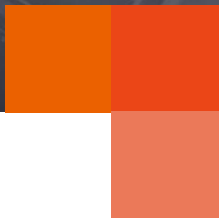




# CAMBODIA'S BANKING INDUSTRY

## UPDATES

August 2023



## EXECUTIVE SUMMARY (1/2)

### Is Cambodia's banking industry highly oversaturated?

The Cambodian banking industry is facing increasing systemic risks due to the looming economic uncertainty and rising non-performing loans (NPLs). Key indicators, such as Total Credit (% of GDP), Credit Non-financial (% of GDP), and Domestic Credit to Private Sector (% of GDP) are recorded at 195%, 188%, and 177%, respectively, as of the end of 2022. These figures are often used to argue that Cambodia's private sector is over-indebted, leading to concerns about the local banking industry being highly oversaturated.

However, using these ratios to assess the overall indebtedness of an economy's private sector and making direct comparisons with other countries requires a few important adjustments to both the numerator (Credit amounts to private sector) and the denominator (GDP figures).

First, the above-mentioned ratios do not effectively serve our purpose of assessing the private sector's level of indebtedness. For example, the "Total credit (% of GDP)" includes financial institutions (banks & MFIs) as borrowers, while both "Credit to Non-financial (% GDP)" and "Domestic Credit to Private Sector (% of GDP)" do not account for borrowings from overseas lenders, non-financial institutions, general governments, households, and others. Although these factors may not be significant in Cambodia, they can have a substantial impact in other countries to which Cambodia is usually compared.

In that matter, the IMF's "private debt, loans, and debt securities % of GDP" seems more suitable for comparing the overall indebtedness of private sector across countries with different level of economic and financial development.

Furthermore, we believe that the private sector's debt level relative to GDP, particularly for countries like Cambodia, tends to be overestimated due to the country's substantially larger informal economy and significantly smaller government final consumption expenditure. These can make the country's GDP appear much smaller than that of other countries, thereby making Cambodia's ratio look much greater compared to that of other countries.

After factoring in the necessary adjustments, we were able to draw meaningfully different results with some useful takeaways mentioned below.

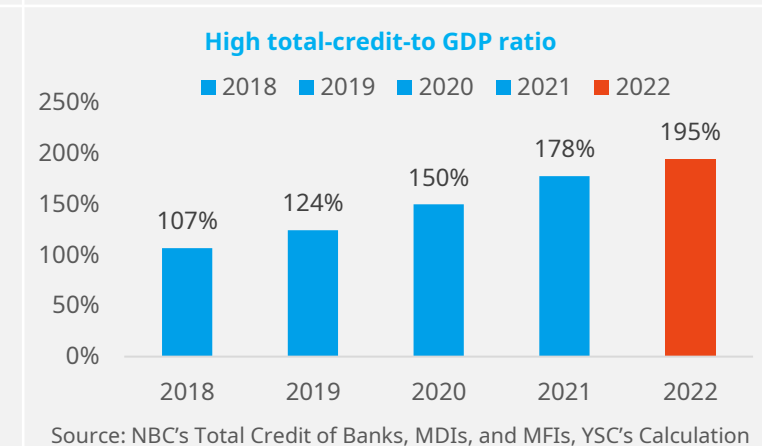
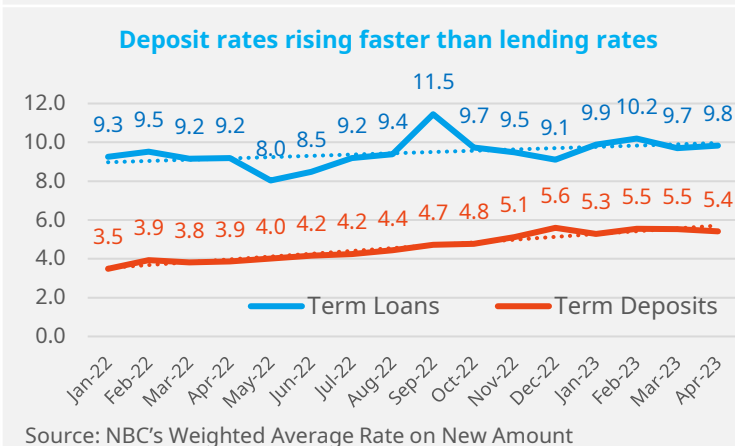
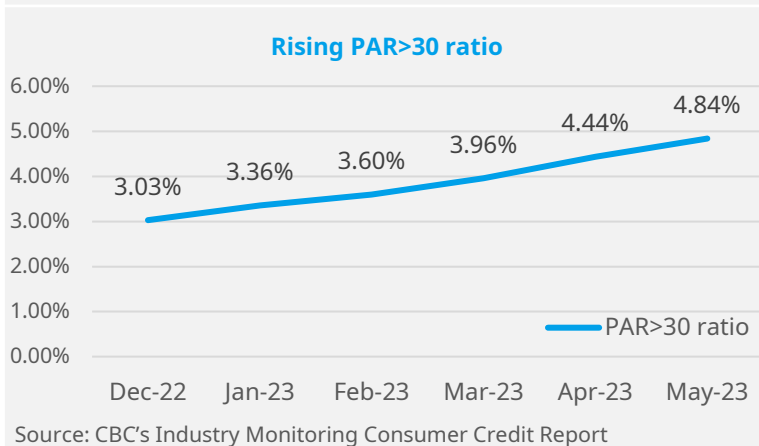
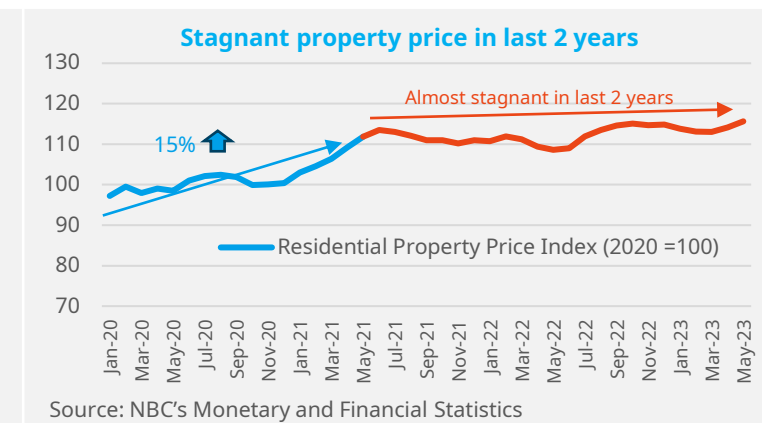
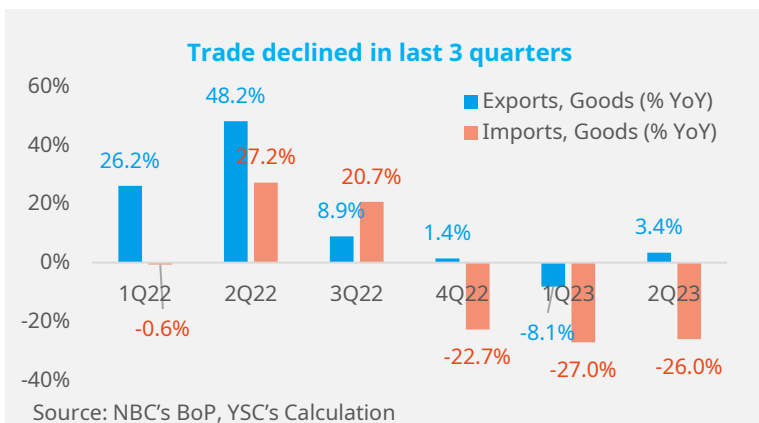
## EXECUTIVE SUMMARY (2/2)

