The Exchange Rate of KHR Against Currencies other than the US Dollar

In terms of a number of currencies of Cambodia’s major trading partners, the respective cross rate of those units against the local unit, the KHR, as measured through the US dollar, showed a very large fluctuation within a range of +30 and -3 percentage points around the base (end December 2008 - see chart below). In the early period of the year, when the dollar generally strengthened against various international currencies, the riel also posted some gains vis-à-vis a number of currencies under review, such as the Thai baht, the
Japanese yen, the Euro, and the Singapore dollar. However, during the last six months of the reporting year the local currency lost ground, possibly owing to the weakness of the US dollar. Among foreign currencies under consideration, the following units appreciated against the Cambodian riel compared to the base period: Australian dollar, 32.7 percent; Indonesian rupiah, 19.8 percent; Korean won, 18.6 percent; Thai baht, 6.8 percent; Philippines peso and Singapore dollar, each 4.3 percent; Malaysian ringgit, 4 percent; and the Euro and the Chinese yuan, 3.7 percent and 2.2 percent, respectively. Meanwhile, the end-period cross-rates of the Vietnamese dong weakened vis-à-vis the local unit, with a depreciation of 3.4 percent on its value a year ago. Over the same period, the Japanese yen remained broadly stable against the riel.

In general, the riel/US dollar rate broadly followed the pattern set by the US dollar rate vis-à-vis several major currencies. A more stable macroeconomic outlook and improved sentiment in many Asian and Euro area financial markets were factors boosting the currency of those economies against the US dollar. Thus, over the review period, the US dollar tended to weaken, especially toward the end of the year.

**Chart 6: Currencies Against Cambodian Riel**

*Index: End-December 2008 = 100*
2. Monetary Development

The monetary policy of the NBC aimed at maintaining price stability through conducting a managed floating exchange rate regime, accumulating more international reserves and strengthening the confidence of the public.

During 2009, the unfavorable international economic environment resulting from the recent global financial crisis continued to cast its shadow on Cambodia’s economy, especially on its real estate sector, construction, garment exports and tourism. The slowdown of these sectors, combined with the decline in capital inflow, had in turn an indirect impact on monetary development and banking system operations. During the year, the NBC reduced the reserve requirement ratio for foreign currency deposits from 16 percent to 12 percent, with the objective of increasing banks’ ability to provide more loans to the private sector to support the economic recovery.

Cambodia’s financial system maintained stability and modest growth in the face of the recent financial turmoil. Banking intermediation continued without interruption, though at a slower pace than what had been observed before the crisis. Statistical records show that
broad money (M2) picked up at a faster rate than last year, mainly due to the increase in residents’ foreign currency deposits with the local banking system.

Chart 8: Monetary Survey

2.1. Monetary Aggregates

In 2009, M2 increased by KHR 4,369.4 billion (36.8 percent) from the stock position of KHR 11,858.9 billion at the end of December 2008 to KHR 16,228.3 billion at the end of December 2009. The increase in M2 resulted mainly from the increase in residents’ foreign currency deposits of KHR 3,474.8 billion (37.5 percent) coupled with the expansion of currency outside banks of KHR 706.8 billion (30.8 percent), and time and savings deposits of KHR 173.9 billion (94.1 percent), while demand deposits increased by only KHR 13.8 billion (13.2 percent). The expansion in foreign currency deposits reflected the increase of term deposits of KHR 2,399.5 billion (61.4 percent), savings deposits of KHR 786.9 billion (22.7 percent), and demand deposits of KHR 251.2 billion (10.2 percent). It should be noted that foreign currency deposits rose continuously almost every month during 2009, except for a slight decline in February.

On the whole, this year’s monetary development reflected the improvement in investors’ confidence in Cambodia’s government policies following an episode of tranquility,
the soundness of the banking system, and a positive economic outlook when few new banks entered the market and contributed to the growth of the local banking sector.

**Chart 9: Structure of Money Supply**

![Chart 9: Structure of Money Supply](image)

**Table 2: Liquidity Components & Inflation**

*(Year-on-Year Percentage Change)*

<table>
<thead>
<tr>
<th></th>
<th>2004</th>
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<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
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<tr>
<td>Net claims on government</td>
<td>-63.1</td>
<td>-101.8</td>
<td>-126.4</td>
<td>-90.5</td>
<td>-64.5</td>
<td>24.6</td>
</tr>
<tr>
<td>Credit of private sector</td>
<td>35.9</td>
<td>31.8</td>
<td>51.6</td>
<td>76.0</td>
<td>55.0</td>
<td>6.5</td>
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<tr>
<td>Liquidity (M2)</td>
<td>30.0</td>
<td>16.1</td>
<td>38.2</td>
<td>62.9</td>
<td>4.8</td>
<td>36.8</td>
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<td>Currency outside banks</td>
<td>22.7</td>
<td>15.0</td>
<td>24.8</td>
<td>24.4</td>
<td>15.3</td>
<td>30.8</td>
</tr>
<tr>
<td>Inflation rate</td>
<td>5.3</td>
<td>8.4</td>
<td>4.2</td>
<td>14.0</td>
<td>12.5</td>
<td>5.3</td>
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**2.2. Factors Affecting Money Supply**

In the year under consideration, money supply M2 grew at a faster pace than the previous year’s increase of 4.8 percent. This improvement reflected a significant increase in net foreign assets, while net domestic assets of the banking system increased slightly.
Net foreign assets rose by KHR 4,309.5 billion (41.7 percent), whereas domestic assets only up by KHR 59.9 billion (4.0 percent). The increase in net domestic assets was due to a significant increase in net claims on government and credit to the private sector of KHR 735.3 billion (24.6 percent) and KHR 638.0 billion (6.4 percent), respectively. When, capital and reserves of the banking system increased by KHR 1,482.1 billion (25.7 percent).

Of the total credit at end-December 2009, Wholesale and Retail Trade accounted for 31 percent; Hotels & Restaurants, 12 percent; Construction and Manufacturing, each 9; Personal Lending, 8 percent; Agriculture, 7 percent; and Real Estate Activities, 6 percent. The “Others” category, which consists of Transport, Telecom, Utilities, etc., accounted for 19 percent.

2.2.1. Financial Operations of NBC

In 2009, the net domestic assets of NBC increased by KHR 155.7 billion (3.3 percent), from KHR -4,676.2 billion in December 2008 to KHR -4,520.5 billion in December 2009, after having declined KHR 1,115.5 billion (31.3 percent) in December 2008. The raise in domestic assets was mainly due to the growth in net claims on government of KHR 720.2 billion (26.7 percent), while other items net and net claim on banks decline of KHR 462.2 billion riel (25.8 percent) and KHR 102.1 billion (52.5 percent), respectively. The increase in net claims on government resulted entirely from the decrease in government deposits of KHR 720.0 billion (24.3 percent).

At the same time, the net foreign assets of NBC recorded a significant increase of KHR 2,485.7 billion (23.1 percent). This growth was due to the increase in foreign assets of KHR 2,933.4 billion (27.2 percent), while the foreign liabilities of NBC expanded KHR 447.7 billion (100%), reflecting the IMF’s SDR allocation for the member countries with the aim to support the rebuilding of the global economy. It should be noted that the price of gold (which is a component of foreign assets) continued to increase at an accelerated level.

2.2.2. Financial Operations of Deposit Money Banks

In 2009, the total assets of deposit money banks grew by KHR 4,035.5 billion (23.3 percent), while domestic liabilities in terms of local deposits increased by KHR 3,657.9 billion (38.4 percent). The rapid recovery in customers’ deposits after a sharp slowdown in the recent past is expected to be the primary factor supporting banks’ credit activities and contributing to growth in the economy and investment.
Net domestic assets declined by KHR 228.9 billion (3.8 percent) in 2009. This decrease mainly mirrored the decreases of KHR 922.2 billion (25.6 percent) in other items net, while credit to the private sector and net claims on government increased by KHR 638.5 billion (6.5 percent) and KHR 15.4 billion (5.3 percent), respectively. At the same time, total banks’ reserves placed with NBC increased by KHR 2,063.1 billion (51.5%). The decrease in other items net reflected the increase in the net worth of the banking sector, which was largely the result of injection of additional capital by one new bank and the recapitalization of an existing bank.

