Yuanta Securities

Cambodia's Banking Industry: Why Size Matters

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Yuanta Securities

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001 Introduction

INTRODUCTION

- Cambodia’s banking sector has experienced **rapid expansion**, with the number of commercial banks reaching **59** as of December 2024. While this growth has significantly contributed to **financial inclusion**, it has also led to increased **market fragmentation**, **operational inefficiencies**, and heightened **financial risks**.
- In 2024, the **Top 5 banks** in Cambodia account for **49%** of total banking assets, a decline from **52%** in 2018, reflecting the rise of **smaller competitors**. However, many of these smaller banks face significant challenges related to **cost efficiency**, **risk management**, and **sustainable growth**. These challenges often arise from **high loan-to-deposit ratios**, reliance on **external borrowing**, and a rise in **non-performing loans (NPLs)**. This report analyzes Cambodia’s banking sector, highlighting both its structural challenges and the strategic opportunity for **consolidation** to enhance **efficiency**, **stability**, and **resilience**.
- The primary objective of this report is to provide a **data-driven analysis** of the banking sector and to offer **strategic recommendations** to improve its structure and competitiveness. The insights are particularly relevant to:
    - **Banks:** The report outlines how **consolidation** through mergers and acquisitions (M&A) can help banks **optimize operations**, achieve **economies of scale**, improve **risk management**, enhance **financial stability**, and increase **profitability** in the face of increasing **market fragmentation**.
    - **Relevant stakeholders:** For **NBC,** the report highlights the **risks** associated with the **fragmented banking system** and provides recommendations to facilitate **consolidation.** The report suggest how strategic **policy adjustments**—such as **incentives for M&A** and **relaxed regulatory requirements** during consolidation—could enhance **financial stability**, **reduce systemic risk**, and improve the **overall health** of the Cambodian banking sector.
- This report seeks to answer the following key questions:

☑ What are the **risks** and **inefficiencies** associated with a **fragmented banking system**?

☑ How does **bank size** influence **financial stability**, **lending capacity**, and **cost efficiency**?

☑ What lessons can Cambodia learn from global **banking consolidation strategies?**

☑ What **policy measures** and **incentives** can support **responsible M&A** in the sector?

002 Why Bank Size Matters

ADDRESSING AN OVERCROWDED BANKING SYSTEM

- Cambodia's banking sector remains fragmented, with numerous small banks creating inefficiencies and high operational costs that hinder long-term growth. Consolidation into larger, well-capitalized institutions is essential to improve efficiency, stability, and support the broader economic development of the country.

Fragmentation and Challenges in Cambodia's Banking Sector

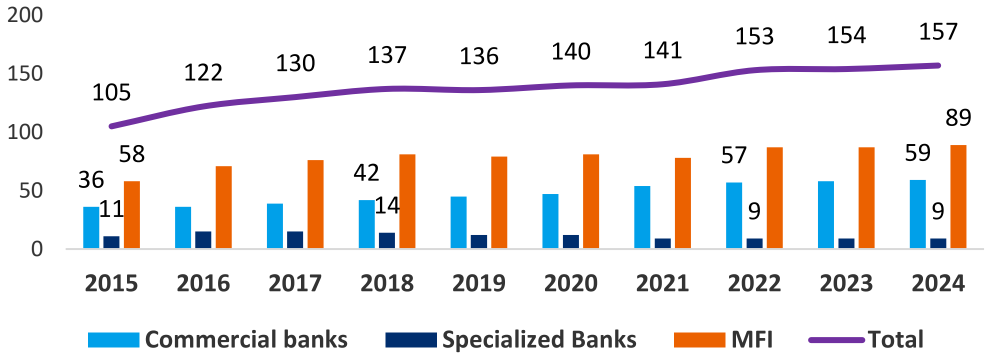
- Emerging markets often experience highly **overcrowded banking system**, dominated by numerous **small banks**. While this structure promotes **consumer choice** and foster **competition**, it also leads to **inefficiencies**, **high operational costs**, and **challenges** that hinder the sector’s ability to contribute to broader **economic growth**.