### The key takeaways

1. First, after adjusting for (1) government final consumption expenditure and (2) informal economy, Cambodia's level of private sector debt remains relatively lower compared to more advanced economies in Asia, such as Thailand, Malaysia, Singapore, and South Korea.
2. Although the adjusted ratio itself suggests that Cambodia remains lower in the overall private sector debt, the rapid growth rate of private sector debt raises concerns about potential over-indebtedness, highlighting the financial sector's susceptibility to external shocks.
3. Interestingly, Thailand had a similar experience during 1990s where the ratio rose steeply in the first half of 1990s followed by a seemingly painful correction in the second half. Even if the correction may have been exacerbated by the Asian financial crisis triggered by sudden outflows of capital from foreign lenders, the drop in private sector debt seems much deeper in Thailand than other Asian economies. Although it is not likely for Cambodia to follow suit as Cambodia's current situation is fundamentally different from Thailand's back then, as Cambodia's private sector almost solely rely on credit from domestic banking industry while Thailand's private sector back then was heavily reliant on credit from overseas lenders, Thailand is an example of a potential risk of rapidly increased private sector debt.
4. Therefore, it is more important for Cambodia's banking sector, as the major domestic lender, to be mindful of the growth rate and maintain a sustainable ratio moving forward. For example, the local private sector still has room for a double-digit growth of 10% for the next five years then continue to grow at the expected rate of nominal GDP growth of approximately 7%, while maintaining the adjusted ratio at around 140%.
5. Sustaining future credit growth rates similar to the past five-year average of 20% may no longer be feasible or advisable. The current situation calls for a long-term oriented approach, shifting focus towards qualitative rather than purely quantitative growth. By adopting responsible and cautious approach, relevant stakeholders may mitigate potential risks and ensure the stability and health of Cambodia's banking industry and overall economy.

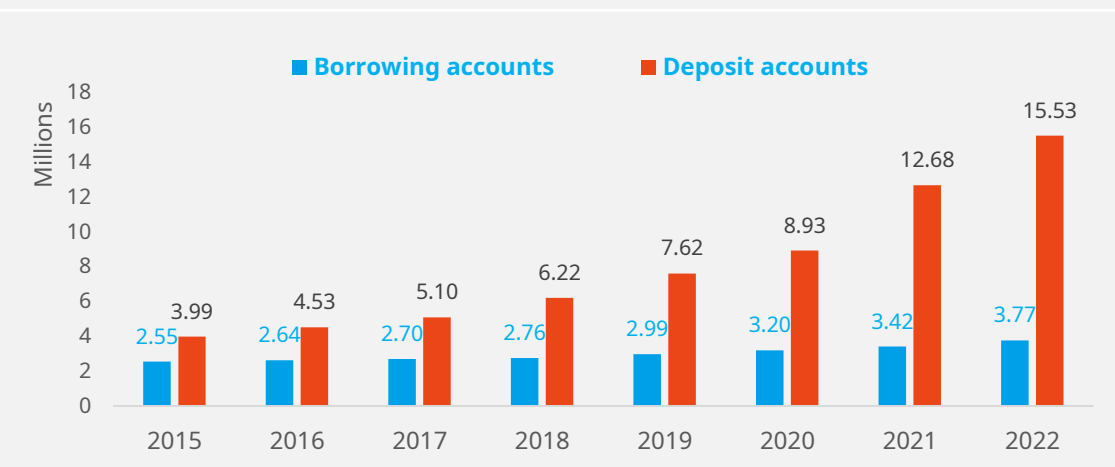
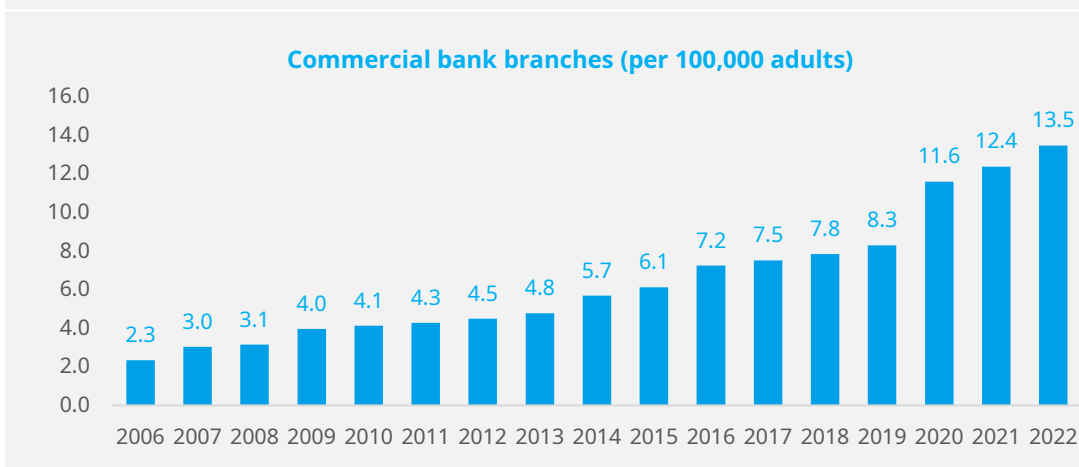
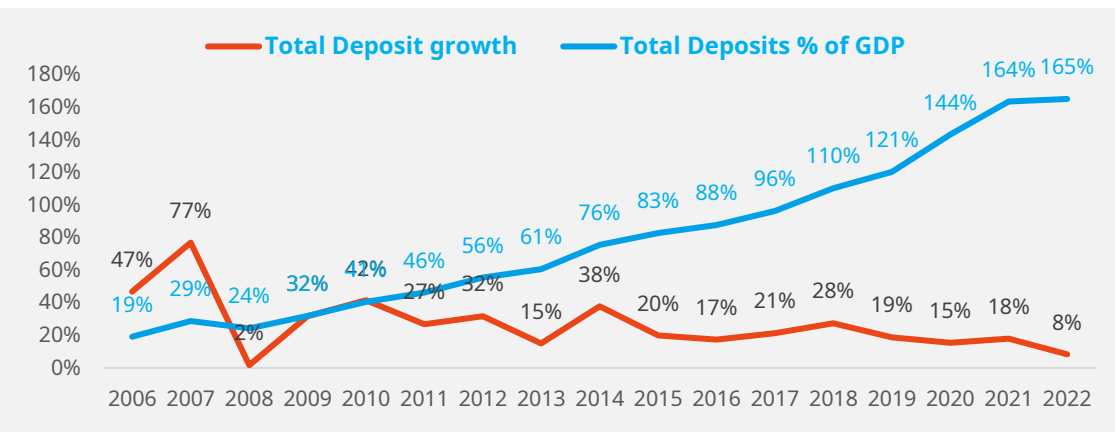
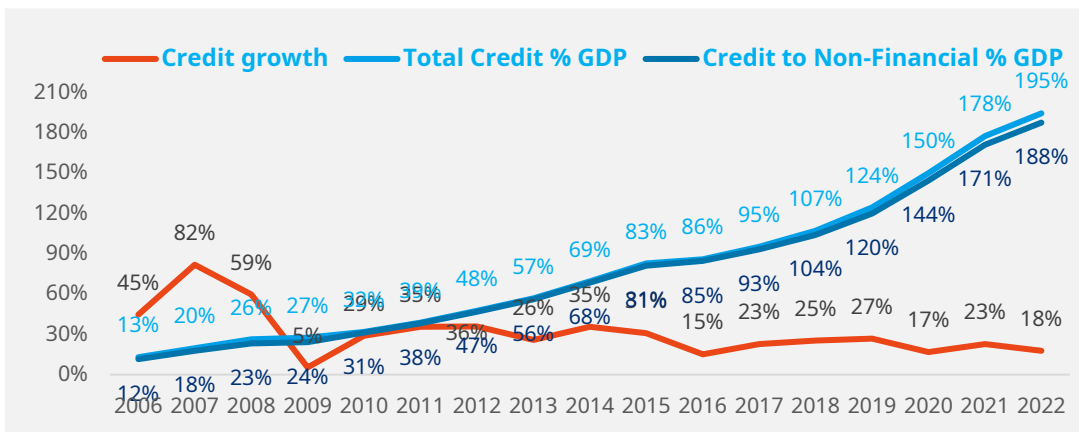
# RECENT DEVELOPMENTS AND ISSUES