Residents’ foreign currency deposits, a key component of banks’ domestic liabilities, went up by KHR 3,474.8 billion (37.5 percent), whereas term & savings deposits and demand deposits rose by KHR 173.9 billion (94.1 percent) and KHR 9.1 billion (11.8 percent), respectively.

Net foreign assets of deposit money banks increased by KHR 1,823.8 billion (423.6 percent), from KHR -430.6 billion in December 2008 to KHR 1,393.2 billion in December 2009. This increase resulted from the increase of KHR 694.2 billion (32.9 percent) in foreign assets combined with the decline of KHR 1,129.6 billion (44.5 percent) in foreign liabilities.

2.3. Interest Rates Movements

The global economy has shown signs of a gradual recovery after having contracted last year and in early 2009. Against the backdrop of severe and uncertain financial and economic conditions that prevailed at that time, many countries took actions to tighten monetary policy, while some even stepped up their use of non-standard monetary policy measures designed to enhance liquidity and support the extension of credit by banks, and thus restore their economy from the setbacks impacts of the global financial crisis, by frequently reducing official interest rates to levels closer to zero.

Although the global economic environment has been improving and the world economy is growing again at some degree, until now various central banks have remained reluctant to implement an exit strategy. In many economies, especially in the United States, the policy rates have been kept near zero. Such specific decisions were made on account of the downside risk to the outlook, the fear of an overreaction, as well as because of the view that inflationary pressure has posed less of a threat at this present time. Nevertheless, a few countries, namely Australia and Norway, recently had the courage to move ahead with the
exit strategy by resolving to implement tight monetary policy measures, raising their policy rates in response to the changing environment in their individual economies.

In the context of Cambodia, following an episode of policy tightening, and amid the weak prospects for economic growth, the NBC introduced an accommodative monetary policy in early 2009 by reducing the reserve requirement ratio on foreign currency deposit from 16 percent to 12 percent. This action aimed to encourage banks and financial institutions to lower the costs of borrowing for their customers.

However, until recently, the policy actions did not seem to have yielded the desired economic outcomes, i.e., the expansionary monetary policy did not lead to a decline in domestic lending rates during the survey period. This trend could be observed not only in Cambodia, but also in various part of the world. In fact, interest rates on loans have remained relatively high, and have even picked up in some countries, while the lending activities of banks and financial institutions did not resume at desirable pace.

In Cambodia, the impact of the recent policies was mixed, with deposit rates falling and lending rates rising.

The weighted average interest rates on 6-month deposits for both KHR and US dollar deposits showed a continuous decline. Statistical records show that interest rates on deposits in KHR and US dollars fell from 6.46 percent and 5.48 percent in December 2008 to 5.23 percent and 4.45 percent in December 2009, respectively. This development was explained by an unexpected acceleration in liquidity of the banking system, which reflected a remarkable growth of public deposits since the second half of 2009.

During the same period under consideration, the weighted average lending rates for loans with a maturity of 6 months generally increased during the beginning of the year, but fell to some extent going into the end of the survey period. The lending rates on KHR and US dollar loans rose from 18.77 percent and 16.3 percent in December 2008 to 21.96 percent and 17.15 percent in December 2009, respectively. The yearly average interest rate on local currency loans stood at 22.08 percent, while that on US dollar loans was 17.21 percent. The increase in lending rates could be a result of banks strengthening their lending standard as they have given greater focus on credit risks, when economic activity has weekend and growth prospect remains uncertain.
Over the reviewed year, banks’ interest rate spreads on the KHR portfolio increased from 12.31 percent to 16.65 percent, while interest rate spreads on the US dollar portfolio declined from 10.82 percent to 12.60 percent.

### Table 3: Weighted Average Interest Rates on Loans and Deposits

*(6-month maturity)*

<table>
<thead>
<tr>
<th>KHR</th>
<th>Dec-08</th>
<th>Feb-09</th>
<th>Apr-09</th>
<th>Jun-09</th>
<th>Aug-09</th>
<th>Oct-09</th>
<th>Dec-09</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deposits</td>
<td>6.46</td>
<td>6.44</td>
<td>6.44</td>
<td>6.22</td>
<td>5.60</td>
<td>5.37</td>
<td>5.23</td>
</tr>
<tr>
<td>Loans</td>
<td>18.77</td>
<td>20.02</td>
<td>22.68</td>
<td>22.68</td>
<td>22.67</td>
<td>22.21</td>
<td>21.96</td>
</tr>
<tr>
<td>Spread</td>
<td>12.31</td>
<td>13.58</td>
<td>16.24</td>
<td>16.46</td>
<td>17.07</td>
<td>16.84</td>
<td>16.84</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>USD</th>
<th>Dec-08</th>
<th>Feb-09</th>
<th>Apr-09</th>
<th>Jun-09</th>
<th>Aug-09</th>
<th>Oct-09</th>
<th>Dec-09</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deposits</td>
<td>5.48</td>
<td>5.59</td>
<td>5.57</td>
<td>5.42</td>
<td>5.14</td>
<td>4.82</td>
<td>4.45</td>
</tr>
<tr>
<td>Loans</td>
<td>16.30</td>
<td>17.29</td>
<td>17.21</td>
<td>17.22</td>
<td>17.28</td>
<td>17.13</td>
<td>17.15</td>
</tr>
<tr>
<td>Spread</td>
<td>10.82</td>
<td>11.7</td>
<td>11.64</td>
<td>11.8</td>
<td>12.14</td>
<td>12.31</td>
<td>12.70</td>
</tr>
</tbody>
</table>

### 3. Balance of Payments

The preliminary estimates of Cambodia’s balance of payments transactions for 2009 posted a surplus on the overall balance of USD 70.2 million, a decline of 79.7 percent compared with 2008. The decline in the surplus on the overall balance was mainly attributable to a marked contraction of USD 556.4 million (or 47.8 percent) in the surplus on the financial account balance, while the deficit in the current account balance (excluding official transfers) fell only by USD 209.2 million (or 16.6 percent) and the capital account improved by USD 81 million (or 17 percent). In 2009, the current account balance to GDP ratio was 9.6 percent.

#### 3.1. Current Account (Excluding Official Transfers)

In 2009, the current account balance exhibited a deficit of USD 1,050.6 million, a decrease of 16.6 percent compared with 2008. The main reasons for this swing were the large contraction in the merchandise trade deficit (14.4 percent) and the fall in net private
inward transfers (25.6 percent). In addition, net outflows on the income account declined slightly (7.9 percent), while a small surplus was registered on services (1.8 percent).

Chart 10: Balance of Trade
(1998-2009)

On the basis of Customs data and NBC’s estimates, the merchandise trade gap narrowed to USD 1,541 million in 2009, down by 14.4 percent after having widened by 30 percent in the previous year. While both exports and imports contracted, the latter fell more markedly over the year. This contrasts sharply with the rapid growth in both components recorded in 2008.

Domestic exports amounted to USD 3,619 million, a decrease of USD 804.7 million (or 18.2 percent) compared to the previous year’s exports. The declines of USD 716.2 million in garment and textile exports and USD 88.4 million in other domestic exports were the main factors contributing to the unfavorable export performance in the year under consideration. In 2009, the United States of America, European Union and Canada, which are the main importing countries of Cambodia’s garment and textile products, were facing the global economic crisis. As a result, Cambodia’s garment and textile exports to those countries decreased 23.8 percent compared to the previous year’s exports. During the same period, other domestic exports, especially the exports of agricultural products, decreased 6.2
percent. The decrease in the prices of rubber, fish, paddy rice and other agricultural products were the contributors to the decrease in the exports of other domestic exports.

In 2009, the estimate of retained imports was USD 5,208.2 million, a decrease of USD 1,063.2 million (or 17 percent) compared to the estimate of retained imports for 2008. All the main import categories registered declines. Of this overall contraction, imports of garment materials and other inputs for the textile manufacture fell by USD 321 million (22.9 percent), followed by a shrink in import of transport equipment of USD 217 million (53 percent). Meanwhile, purchase of petroleum products dropped by USD 165 million (8.5 percent). The remaining imports together recorded a decrease of USD 579 million (19.7 percent).