- The Cambodian economy, impacted by weaker external demand due to global economic crisis, showed sharp decline in trades in the 1<sup>st</sup> half of this year. While such impact is partially offset by the gradual recovery of the tourism and service sectors, it seems less likely to meet the expected GDP growth of 5.8% in 2023. Property price has remained stagnant over the last 2 years due to COVID pandemic, rising interest rates, and absence of foreign investments.
- Banking and MF sectors are under acute stress with rising non-performing loans (PAR>30 ratio increased to 5% as of June 2023), higher funding cost, and timid increase in lending rates. The Total-credit-to-GDP ratio came close to 200% at the end of 2022, appearing to suggest a market saturation.



# OVERVIEW OF CAMBODIAN BANKING SECTOR

- 2006-2016 was the era of impressive growth due to the market under-penetration. The Total-Credit-to-GDP ratio grew from 13% in 2006 to 86% in 2016, while the deposit-to-GDP ratio increased from 19% to 88% during the same period. From 2016 until 2022, growth remained solid with the ratio reaching 195%.
- The number of banks, bank branches, borrowing and deposit accounts, have also seen staggering growth during the period.



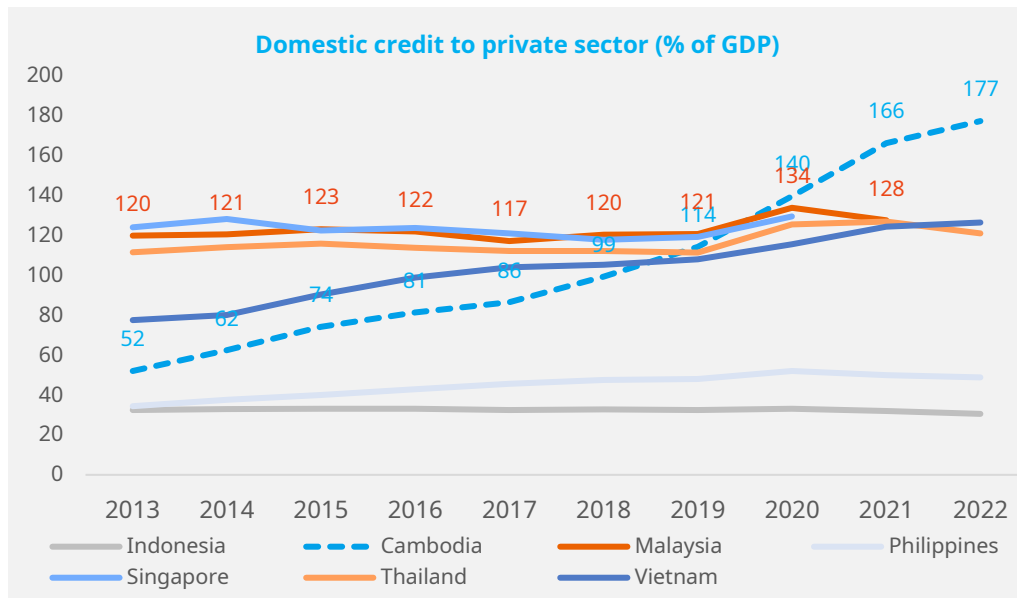
Source: NBC's Annual Supervision Report 2006-2022, YSC's Calculation

# IS CAMBODIAN BANKING SECTOR HIGHLY OVERSATURATED? (1/5)

- Cambodia's domestic-credit-to-private-sector-to-GDP ratio appears excessively greater than that of its ASEAN peers. However, it may be inappropriate to use the ratio as a comparable indicator to evaluate the overall indebtedness of an economy and make direct comparisons with other countries in the region for at least 3 reasons: (1) unlike other ASEAN countries where corporate bond markets play a crucial role in funding the private sector (e.g., in Thailand, non-financial entities and individuals hold more than 40% of corporate bonds outstanding), Cambodia's corporate bond market is almost non-existent; (2) the definition of the ratio is somewhat less clear-cut, because some countries may include credit to state-owned enterprises fully, partially, or not at all; (3) in more developed economies, other economic agents besides financial corporations, including general government, non-financial corporations, households, and overseas lenders are also significant sources of private sector debt.

## High credit to private sector % of GDP may indicate oversaturation

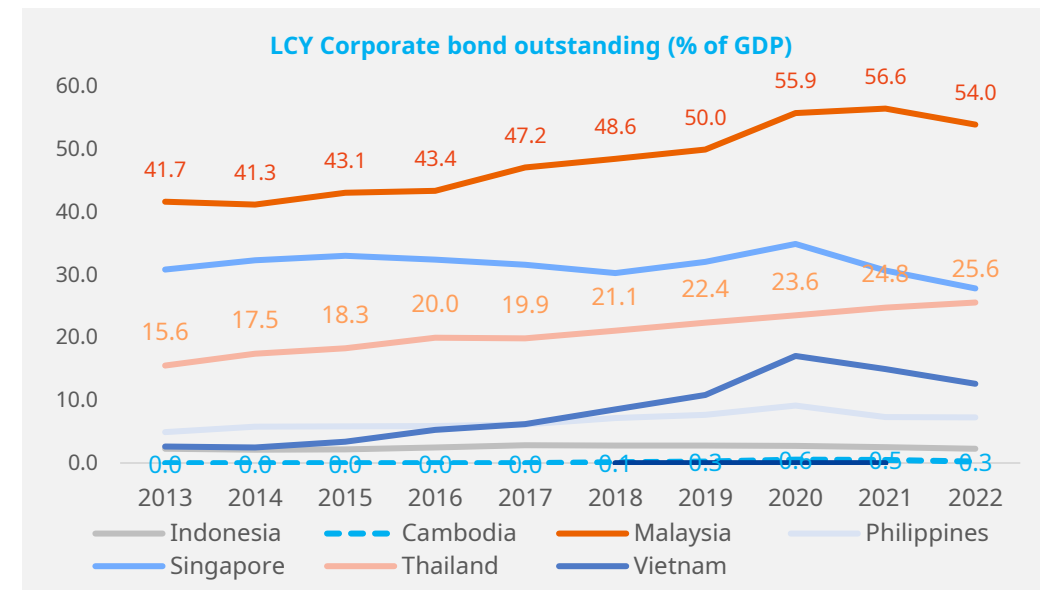
Domestic credit to private sector of Cambodia reached 177% of GDP by far surpassing ASEAN peers. Based on this indicator, Cambodian banking sector appears highly oversaturated.



Source: World Bank's WDI

## But corporate bond market remains under-developed

Private sector in other countries relies on not only bank/MFI loans but also debt financing from other channels, including the corporate bond market, in which households and non-financial corporations can be significant investors.

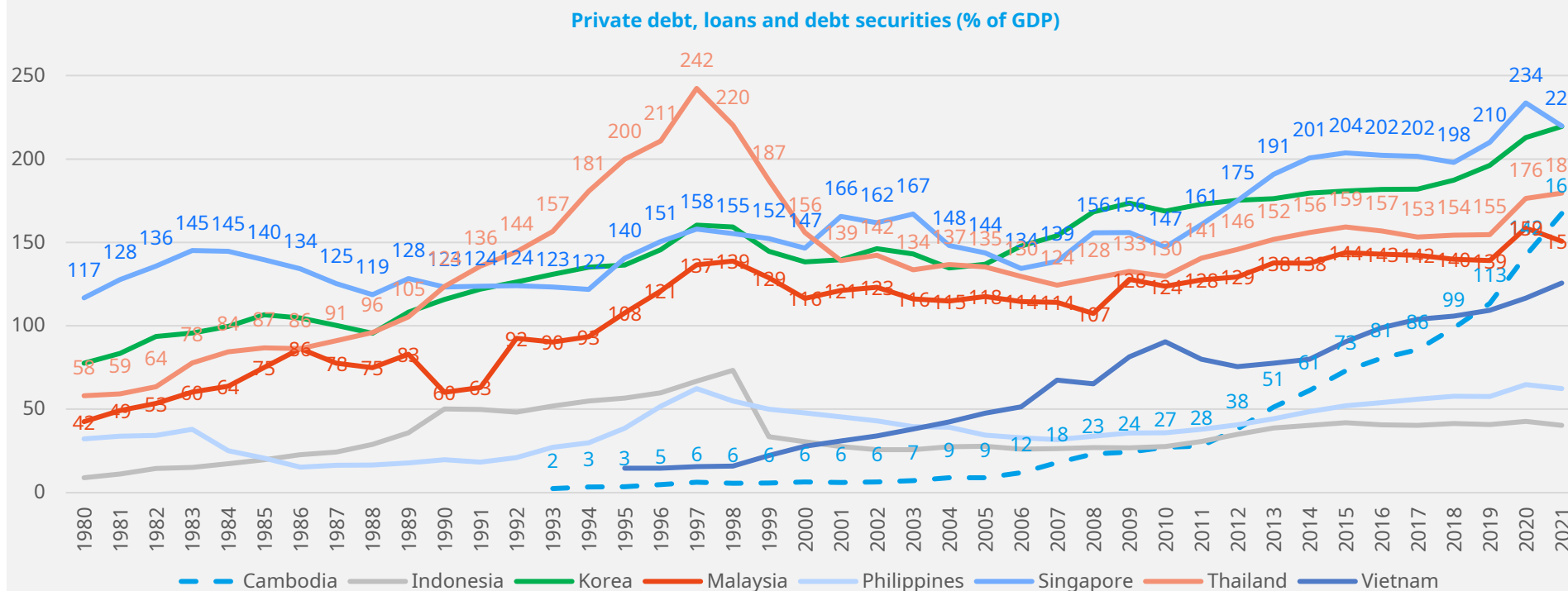


Source: Asian Bond Online

# IS CAMBODIAN BANKING SECTOR HIGHLY OVERSATURATED? (2/5)

- We believe the “private debt, loans and debt securities % of GDP” from the IMF is a better indicator for making valid comparisons across countries with varying levels of economic and financial development. This indicator represents the total stock of loans and debt securities issued by households and non-financial corporations as a proportion of nominal GDP. The definition of private debt includes debt provided not only by financial corporations but also by non-financial corporations, households, general government, and overseas lenders.
- As of 2021, Cambodia’s private sector debt % of GDP stood at 167%, which is lower than Thailand’s 180%, Korea’s and Singapore’s 220%.

Comparisons between peers in the region: IMF’s private debt, loans and debt securities (% of GDP)



Private debt, loans and debt securities (% of GDP) is total stock of loans and debt securities issued by households and non-financial corporations as a share of GDP

Source: IMF’s Global Debt Database

The private sector debt % of GDP of Indonesia and the Philippines are noticeably low and could be due to various reasons.

**Indonesia:**

(1) Lack of competition (oligopoly has led to high lending rates and impose deterrent to borrowers, in particular MSMEs) due to regulatory reforms in the post Asian financial crisis, in which Indonesia has had traumatic experience, and (2) the strict regulation of KYC, are listed as potential challenges to financial inclusion in Indonesia.

**Philippines:**

One problem facing the Philippines is the country’s archipelagic nature that create infrastructure gaps and imposes barrier to financial access.