Meanwhile, the net services was a surplus of USD 611.1 million, an increase of USD 11 million (or 1.8 percent) on the previous year’s surplus. The increase was due to a decrease of USD 54.9 million (or 5.2 percent) in payments on services to non-residents, while services receipts decreased USD 43.9 million (or 2.7 percent). The travel services receipts amounted to USD 1,211.4 million, a decrease of 1 percent compared to the previous year’s estimate. Due to the strong commitments of the Government of Cambodia to accelerate the reform agenda pertinent to the country’s tourism sector in light of the recent global economic crisis (such as implementing additional infrastructure projects, improving legal framework and institutional capacity, diversifying tourism markets as well as conducting active tourism promotion activities), the number of tourists visiting Cambodia was estimated at 2.2 million, up by 3.8 percent compared to tourist arrivals of 2,125,465 in 2008. The number of tourists from some countries such as Laos, Switzerland, and Vietnam increased significantly. During the same period, the number of tourist arrivals from Korea and Japan (which dominated arrivals in 2008) declined. The number of tourist arrivals that accounted for the biggest share of the total number of tourist arrivals in Cambodia in 2009 was Vietnam (14.2 percent), followed by Korea (10 percent), USA (7.1 percent), Japan (6.3 percent) and China (5.7 percent).

During the same period, the net income account deficit was USD 397.5 million, a decrease of USD 34 million (or 7.9 percent) compared to the previous year’s deficit. The decrease in this deficit was due to the decrease in income remitted to non-residents, especially the decline of 16.7 percent in the outflows of income on equity of direct investment. Net private transfers were a surplus of USD 276.9 million, a decrease of USD
95.4 million (or 25.6 percent). The decline in the worker and family remittances abroad was the main factor in this decrease.

### 3.2. Capital and Financial Account

In 2009, the balance on the current account and capital account recorded a deficit of USD 490.9 million, a decrease of USD 290.7 million (or 37.2 percent) compared to the previous year’s deficit. This decrease resulted from the decreases in the current account deficit and private transfer inflow.

Net official transfers in the form of cooperation financing (grants) was USD 559.7 million, up USD 81.4 million (or 17 percent) compared with 2008. During the same period, net official sector loans (excluding loans from the IMF) was USD 182 million, a decrease of USD 52.7 million (or 22.5 percent) compared with 2008. Net foreign direct investment registered a net inflow of USD 514.7 million, down USD 280 million (or 35.2 percent) compared with 2008. During the period, foreign direct investment inflows from the garment, resort, telecommunications, beverages, and packaging sector decreased dramatically.

**Chart 11: Balance of Payments**
(1998-2009)
Overall, the impact of the global economic recession on Cambodia has been felt mainly in the real economy but the slowdown has been manifested in decreases in foreign exchange inflows from exports, tourism and other services, remittances, private commercial financing, and in direct foreign investments. Cambodia’s balance of payments transactions showed therefore that the overall balance of the balance of payments has weekend, posting a smaller surplus USD 70.2 million as against USD 345 million recorded in the previous year. At the end of 2009, the level of gross official reserves was sufficient to cover 4 months of imports of goods.

Chart 12: Foreign Direct Investment Inflow
(1998-2009)

4. Foreign Reserve Management

4.1. Investment of Foreign Reserves

International foreign reserves have been invested in short-term deposits, overnight deposits and securities such as US T-Bills and Medium Term Instruments, with various international financial institutions, central banks in developed countries and high credit rating commercial banks in France, Luxembourg, Switzerland, USA, Hong Kong, Japan, Thailand and Singapore. In addition, a part of foreign reserves were placed under the management of the external fund managers.
As of the end of 2009, the international foreign reserves invested amounted to USD 2,600 million, an increase of 25.20% compared to December 2008 (2,075.85 million USD).

Since the second quarter of 2009, the global economic and financial condition, which negatively impacted the USA and countries in Europe and Asia, has been improving. Nevertheless, the US interest rate was maintained at 0.25% throughout 2009. The interest rates for the Euro and Pound Sterling were cut gradually from 2% to 1% and from 1.5% to 0.50%, respectively. Conversely, the interest rate for the Australian Dollar was reduced from 3.25% to 3.0% during the first three quarters of 2009, and increased from 3% to 3.50% in the last quarter of 2009. Such prevailing circumstances greatly affected the yields on investment portfolios, which shifted in the following manner: the rate on overnight investment was down from 0.31% to 0.01%; the return on US treasury bills from 0.48% to 0.17%; the interest rate on short-term USD deposits from 1.43% to 0.02%; the interest rate on Euro accounts from 1.30% to 0.20%; the interest rate on pound sterling deposits from 1.60% to 0.10%; and the interest rate on AUD deposits from 4.25% to 2.70%.

As a result of the consecutive drops in interest rates, the proceeds from external investment operations over the year 2009 decreased remarkably, down by 56.90% compared to the performance during 2008.

4.2. Intervention in the Foreign Exchange Market

To respond to the market demand and to maintain the stability of the national currency exchange rate, NBC continued to intervene by purchasing and selling the USD in the foreign exchange market as circumstances required.

In 2009, NBC purchased US dollars 29 times from money changers for a total amount of USD 84.8 million in exchange for KHR 350.1 billion. In addition, NBC conducted 32 auctions to sell US 54 million in the market in order to maintain the value of the Riel. As a result, the Riel exchange rate was stabilized by these interventions even though there was a little depreciation at the end of year 2008.

During the year, NBC also purchased USD 30.1 million from the Ministry of Economy and Finance but also sold USD 77.3 million and USD 43 million to the Ministry of Economy and Finance and the Cambodian Electricity Company (EDC) respectively.
4.3. Management of Gold and Foreign Exchange Business

In 2009, the management of business in metal and precious stones as jewelry was transferred to the Ministry of Commerce. NBC will manage only money exchange businesses and export-import of metal and precious stone. In addition to this management, NBC issued a Prakas on the Licensing and Authorization for money exchange businesses with an appendix on the code of conduct for money changer operations in order to improve the efficiency of the money exchange business.

During the year 2009, NBC issued 36 business licenses to money changers in Phnom Penh and eight business licenses to gold export-import companies. Moreover, 786 foreign exchange business licenses were issued by the provincial branches of NBC.

5. Relations with Bank and Financial Institution

In recent years, the financial system in Cambodia has developed rapidly with active participation from the private sector. Nevertheless, banks are still the core of the financial system, playing the largest role in financing economic activity in Cambodia. The government plans to introduce a stock exchange later in 2010, paving thus the way for mobilizing financial resources through capital markets.

The Cambodian financial sector is regulated by various institutions. Regulation and supervision of banks and microfinancial institutions is under the responsibility of the National Bank of Cambodia.

One of the main lessons emanating from the recent financial crisis is that a properly functioning banking sector is indispensable to sustained economic growth. As the necessity of improving supervision over the sector has come to the forefront and issues related to the appraisal of risks and determination of further development prospects by banks have become more crucial, further efforts are needed to further strengthen the banking system in Cambodia. Therefore, endeavors aimed at enhancing banking supervision remained unabated throughout the year. The NBC enhanced its analyses of the developments and the performance of the banking institutions in order to identify risk exposures which could make the financial system vulnerable to shocks. The analysis using both quantitative indicators and qualitative information, focused in particular on those institutions and operations that are considered important for the domestic financial system.
The result of the performance analysis of banks in 2009 indicates that banks were generally in a good condition, except for a short episode of restraint in liquidity. No banks hold asset-backed securities associated with sub-prime loans; their investment portfolios are satisfactorily secure and they generally follow prudent lending policies. Their funding model, moreover, is based on retail deposits and they have high liquidity and capital ratios. The latter have proved adequate to accommodate the valuation losses experienced as a result of the generalized decline in asset prices. The average bank solvency ratio rose from 27.7 percent in 2008 to 33.8 percent a year later, compared to the minimum regulatory requirement of 15 percent. Furthermore, despite the fact that the weak economic activity has caused an increase in bad loans, they remain at a relatively low level. The non-performing loan ratio, though higher than the 3.7 percent recorded in 2008, remained manageable at somewhat below 6 percent. It should be noted that the recent increase in non-performing loans reflects two things: the adverse feedback loop between the real economy and the financial sector, especially through the credit channel and the slowdown in real estate sector, and the strengthening of regulatory supervision with the introduction of new regulation on credit classification and provisioning in early 2009. Meanwhile, the average liquidity position of the whole banking system increased to 90.6 percent at end-2009, from 81.3 percent a year earlier.

Compared to 2008, total loans outstanding provided by banking and financial institutions increased from KHR 10,905.7 billion to KHR 11,317.7 billion, equivalent to a rise of 3.8 percent. Credit growth decelerated during 2009, mainly as a result of tighter financing conditions and weaker economic activity. The total number of borrowers increased by 9.4 percent, from 1,082,204 at the end of 2008 to 1,184,042 as of the end of the reporting year. Over the same period, the total deposits of residents and non-residents expanded from KHR 10,313 billion in 2008 to KHR 13,685 billion one year later, an annualized increase of 32.7 percent. The number of bank depositors rose remarkably during the year under review, up by 33 percent to reach 1,137,988 at the end of 2009.

In mid-2009, the NBC published “The Annual Report on Banking Supervision 2008.” This report provided a broader picture of the banking sector in Cambodia and its performance for the benefit of the general public. It also highlighted the role and responsibilities of the NBC as the banks’ regulatory authority in further promoting the development of the banking sector in the country and safeguarding the financial sector’s health by providing protection to bank depositors and contributing to the promotion of

1 This number refers to net loans, excluding accrued interest.
sustainable economic growth. In addition, it is expected that such public information would enhance the transparency and the accountability of the banking system, while also serving to educate customers in matters related to financial service providers.

5.1. Off-Site Supervision

Banking supervision is an ongoing effort of the NBC and has been conducted periodically in order to assess banks’ compliance with existing laws and prudential regulations. In light of the recent global financial crisis and the procyclicality in the financial system and its effects on the macro-economy, it is vital to make the supervision framework more prudent and to expand the scope of supervision to ensure that banks manage their risks efficiently, improve corporate governance, and adequately define their strategic aims.

Currently, off-site supervision is being performed through the examination of regular financial reports that help reveal unusual transactions, enable prompt corrective actions, and allow appropriate sanctions. The supervision specifically focused on indicators such as capital adequacy, quality of assets, earning capacity, and liquidity management.

Off-site analysis showed that, overall, the majority of banking institutions maintained good financial conditions. They also complied well with the regulatory requirements as set out in the relevant laws and NBC’s Prakas.

On the front of banking sector infrastructure, the Credit Information Sharing System (CIS) that was introduced two years ago to allow the sharing of negative credit information among member banks has been operating smoothly. Nevertheless, some technical improvements are still needed to better serve the requirements of users with respect to customer information that would in turn enhance efficiency in their decision making on credit provision. Meanwhile, the NBC has signed a Memorandum of Understanding (MOU) with the IFC to conduct a feasibility study on the establishment of private credit bureaus in Cambodia in the near future.

5.2. On-Site Inspection

Critical to the endeavors to further strengthen the banking system in Cambodia was the enhancement of the on-site supervisory activities. In this respect, banking supervision by the NBC has centered on reflecting and determining the financial performance as well as the overall conditions of banks by checking and verifying the truthfulness and correctness of banks' financial reports and assessing critical areas related to bank risk management.
framework and corporate governance. The on-site inspection helps to identify sources of risk and tests the resilience of the banking sector to withstand eventual shocks. The on-site supervision also covered the assessments related to a bank's compliance with laws, regulations and prudential rules introduced by the NBC.

In order to ensure systematic supervision, a plan is developed every year to determine financial institutions that should be subject to annual on-site supervision. In line with the on-site examination plan approved on January 06, 2009 and the revision to the original plan during a Bank Supervision Department’s meeting in July 2009, during 2009 the NBC successfully completed on-site examination of 17 commercial banks and two specialized banks.

According to the results of the on-site examinations during 2009, banks’ financial conditions, their performance and management, and their compliance with laws and regulations were generally sound and satisfactory. This was a good outcome, taking into consideration the impacts of the global financial crisis on the local economy. Despite this broad picture, some banks still have difficulties in following the calculation of Net Worth and Solvency Ratio as set out in NBC’s Prakas. Some other banks have been facing constraints in complying with a number of new Prakas, in particular the Prakas on Asset Classification and Provisioning for Banking and Financial Institutions, the Prakas on Governance and the Prakas on Fit and Proper Regulatory Requirements for Applying Entities and Licensed Banks and Financial Institutions.

Cases of non-compliance with NBC’s directives, regulations, and other corporate governance and management weaknesses revealed in the examination of each bank were deliberated on by the Commercial Bank Supervisory Committee and appropriate recommendations were issued for the relevant institutions. The Central Bank also undertook appropriate steps to monitor the progress by the relevant banks of its recommendations. Most banks have been able to follow the recommendations and remedy their deficiencies, thereby improving their condition and compliance status.

5.3. Microfinance Institutions Supervision

The quest by the NBC for the safety and soundness of the financial system is not limited to the deposit money banks, but also to other financial institutions under its purview, especially the microfinance institutions.
The rural financial sector in Cambodia has undergone rapid development over the past years, both in terms of the scope and the size of its operations. This sector has played a growing role in providing resources for the development of small and medium enterprises and the agricultural sector in Cambodia, which has in turn contributed to the government’s policy toward poverty reduction.

As of end-2009, the microfinance system in Cambodia consisted of 20 licensed microfinance institutions (MFIs), 26 registered rural credit operators, and around 60 NGOs, all of which provide informal financial services in the areas throughout the country.

Notwithstanding the direct and indirect impacts of the global financial turmoil on the domestic economy, the Cambodian microfinance industry witnessed appreciable growth during the year under review. In 2009, microfinance institutions and rural credit operators issued loans amounting to KHR 1,264 billion to 917,743 clients. When compared with the records a year ago, the portfolio outstanding and the number of borrowers increased by 9% and 8%, respectively, in 2009. Meanwhile, total deposits were KHR 38 billion, which were mobilized from 169,516 clients, with an annual increase of 47% and 9%, respectively. All of these indicators reflected not only the growth of rural economy and the dynamics of the rural finance sector in Cambodia, but also the increased confidence from investors and the public in the country’s future prospects, as economic and political stability has been broadly maintained.

Apart from conducting regular off-site supervision, as the supervisory authority NBC has performed on-site inspections on 14 microfinance institutions and four rural credit operators, aiming at monitoring the banks’ compliance with prudential regulations and other circulars, which should in turn further promote the confidence of the investors and the public in the country’s rural finance industry.

The on-site examinations showed that the non-performing loan ratio has picked up in recent years, which is due mainly to the effects of natural catastrophes and the practice of multiple loans. Nevertheless, the risk remained within the range deemed manageable.

Despite the many challenges to building a strong and sound commercial microfinance industry, thanks to their firm commitments and efforts, several MFIs have made remarkable progress toward an increase in efficiency in microfinance activities and the fulfillment of all NBC requirements for a license as a microfinance deposit-taking institution. Two
microfinance institutions have been granted a microfinance deposit-taking license: Sathapana and AMRET. While another two institutions, namely Angkor Mikroheranhvatho (Kampuchea) and Hattha Kaksekar, have already submitted the application for a license.

In harnessing greater support for the development of the microfinance industry in Cambodia, the NBC continued to collaborate closely with various local and international partners. Meanwhile, the Asian Development Bank has provided technical support for various areas related to microfinance in order to strengthen efficiency and improve the soundness of MFIs. Recent assistance involved the update of the uniform chart of accounts for licensing microfinance institutions and the provision of an expert to follow up on the implementation of the new chart of accounts and to provide capacity building to NBC’s supervision staff on both off-site and on-site examinations.