Source: ADB’s Financial Inclusion in Asia: Country Surveys, 2014)

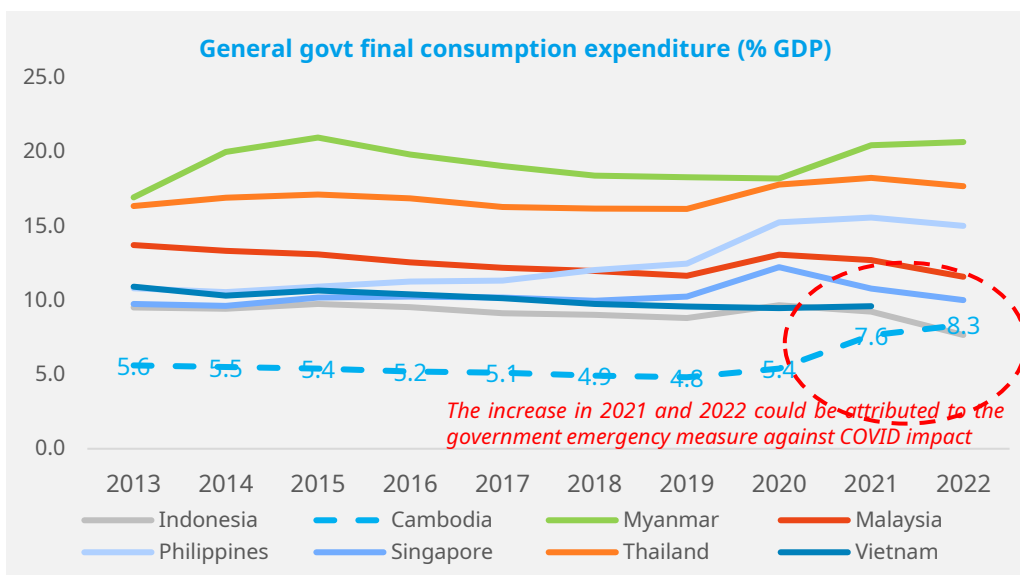


# IS CAMBODIAN BANKING SECTOR HIGHLY OVERSATURATED? (3/5)

- The relatively smaller government expenditure, leading to smaller GDP figures, also contributes to a higher private-sector-debt-to-GDP ratio for Cambodia. In Cambodia, government financial consumption expenditure % of GDP stood mostly below 5%, except in 2021 and 2022 (government emergency measures to mitigate the impact of COVID). This suggests that Cambodia's private sector contributes more to the GDP compared to other countries in the region.
- In addition, Cambodia has a much larger informal economy than most of its peers, which accounts for more than 40% of the GDP figure.
- By adjusting for the government final consumption expenditure and informal economy, we derive an indicator for a more reliable comparisons across economies with different level of development.

## Low GDP figure due to small govt consumption expenditure

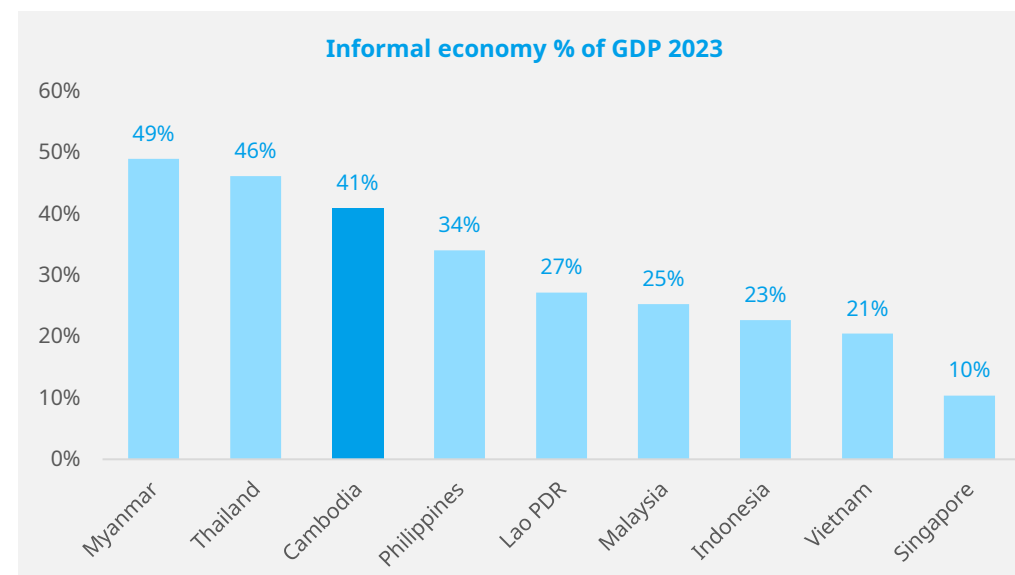
Cambodia has a very low government final consumption expenditure compared with its ASEAN peers. Cambodia's general government gross debt (% of GDP) was 36.5% in 2022, the lowest in ASEAN (exc. Brunei). Smaller government suggests bigger contribution of private sector to the economy.



Source: IMF's WEO April 2023

## Huge informal economy

Cambodia's informal economy accounts for more than 40% of the GDP, the 3<sup>rd</sup> highest in ASEAN, which is not fully reflected in the GDP figure.



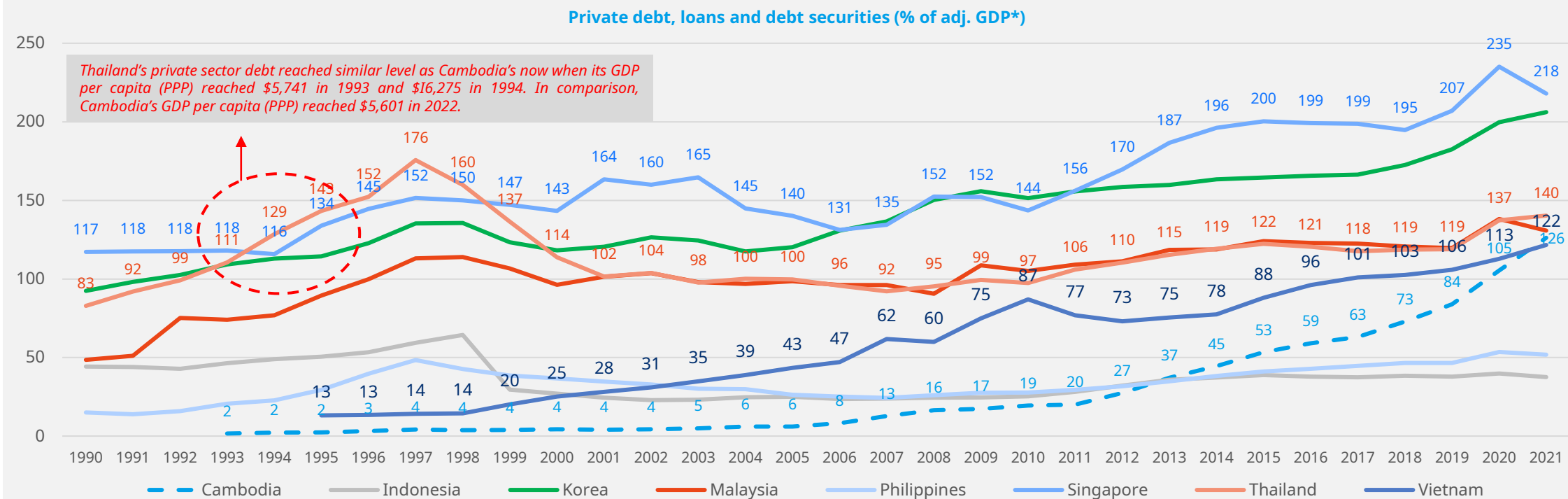
Source: Quarterly Informal Economy Survey (QIES) by World Economics



# IS CAMBODIAN BANKING SECTOR HIGHLY OVERSATURATED? (4/5)

- After factoring in (1) government final consumption expenditure and (2) the informal economy, we have derived a more relevant and comparable measure across different economies. The adjusted indicator below shows that Cambodia's level of private sector debt remains relatively lower when compared to more advanced economies such as Malaysia, Singapore, and South Korea. However, we also note that Cambodia has experienced much more rapid growth over the past several years.
- Interestingly, Thailand reached a similar level of private sector debt in 1994 when its GDP per capita PPP was at a level comparable to Cambodia's in 2022. Purely drawing from the case of Thailand in early 1990s, Cambodia may exercise caution against further overheating in private sector debt to avoid potential downward corrections in the future.

## Cambodia's level of private sector debt is still relatively lower compared to more advanced economies



\*Adj. GDP = GDP less government final consumption expenditure and plus informal economy

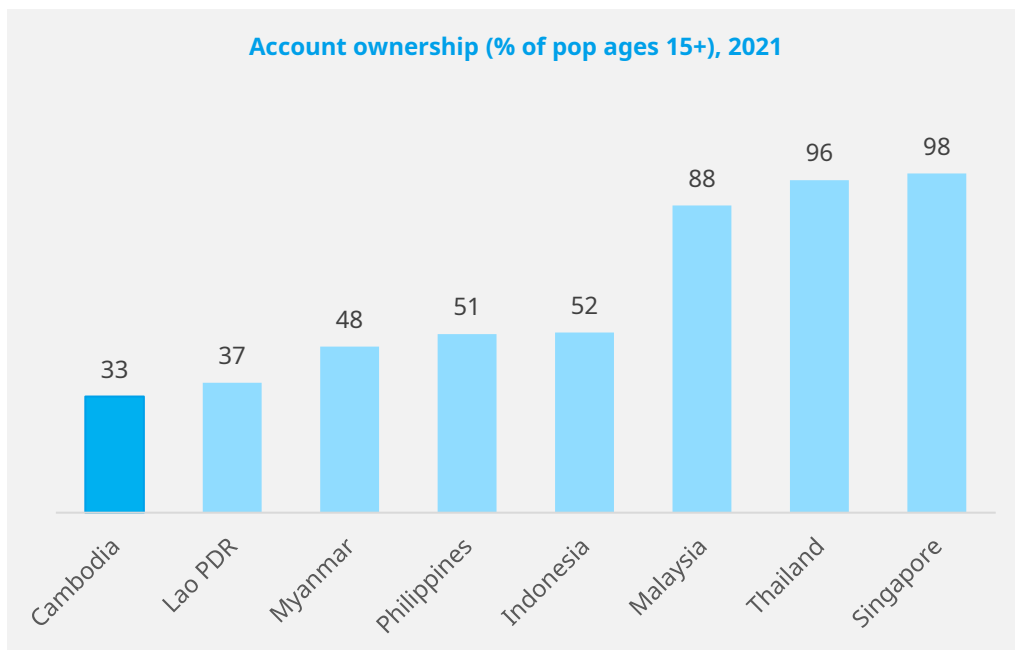
Source: IMF's Global Debt Database, World Economics, YSC's Calculation

# IS CAMBODIAN BANKING SECTOR HIGHLY OVERSATURATED? (5/5)

- Other indicators, including the percentage of adult population with account ownership and the number of ATMs per 100,000, seem to suggest that Cambodia's banking and financial sector remains under-penetrated compared to the Kingdom's regional peers.

## Low percentage of account ownership despite total number of a/c

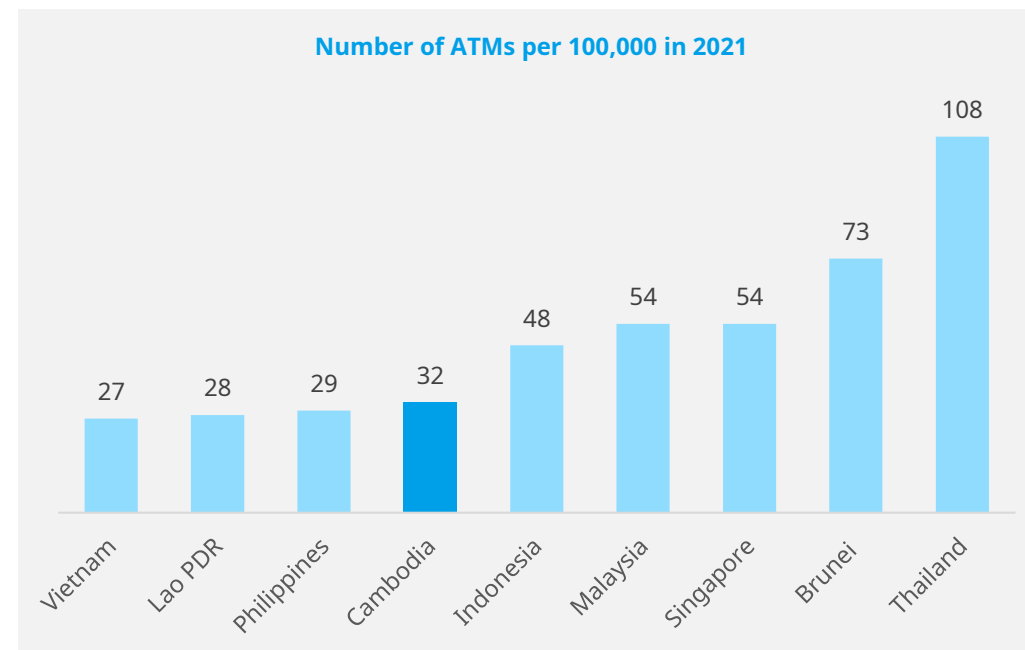
The number of account ownership at banks or mobile-money-service providers stood at 33% of population aged 15+ in 2021, which is significantly lower compared to ASEAN peers. The total number of 12.68 million accounts may have counted the multiple accounts owned by a single person.



Source: WDI

## Number of ATMs per 100,000 is lower compared to peers

The number of ATMs per 100,000 in 2021 was 32, which is still lower than most ASEAN peers.