5.4. Development of the Banking Sector’s Legislative Measures

As the regulatory authority, the NBC has the responsibility to provide for an adequate legal framework for the smooth and efficient functioning of the banking sector. In this spirit, the NBC carried out a review of the existing Prakas, directives, guidelines, and circulars for banks and financial institutions, issued new Prakas, and made amendments to the old and outdated ones as necessary. In response to the new developments in the banking and financial sector and to the increased complexity of their operations, as well the ongoing international economic integration and financial globalization, in 2009 the NBC adopted eight new Prakas and a new circular, which are the following:

- Prakas on Overdraft Facilities Made Available by the NBC to Banks and Financial Institutions Facing Temporary Liquidity;
- Prakas on Licensing Fees For Microfinance Deposit Taking Institutions;
- Prakas on The Maintenance of Reserve Requirements Against Commercial Banks’ Deposits and Borrowings;
- Prakas on Asset Classification and Provisioning in Banking and Financial Institutions;
- Prakas on The Maintenance of Minimum Reserve Requirements of Banking and Financial Institutions;
- Prakas on The Liberalization of Interest Rate Setting;
- Prakas on Controlling Banks and Financial Institutions’ Large Exposures;
- Prakas on The Implementation of the Repo Master Agreement for Secured Interbank Transactions in the Money Market; and
- A Circular on the Cancellation of the Ceiling on Loans to the Real Estate Sector.

In addition to the above legislative documents, work on preparing a few more regulations is ongoing. This includes the drafting of an amendment to the Law on Banking and Financial Institutions.

5.5. Licensing and Registration

The NBC has the authority to license banks and financial institutions. In carrying out this duty, it is responsible for communicating to the interested parties all information related to the licensing policy, requirements, and procedures, while also analyzing applications submitted for approval to open operations as a commercial bank, a specialized bank or a microfinance institution in Cambodia.

In 2009, NBC issued licenses to a number of institutions, including a new commercial bank, two foreign bank branches, a bank representative office, and two new microfinance institutions.

As of the end of the reporting year, the banking system in Cambodia consisted of 27 commercial banks, 6 specialized banks, 3 representative offices of foreign branches, 20 microfinance institutions (MFIs) and 26 registered microfinance institution.

6. Central Bank Services

6.1. Accounts Management

The NBC holds and maintains the accounts of various government ministries and agencies, banking and financial institutions having licenses to operate in Cambodia, and international financial institutions. Currently, there are 1,471 accounts denominated in local and foreign currencies held with the NBC.

6.1.1. Government Account Management

The NBC actively contributed to the implementation of government policies toward improving the efficiency of the Public Financial Management Reform Program adopted by the Royal Government of Cambodia. To this effect and as fiscal agent for the government, it
opens and manages accounts for the central government agencies, and facilitates cash withdrawal and account transfers on behalf of the National Treasury. It also provides payroll services to the armed forces and to Government employees and carries out cash distribution according to the transfer orders of the Treasury.

The payment of taxes and customs duties to the government by the relevant tax debtors continued to be effected directly at NBC and the process went smoothly. For 2009, such collection amounted to 3,360 billion KHR.

6.1.2. Repository of Accounts for Bank and Financial Institutions

There are various types of accounts that banks and financial institutions hold with the NBC. These consist of current accounts, fixed deposit accounts, capital guarantee accounts, and reserve requirement accounts. As of end-2009, the total balance on the accounts of banks and financial institutions was a combined KHR 140 billion and USD 1,500 million.

6.1.3. Local Money Transfers

Other services provided to banks and financial institutions by the NBC besides managing their accounts include the domestic money transfers. During the year, the following transfers were made pursuant to the requests from banks and financial institutions as well as the money changers.

The transfer from provincial branches to Phnom Penh headquarters amounted to
- KHR 1,600 billion and
- USD 379 million.

The transfer from Phnom Penh headquarters to provincial branches amounted to
- KHR 2,300 billion and
- USD 51 million.

6.2. Clearing House Activities

The NBC continued to manage the Clearing House, through which all checks issued in Cambodia are settled. The clearing operations for both KHR and USD-denominated checks proceeded effectively and smoothly and were held every business day. The number of checks being used by the public increased steadily, especially within the banking community and in the public sector. The Government’s regulation requiring that payments of all kind of
taxes and duties with an amount above a certain threshold be made in checks has led to the increasing use of checks as a means of payment.

6.2.1. Clearing and Settlement of KHR-Denominated Checks

As of end-2009, 26 institutions have participated in the Clearing House for KHR-denominated checks. Those members included 24 commercial banks, one specialized bank, and the NBC itself.

In the reviewed year, the Clearing House operated on 238 days, during which 31,000 checks, valued KHR 1,273 billion, were cleared and settled. Both the volume and value of KHR-denominated checks declined compared to 2008. The statistics showed that the volume of checks cleared decreased by 3 percent, from 32,116 checks to 31,000 checks, while their value fell by 7 percent, from KHR 1.371.2 billion to KHR 1,273 billion.

6.2.2. Clearing and Settlement of USD-Denominated Checks

During 2009, the Clearing House for USD-denominated checks was participated in by 31 members, including 27 commercial banks, 3 specialized banks, and the NBC itself.

In the year under consideration, the Clearing House operated on 238 days, during which 416,000 checks, valued USD 5.7 billion, were cleared and settled. The number of checks going through the clearing process posted an increase, while their total value was down compared to 2008. In fact, the volume of checks cleared increased by 1 percent, from 413,367 checks to 416,000 checks, whereas their value shrunk by 20 percent, from USD 7,100 million to USD 5,700 billion.

6.3. Lending Activities

Over the course of the reporting year, the following records were made relating to the issuance of loans by the NBC and collection of debt owed to it:

♦ Banks and Microfinance Institutions:
  - Loans outstanding at the beginning of 2009: KHR 88.1 billion
  - Loans granted during the period: KHR 110.3 billion
  - Collection of debt owed: KHR 165.4 billion
  - Outstanding balance at end of 2008: KHR 33 billion.
7. Currency Management

The major functions of currency management at the NBC relate to the distribution of banknotes, cash withdrawals and deposit taking, inventory management and accounting, withdrawal of soiled notes from circulation and destruction, and anti-counterfeit measures. In the reporting year, cash transactions carried out through NBC’s teller desks experienced some decline. The record shows that during 2009 cash receipts through NBC’s teller desks amounted to KHR 6,812.4 billion, a decline of 8.7 percent compared to 2008. This decrease in cash receipts during the reporting year reflected the following movements: a drop in cash releases from the strong room of KHR 18.7 billion (0.6 percent), a drop in the current account deposits of financial institutions of KHR 471.1 billion (21.4 percent), a decrease in cash receipts in the form of taxes and customs duties of KHR 117.7 billion (10.9 percent), a decline in the deposits of Electricité du Cambodge of KHR 55.8 billion (10.4 percent), and a fall in the cash transfers from NBC’s municipal and provincial branches of KHR 180.9 billion (35 percent).

Meanwhile, other operations led to a substantial increase in cash inflows through the NBC’s teller desks. Cash proceeds from the sale of US dollars rose by KHR 196.9 billion, an increase of 16 times compared to last year’s operation, whereas cash receipts from other sources registered an increase of KHR 0.6 billion (32.2 percent).

During the same period under consideration, cash payments through NBC’s teller desks totaled KHR 6,826.1 billion, a decrease of 8.3 percent on 2008. Of this decrease, the amount placed into the strong room was reduced by KHR 154.9 billion (5.8 percent); the amount of local currency used to purchase foreign currency declined by KHR 990.9 billion (77.7 percent); cash withdrawals by Electricité du Cambodge declined by KHR 16.7 billion (5.1 percent); and cash outflows for other purposes decreased KHR 6.8 billion (14.6 percent).

In the course of the year, some other account items reflected moderate cash outflows. Withdrawals from current accounts deposits rose by KHR 127.7 billion (13.7 percent); the cash withdrawals by the National Treasury increased KHR 366.1 billion (33.4 percent); cash paid out to NBC’s provincial and municipal branches increased KHR 53.1 billion (5.4 percent); and cash withdrawals amounted to KHR 3 billion (66.8 percent).

As for currency operations in US dollars during 2009, cash receipts through the teller desks amounted to USD 3,075.2 million, representing an increase of USD 447.7 million (17
percent) on operations in 2008. In contrast, the amount disbursed through the teller desks amounted to USD 3,075.4 million, representing an increase of USD 447.7 million (17 percent), compared to 2008.

NBC examined notes and coins regularly to ensure that a high quality standard was maintained. Notes and coins that were deemed unfit for circulation were destroyed. For this purpose, NBC collected old, worn and torn local currency notes from circulation and replaced them with new ones, thereby promoting the use of local currency. Concerning the old and soiled notes, NBC cautiously recounted and sorted them, and duly destroyed unusable notes according to the prescribed procedure.

With respect to counterfeit notes, the NBC continued with its various anti-counterfeit measures to prevent and minimize the circulation of counterfeit notes. As part of a public awareness campaign, the NBC also issued a Master Circular for the guidance of the banks and the general public regarding detection of forged notes and the procedure to be followed on detection of forged notes. In addition, NBC continued to cooperate with the relevant authorities very closely to ensure that any counterfeit notes were quickly detected.

8. Payment System Development

The modernization of the Clearing House for the Interim Solution has been completed and was commissioned at the end of the first semester of 2009. Through this new system, the transmission of data for check clearing to and from clearing house and members could be made electronically, which is faster, more convenient and more secure. Moreover, technical and physical standards have also been introduced and implemented consistently in this new system. After the introduction of this Interim Solution, the National Bank of Cambodia began undertaking the development of the follow-on second phase, Full Solution, which is more robust, with increased security and efficiency. This will enable electronic inter-city clearing between provincial Clearing Houses and will also extend the processing capabilities of the system to provide new payment instruments into clearing and settlement systems, e.g, electronic payment orders.

In order to facilitate the orderly use of this new system and as a fundamental basis for clearing and settlement operations, the National Bank of Cambodia has issued a set of NBC Clearing House Rules and Procedures and an associated Clearing House Service Level Agreement.
II. Internal Management of NBC

1. The Activities of the Board of Directors

The Composition of the Board of Directors of NBC was as follows:

- H.E. Chea Chanto  NBC’s Governor  Chair
- H.E. Neav Chanthana  NBC’s Deputy Governor  Member
- H.E. Aun Pornmoniroth  Representative of the Head of the Royal Government  Member
- H.E. Iv Thong  Representative of the academics  Member
- H.E. Chou Kimleng  Representative of the MEF  Member
- Mr. Lay Mengsun  Representative of the private sector  Member
- Mrs. Mao Son  Representative of NBC’s staff  Member

Over the course of the year 2009, the Board held six meetings, during which important matters related to NBC’s activities were brought forward for discussion and approval. These meetings are outlined below:

- The 72th Meeting on January 28, 2009, to review and adopt the draft decision to establish a committee to examine NBC’s accounting record for the financial year 2008;
- The 73th Meeting on February 18, 2009, to review and adopt the draft report on NBC’s budget implementation for the financial year 2008 and the budget plan for 2009;
- The 74th Meeting on July 8, 2000, to discuss and adopt the draft report of First Semi-annual Report of NBC for 2009;
- The 75th Meeting on July 20, 2008, to discuss the report on NBC’s foreign exchange management;
- The 76th Meeting on September 10, 2009, to review and adopt the draft report on NBC’s budget implementation for the first semester of 2009 and the budget plan for the second semester of 2009;
- The 77th Meeting on December 22, 2009, to discuss and adopt the draft Annual Report of NBC for 2009.
2. Human Resource Development

2.1. Staff Statistics

- The full-time staff under NBC’s official staff status (at the headquarters) as of end-2009 totaled 851 persons (477 male and 374 female). This number also included an NBC staff that had been attached to the Foreign Trade Bank of Cambodia. In addition, 29 persons are working for NBC on a contractual basis (24 male and 5 female).

- Staff working at NBC’s municipal and provincial branches totaled 396 persons (226 male and 170 female).

The total number of NBC staff as of end 2009 amounted to 1,247 persons (703 male and 544 female). When compared to the previous year’s record of 1,141 persons (645 male and 496 female), the following changes were observed:

- At the headquarters: an increase by 69 persons (90 were newly recruited; 21 resigned or retired).
- At municipal and provincial branches: an increase of 37 persons (56 were newly recruited; 19 resigned or retired).

2.2. Training and Development

2.2.1. Local Training

NBC continued to pursue its commitment to enhance its staff’s skills and capabilities, both at the headquarters and at the municipal and provincial branches. A number of in-house training programs were organized for this purpose during the reporting year. To improve the professional skills of the staff at the municipal and provincial branches, in 2009 NBC conducted a guiding session, which was the 13th of its kind, for the benefit of 41 employees. Other sessions included the 10th perfection course for 90 employees (of which 44 employees were from headquarters and 46 from provincial branches).

To improve the foreign language knowledge of staff, NBC facilitated English training classes in five provincial branches, in which 55 staff participated, and a Thai language class for eight employees in the Koh Kong provincial branch.
Eight other in-house seminar events on a wide range of topics related to central banking, with participants totaling 350 persons, were also organized over the course of the reporting year. The courses covered included Anti-Money Laundering, Role of the Banking Sector in the Development of the Capital Market, Securities Issuing and Trading, and Issues Related to Open Market Operations.

NBC also sent a number of its officials to participate in various long-term training courses and academic degrees offered by local training institutions, which included the following:

- The high-level perfection course (1 staff) and the medium level perfection course (1 staff) at Royal Administration School
- A master’s degree at Specialist University in Cambodia (1 staff) and
- Long-term course at the Centre for Banking Studies (total 14 staff, 9 of whom were in the 18th graduating group and 5 of whom in the 19th graduating group).

2.2.2. External Training

Along with the training programs organized within the country, as a result of NBC’s active cooperation with foreign central banks and a number of multilateral financial institutions, various technical assistance and training support programs were provided to NBC over the reporting year for the human resource capacity building of its employees. On the whole, a total of 221 staff members attended 133 seminar events organized abroad during 2009. Besides this, 22 employees participated in eight study tours; 39 officials took part in 15 different short-term courses, and nine staff members attended long-term academic study programs. Furthermore, 98 NBC officials were sent abroad to join 41 different international meetings on various subjects relevant to the central bank’s operations.

The abovementioned training events and meetings were supported by various international and regional institutions such as the International Monetary Fund, the World Bank, the Asian Development Bank, the SEACEN Centre, the Government of India, the Deutsche Bundes Bank, the Central Bank of Luxembourg, the Bank of Korea, the People Bank of China, the Bank Negara Malaysia, the Bank of Thailand, the Bank of Vietnam, the Japan International Cooperation Agency, and various other friends and partners.
3. Internal Audit and Inspection

The objective of the NBC’s internal audit function is to provide assurance that the operations of the NBC are conducted within an adequate risk management, control and governance framework. During 2009, in order to further strengthen the efficiency of the Internal Audit and Inspection functions, the NBC issued a number of Prakas related to rules and procedures for the conduct of the internal audit. In the reporting year, internal audit assignments were conducted on the Foreign Exchange Department of the NBC and a number of its branches, namely Takeo, Kampong Chnang, Kampong Cham, Svay Rieng, Ratanakiri, Kampong Speu, Bantey Meanchey, Pursat, Kratie, Prey Veng, and Kandal provinces. After the audit assignments were completed, internal audit reports were issued with some recommendations for corrective actions. On top of that, a follow-up audit on five other NBC branches took place: Siem Reap, Battambong, Kampot, Steung Treng and Kampong Cham. It was noticed that the branches have appropriately taken corrective actions upon auditors’ recommendations, except some of them which have not fully implemented due to the delay in updating the procedure manual for branches (the Red Book).

The Internal Audit Department of the NBC is a relatively young unit. Therefore, there is a great need to upgrade the staff capacity for the assignments. Training has been conducted on an ongoing basis. The practical conduct of on-site audit at various branches and some departments at headquarters provided a platform to enhance the skills and experiences of the Audit Department. In addition to in-house training, some staff were also sent to overseas training. In 2009, two NBC auditors were attached to the Central Bank of Luxembourg for a period of two months and another auditor was sent to participate in a short-term seminar at Deutsche Bundes Bank in Germany and Armenia.

With respect to the inspection functions, besides conducting off-site inspection by examining monthly reports of key departments at NBC’s headquarters and its branches, efforts were made that on-site inspection activities were carried out in accordance with the annual inspection plan for 2009. This year, ten surprise visits were made on NBC’s municipal and provincial branches; some branches were inspected twice. Over the course of the inspection process, the inspectors focused on monitoring particular areas of performance within them, took prompt corrective action on every failure that was determined and carried out necessary follow-up examinations. The branch’s inspection assignments focused on cash
and vault management, corporate governance, as well as the solidarity among officers. In addition, inspectors advised the branch’s management to establish and regularly maintain internal control.