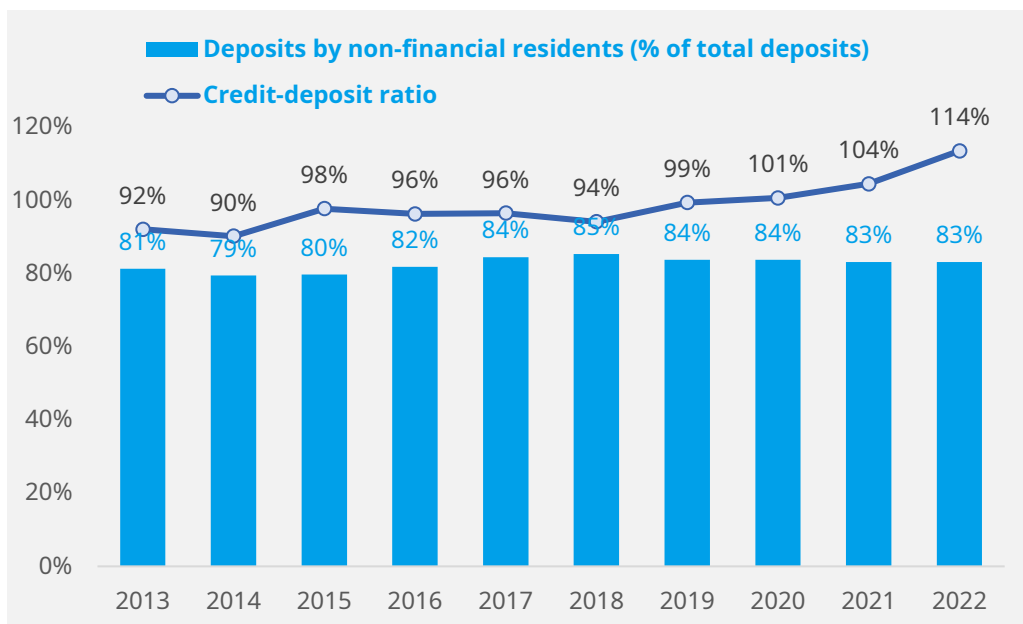
Source: WDI

# CREDIT PENETRATION IS BACKED BY DOMESTIC WEALTH

- Credit offered by banks and MFIs in Cambodia has been almost sufficiently financed by deposits, with a significant portion of these deposits (more than 80%) coming from non-financial resident depositors. This suggests that high credit penetration is backed by a rapidly growing domestic wealth.
- In addition to deposits, the major stock of Cambodian people’s wealth is tied to land and properties they own. While the value of these assets may fluctuate from time to time, including occasional share changes, in the long run, they are expected to appreciate, particularly in developing countries like Cambodia, contributing to further accumulation of domestic wealth.

## Credit is backed by deposits of non-financial resident depositors

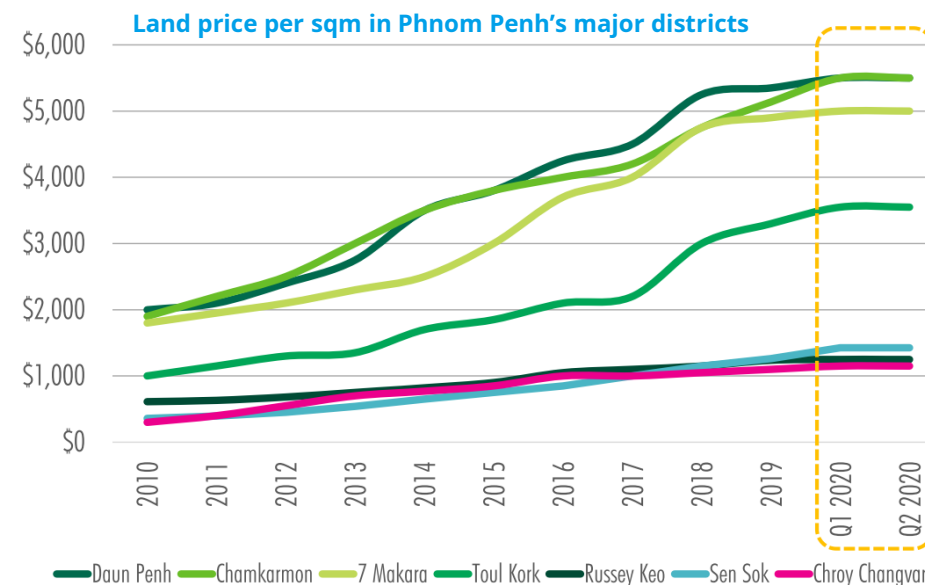
Despite high credit growth, the credit have been almost sufficiently financed by deposits. In addition, more than 80% of deposits have been made by non-financial residents, suggesting that credit offered by banks and MFIs are backed mostly by domestic wealth.



Source: NBC, YSC's Calculation

## Credit is also backed by increasing properties value

Although fluctuating from time to time, sometimes even sharply, property value in general will continue to appreciate in developing countries like Cambodia serving as important part of domestic wealth that supports the increasing credit penetration.



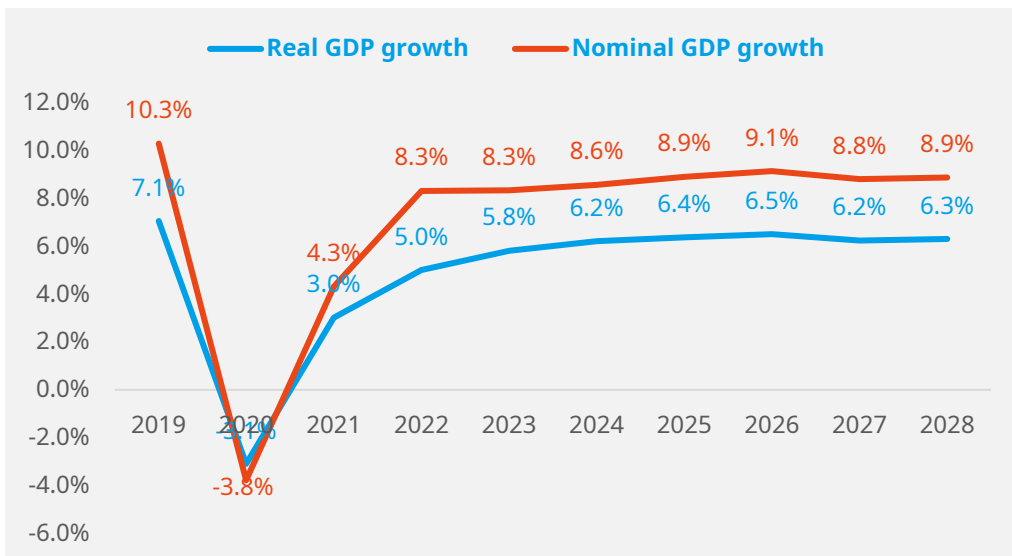
Source: CBRE

# WHERE IS LOCAL BANKING SECTOR HEADING TO?

- The Cambodian GDP growth in 2023 is likely to be affected by global headwinds and may fall short of IMF’s estimated 5.8% growth. However, there are some positive signs of partial recovery in the tourism and service sectors post-COVID. As the global economic recovery begins, it is likely return to over 6% in real rate and 9% in nominal rate.
- Despite the seemingly high credit-to-GDP ratio, Cambodia may maintain the ratio at 142% in the future while achieving a double-digit credit growth of 10% over the next five years followed by 7% growth from 2029 onwards; aligning with the expected nominal GDP growth rate (expected real GDP rate of 5% + inflation rate 2%).