4. Management of NBC’s Branches

Over the course of the year under review, the management of NBC’s provincial branches focused on increasing the efficiency of branch operations, thereby enhancing the role of the Central Bank as the fiscal agent for the Government, and in particular as a partner for the Ministry of Economy and Finance, in collaboration with provincial and municipal authorities, to implement the second phase of the Public Finance Management Reform initiated by the Government.

To this effect, NBC offered salary payment services to Government institutions in various cities and provinces, including the armed forces, commune and district councils. Meanwhile, NBC’s provincial branches have also arranged themselves in terms of human resources, technical capacities and necessary infrastructure in order to smooth and enhance the efficiency of such operations.

Moreover, during 2009, an instruction from NBC’s headquarters had already been issued to allow provincial branches in Banteay Meanchey, Battambang, Siem Reap, Sihanoukville and Svay Rieng to open accounts for the provincial post offices in order to process international postal money orders initiated by their customers.

Moreover, during 2009, the Ministry of Economy and Finance decided to use, on a pilot basis, banking services for collecting the Government’s revenue and effecting Government payments. This new scheme, which aimed at improving cash management and strengthening the single account of the Treasury at the NBC, has been tried out in Kandal and Banteay Meanchey provinces. Consequently, the two relevant provincial treasuries were required to open accounts with Acleda Bank, which in turn collects tax revenue and makes payments on behalf of the government. Nevertheless, the services currently provided to the public sector by NBC’s provincial branches in other provinces remain unaffected and have continued smoothly and efficiently.
Meanwhile, NBC has reaffirmed its role and responsibilities with regard to the control over the purchase and sale of precious metals and stones and then clarified these responsibilities with other relevant authorities. Such business operations are in practice under the oversight of the Ministry of Commerce and the municipal and provincial branches of the NBC have carried out their responsibilities adequately with respect to this issue.

In addition, the NBC has also made further efforts to strengthen the services and operations of its branches. Besides providing regular training to branch managers, senior NBC officials from the head office have made regular visits to all the branches.

III. International Relations

1. Multilateral Relations

1.1. Relations with International Monetary Fund

During 2009, IMF Missions visited Cambodia on two different occasions in the context of the regular bilateral discussions in terms of Article IV of the Fund’s Articles of Agreement on economic development and policies. The first visit took place from 19 February to 4 March 2009, while the second one went from 9-23 September 2009. In their latest visit, when an assessment on the latest economic and financial development in Cambodia was made, the Mission stated that the global economic crisis is having a larger impact on Cambodia’s economy than previously anticipated. Garments, tourism, and the construction sector are expected to be more adversely affected by the crisis more than had been expected during the Mission in March. By contrast, efforts to develop infrastructure projects such as rural roads, bridges and irrigation systems can support growth in agricultural production, which would rise by 5 percent in 2009 and next year, and contribute to bringing down operating costs in the period ahead. As a result, the Fund has projected that the Cambodian economy would have a negative real growth of -2.7 percent in 2009. Nevertheless, thanks to expected improvements in external conditions, Cambodia is economic performance is expected to recover modestly next year, with growth scaling upward to 4.2 percent in 2010; the medium-term outlook for growth could reach 6-6.5 percent.

In addition, the Fund articulated that inflationary pressure in Cambodia has become subdued in 2009 on account of lower domestic demand on goods and services and commodity prices. In addition, the lower money supply and the strength of the US dollar also
contributed. The overall inflation is expected to increase to around 5.25 percent by the end of 2009 and is projected to rise modestly in 2010 owing to the risks of higher oil prices and the large domestic financing of the budget.

During the two visits, the Missions commended the NBC for taking appropriate actions in response to the strains on the banking system from tighter liquidity conditions and for safeguarding the health of the banking system through, among other measures, the enhancement of the management of banks’ short-term liquidity risk, the introduction of an overdraft facility, the strengthening of the credit classification standard, and the implementation of the new reserve requirement system. Moreover, the Fund also welcomed the NBC’s strong commitment to continue strengthening bank supervisory capacity and to enhance the compliance by banks with prudential regulations. It also praised the NBC’s efforts to put in place a framework for a bank’s exit when its condition requires it. In light of the establishment of the stock exchange in the very near future, the Mission recommended the two relevant supervisory and regulatory authorities (Ministry of Economy and Finance and the National Bank of Cambodia) to strengthen their cooperation in order to avoid the spillover risk from sector to another.

With regard to technical assistance, the NBC has received useful support from both the Fund’s technical mission and the principal advisor. Over the year under review, the technical assistance focused on on-site inspection of commercial banks, strengthening the internal audit, enhancing human resource capacity in the field of bank supervision, and improving regulatory frameworks. Assistance was also provided in the area of implementing recommendations by the IMF and ADB related to banking and financial sector reforms.

Concerning financial relations with the Fund, in 2009 Cambodia received SDR 64 million under the Fund’s General and Special SDR allocation.

1.2. Relations with the Asian Development Bank

Over the course of the year, the NBC as the executing agency for the Financial Sector Program Loan II (FSPL II), which is supported by the Asian Development Bank, continued to work closely with other relevant ministries to implement the next steps of the reform program as set out in the “Financial Sector Development Strategy for 2006-2015.” The financial support provided under the FSPL II amounted to USD 40 million and was split into
four sub-programs, with USD 10 million each. Sub-programs 1 and 2 were successfully completed and the amounts of USD 10 million and USD 10.3 million were released for the benefit of the Government in 2007 and 2008, respectively.

The focus of all relevant parties of the FSPL II during 2009 was to carry out the reform agenda under Sub-program 3. According to the Minutes of the Loan Negotiation between the Government and ADB, which was co-signed by representatives of the NBC and the ADB on October 13, 2009, ADB agrees to disburse a further amount of USD 10 million upon completion of the reform activities associated with sub-program 3 within a specified time frame. ADB’s loans, made under FSPL II, carry an interest rate of 1 percent per annum during the grace period, and 1.5 percent per annum thereafter.

Toward the end of 2009, a number of meetings between relevant representatives of the Government and the ADB took place with the aim to discuss the subsequent working schedules under Sub-program 4, which is expected to start in 2010.

With regard to the efforts to enhance the Credit Information System (CIS), NBC signed a Memorandum of Understanding with ADB on August 7, 2009, to upgrade and transform the current CIS into a Credit Bureau. Under the new arrangement, ADB will provide local and international experts for a period of three months commencing from March 2010 to assist NBC on improving software and hardware for the new system, which is expected to enhance its performance.

1.3. Relations with ASEAN Countries

The recent crisis has tested ASEAN as a regional forum as to whether ASEAN represents a suitable regional architecture for co-operations that serve the needs of the people in the region. In general, ASEAN countries as a whole have come out well from the turmoil. The crisis has provided ASEAN members with greater impetus to integrate further so as to address the common challenges that we are currently facing and hence strengthen regional resilience. During this episode, greater and more frequent policy dialogues among finance ministers and central bank governors have been made, policy coordination has been pursued, and cooperation strengthened.

Delegations of high-ranking officials from the NBC attended the 5th ASEAN Central Bank Governors Meeting, the 17th ASEAN Finance and Central Bank Deputies Meeting and
other related meetings under the framework of the cooperation among ASEAN-10, as well as ASEAN+3 (China, Japan and Korea), that were organized during the year. Various efforts have been made aiming to attain integration for three main sectors: regional capital market development, capital account liberalization and financial sector liberalization. ASEAN infrastructure financing represent another initiative of ASEAN cooperation, where members agreed to establish Asean Infrastructure Fund in the near future in order to mobilize resources in ASEAN for an efficient use in the region. Furthermore, in order to improve their capacity to prevent or to detect the occurrence of an economic and financial crisis, Macroeconomic & Finance Surveillance Unit will also be soon established.

On the front of cooperation within the framework of ASEAN+3, the establishment of the regional resource pool called Multi-lateralization of the Chiang Mai Initiatives (CMIM) has been almost completed. These initiatives have the objective of providing liquidity support to members in the region, and to complement the efforts of the international financial institutions such as the IMF in this matter. The formal agreement for such as arrangement has already been finalized, and will be soon co-signed by the Ministers of Finance and Central Bank Governors of ASEAN+3, thereby activating the CMIM.

In addition to the above efforts, the ASEAN+3 countries also pushed forward the implementation of the Asian Bond Market Initiatives. These initiatives encompass efforts to develop and strengthen the local currency and regional bond markets so as to allow the use of Asian savings within the region. In furtherance of that objective, ASEAN countries together with the Asian Development Bank have been working on an arrangement to establish the Credit Guarantee and Investment Mechanism to provide credit enhancement and make investments to allow eligible issuers to access local currency bond markets and thereby avoid currency and maturity mismatches by issuing within the region. The new mechanism is expected to be operationalized by the middle of next year.

1.4. Relations with SEACEN

Since joining as a full member of the South East Asia Central Banks (SEACEN) in April 2006, NBC has worked closely with this association to ensure effective cooperation in the areas of human resource capacity building, studies and research on economic and monetary policy issues, and the exchange of information among members of the SEACEN
Centre. Meanwhile, membership in the SEACEN Centre has also proved to be a platform for the NBC to enhance its bilateral relations with various regional central banks.

Over the course of the year, NBC continued to be actively involved in SEACEN’s activities. On February 6-11, 2009, a high-ranking delegation of the NBC attended the 44th SEACEN Governors’ Conference, which was organized by the Bank Negara Malaysia. The theme of the Conference was “Sustaining Monetary and Financial Stability in an Environment of New Global Financial System,” with a focus on the recent global financial crisis and its implications on central bank policy. The 28th Meeting of the SEACEN Board of Governors was also held back to back with this important conference.

Moreover, during 2009, an NBC delegation participated in the 7th SEACEN Executive Committee (EXCO) Meeting, which was held on January 8-9, 2009 in Yogyakarta, Indonesia. During this occasion a seminar was also organized, promoting discussions related to the crisis in the global financial markets and its repercussions on the global economy, the interactions between the financial system and the real economy, and the need to strengthen the financial system.

Meanwhile, the NBC, in close collaboration with the SEACEN Centre, organized a seminar on “Bank Supervision Based on Risk Analysis,” which was held from August 31 to September 4, 2009 in Siem Reap.

Also throughout the year, a number of preparations were put in place for the NBC to host the 45th SEACEN Governors’ Conference and 29th Meeting of the SEACEN Board of Governors in February 2010 in Siem Reap.

2. Bilateral Relations

Besides the abovementioned multilateral relations, the NBC has been paying great attention to maintaining and fostering close bilateral contacts with foreign central banks and international institutions in various regions around the globe. Such relationships were manifested through the participation of NBC staff in various foreign central banks’ training occasions and conferences, the sending of experienced visiting lecturers and consultants to Cambodia to deliver talks on issues related to central banking, and the exchange of staff
visits in order to facilitate the sharing of experiences and practices as well as to provide opportunities to learn from each other about the banking system in each country.

A Memorandum of Understanding on Bilateral Cooperation between the Bank of Laos PDR and the NBC was signed on January 30, 2009, and stipulates the willingness and commitments of the two parties to exchange their experiences and other relevant information. Following this MOU, during May 25-28 2009, the NBC hosted a special training and study tour on banknote printing to five staff of Bank of Laos PDR.

In the meantime, the NBC signed another MOU with the Central Bank of Malaysia, Bangladesh Bank, and the Central Bank of Sri Lanka on the prevention of money laundering and combating the financing of terrorism.

Concerning cooperation with the Bank of Korea, a high-ranking delegation of the NBC visited the Bank of Korea from May 23-26, 2009. During this visit, both parties exchanged experiences on monetary policy implementation, the actions taken to minimize the impacts of the global financial crisis, areas for technical assistance, as well as capacity building for the NBC. Over the course of the year, the Bank of Korea provided training two times on topics related to payment systems for NBC staff. In addition, two officials from Bank of Korea have seconded at NBC on subjects related to payment systems and the development of a money market in Cambodia.

Meanwhile, a new cooperation was initiated in 2009 by the NBC and the US Treasury, with the latter providing long-term technical assistance to the NBC on banking supervision.

With regard to relationship between the NBC and the Central Bank of Luxembourg, in 2009, the Central Bank of Luxembourg provided two scholarships for a master’s program at University of Luxembourg to staff of the NBC. Moreover, some NBC officials were invited to participate in a short-term training course on banking and financial sector issues.

The cooperation between the NBC and the Bank of Thailand was also strengthened. Over the course of the year, three seminars were organized for the staff of the NBC, which included a visiting lecturer from the Bank of Thailand to the NBC and two NBC staff visits to the Bank of Thailand. The topics of the discussion focused on macroeconomic management and monetary policy, and the implementation of the Basel II. Another
achievement of the cooperation between the NBC and the Bank of Thailand was the signing, in April 27, 2009, by the Krung Thai Bank and ACELEDA Bank Plc, of an agreement to establish an effective payment system to promote investment and trade development between Cambodia and Thailand.

Within the framework of bilateral cooperation with the NBC, the State Bank of Vietnam provided a short-term training course to staff of the NBC on subjects related to banking and finance.

During the period under review, a large number of NBC officials had an opportunity to attend short-term courses sponsored by the Deutsche Bundes Bank on topics relevant to central bank operations.

On the whole, international cooperation has provided various benefits to the NBC. The technical assistance offered in association with such cooperation contributes to narrowing the gap between demand and the need for human resource capacity building within the NBC. The NBC will thus continue to maintain and both the existing multilateral and bilateral cooperation. Apart from the ongoing cooperation, NBC will also seek to further expand relationships with other central banks and financial institutions for the purpose of sharing experiences on monetary policy issues and other subjects of interest to central banks and while also seeking to gain further technical assistance support.
Conclusion

There have been some signs recently that the world is recovering from the worst global recession since the 1930s after policymakers in the advanced economies made decisive efforts to cut interest rates to record lows and boost public spending to revive growth. However, the pace of recovery remains fragile.

The latest projections by various international financial organizations indeed suggest that most major economies, including those in the euro area, will contract this year and a recovery is only likely to set in well into 2010. The Government’s most recent forecast for the Cambodian economy anticipated that GDP growth would fall from 6.7 percent in 2008 to 2.1 percent in 2009.

In light of the spillover effects of the global crisis on the domestic economy, the Government is determined to speed up the structural reforms, diversify the economy, and accelerate the pace of reform in the agricultural sector, which should help achieve more progress in poverty reduction.

First and foremost, the crisis taught that sound macroeconomic fundamentals and prudential measures are the necessary policy conditions for preserving price stability, and sustaining economic growth and achieving financial stability. A general consensus of the causes of the recent crisis is that low interest rates and excess liquidity in the past compromised the quality of loans held by financial institutions and contributed to the challenges threatening the stability of financial sector. However, weaknesses in the institutional framework of the global financial system (especially with respect to regulation, prudential oversight, and risk management to cope with rapid growth of the financial systems) coupled with the complexity and diversity of financial instruments and markets combined to cause damage to financial intermediaries.

These represent new challenges for the banking sector. While at present local banks have been spared the full impact of the financial crisis, in the years ahead they will be operating in an environment that is likely to have changed as a result of the increasing process of economic and financial integration, the attempt of banks to diversify from retail banking to a more complex business structure, and the emergence of a capital market in
Cambodia in the very near future. Therefore, moving ahead, our banks will have to face tougher regulations and strengthen their capacity to manage risk and growth itself.

The shape of financial regulation and supervision also needs to be changed accordingly. We have to learn from the crisis if we wish to move forward effectively and sustainably and NBC is committed to taking its responsibilities in all the important areas very seriously. We need, indeed, to enhance macro-prudential supervision and micro supervision. The two processes are essential and complementary components of an effective monitoring system for financial stability. Financial infrastructure, including the payment system, will have to be strengthened. Due to the current crisis, much more emphasis will be placed over the coming months on contingency planning and crisis management. Last but not least, the capital market, when established, needs to be closely monitored as a failure in one sector can easily affect the performance of another. The latter two issues require, beyond doubt, close collaboration between NBC and the Ministry of Finance. Under the clear and wise guidance of the Royal Government of Cambodia, the two regulatory and supervisory authorities will be a joint force with a greater impetus toward addressing the common challenges that we are currently facing, thereby strengthening the country’s resilience to external shocks.

洗干净
Appendix