## GDP real growth to gradually recover to over 6%

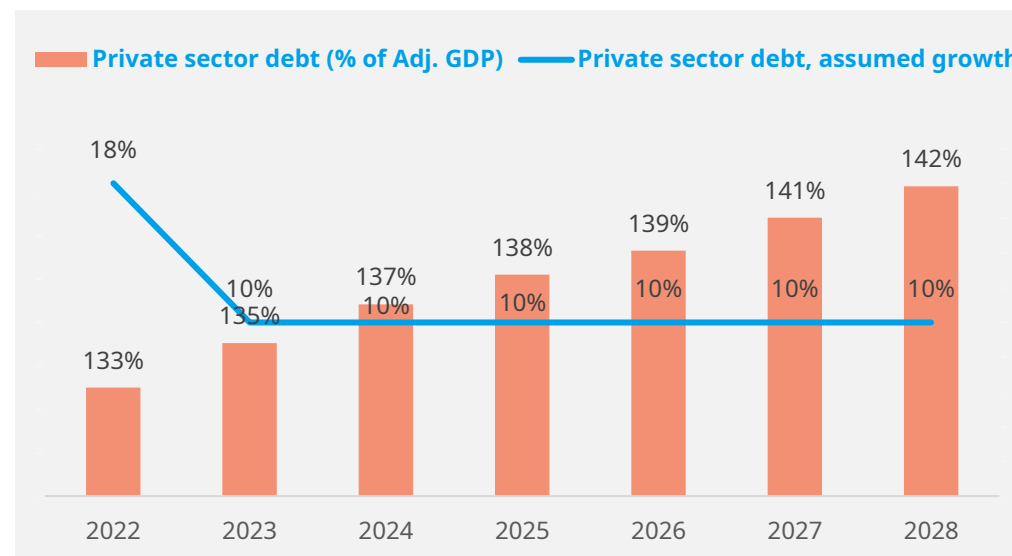
- In 2023, despite the weak external demand (slowdown or decline in exports) due to the global economic slowdown, the growth is expected to recover led by the tourism and service sectors.
- Real GDP growth is forecasted to return to 6.0% from 2024 to 2028, according to IMF forecast with the nominal GDP growth will be close to 9% during the same period.



Source: IMF's WEO April 2023

## Double-digit growth in next 5 years is still viable

- Based on the adjusted ratio, the private sector debt (% GDP + informal economy less govt. final consumption expenditure) stood at around 133% in 2022, compared to Thailand’s 140% (2021), Singapore’s 218% (2021) and Malaysia’s 131% (2021).
- Cambodia may maintain the ratio at 142% (around Thailand’s) while achieving 10% credit growth for the next 5 years followed by 7% growth from 2029 onward, the same level as the expected nominal GDP growth.



Source: YSC's Calculation

# APPENDIX: INDICATORS' DEFINITION COMPARISON

	Domestic Credit to Private Sector (% of GDP)	Private Debt, loans and securities (% of GDP)	Private Debt, loans and securities (% of adj. GDP)
<b>Private Debt Definition</b>			
<b>Borrowers</b>			
Non-Financial Corporations			
Private non-financial corporations	X	X	X
Public non-financial corporations	?	-	-
Households	X	X	X
Non-profit institutions serving households	?	X	X
Financial Corporations	-	-	-
<b>Lenders</b>			
Financial Corporations	X	X	X
Non-Financial Corporations	-	X	X
General Government	-	X	X
Households	-	X	X
Non-profit institutions serving households	-	X	X
Rest of the world (cross-border)	-	X	X
<b>Instruments</b>			
Debt securities	X	X	X
Loans	X	X	X
Trade credits	X	-	-
Other account receivables	X	-	-
<b>GDP definition</b>			
Household final consumption expenditure	X	X	X
Investment	X	X	X
Government final consumption expenditure	X	X	-
Net exports	X	X	X
Informal economy	-	-	X

X	Include
-	Exclude
?	Not clear

Not clear for the "domestic credit to private sector" definition as some countries may include fully or partially or not at all the credit to state-owned enterprises

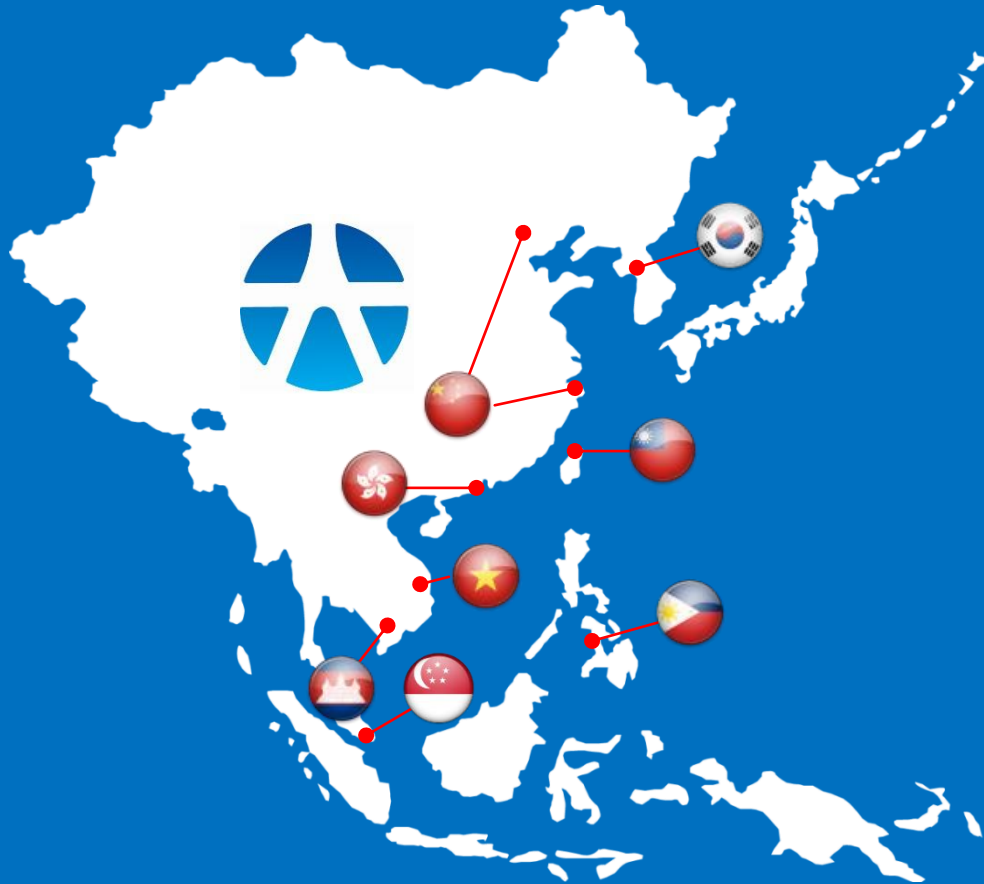
While these are not significant sources of private sector debt in lower-middle income countries like Cambodia, they are quite significant in more developed economies.

Trade credit & other account receivables from financial corporations to non-financial corporations are far from significant

Private sector contributes more to the GDP in countries with smaller government

Developing economies tend to have a huge informal economy, which should be considered

Source: IMF's Global Debt Database, World Bank's Metadata Glossary



# We Know Asia

Thank you

## CONTACT US



4th Fl, Emerald Building, No 64 (Corner St 178)  
Preah Norodom Blvd, Phnom Penh  
Cambodia



[www.yuantacambodia.com.kh](http://www.yuantacambodia.com.kh)



[cf@yantacambodia.com.kh](mailto:cf@yantacambodia.com.kh)

+855 (0)23 860 800 / 804