- The share of total assets held by the Top 5 banks decreased from **52% in 2018 to 46% in 2022**, due to a significant increase in the number of commercial banks, which grew **from 42 to 57** during this period. This trend highlights a further **fragmentation of the market**, with the growing presence of smaller banks creating a **highly competitive environment**. However, this also introduces challenges such as **high costs**, **operational inefficiencies**, and a **lack of economies of scale**—factors that are critical for long-term growth and stability in the banking sector. As the growth in the number of banks has slowed, the share of the **Top 5 banks increased to 49% in both 2023 and 2024**, which indicate that smaller banks are **struggling to grow due** to their **lower competitiveness** compared to the larger banks.

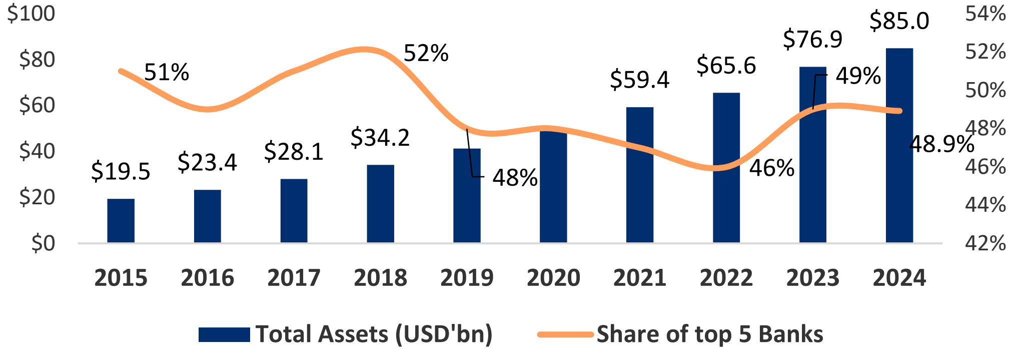
Strategic Implication:

a) To improve **efficiency**, **resilience**, and **long-term sustainability**, a more **consolidated banking sector** with **larger, well-capitalized institutions** is crucial. Strengthening the **asset bases** of these banks can drive **cost efficiencies**, enhance **risk management**, and promote **economic stability**. This, in turn, will reinforce the sector’s capacity to support **broader economic development** goals in Cambodia.

Financial Institutions in Cambodia



Banking Sector Total Assets



Source: NBC and YSC Research

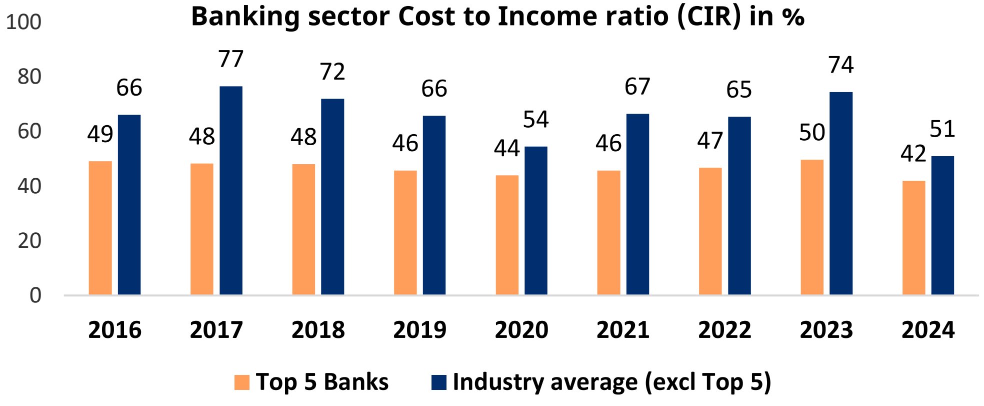
***Top 5 banks =** are banks with the highest total assets at the end of each FY between 2015 to 2023

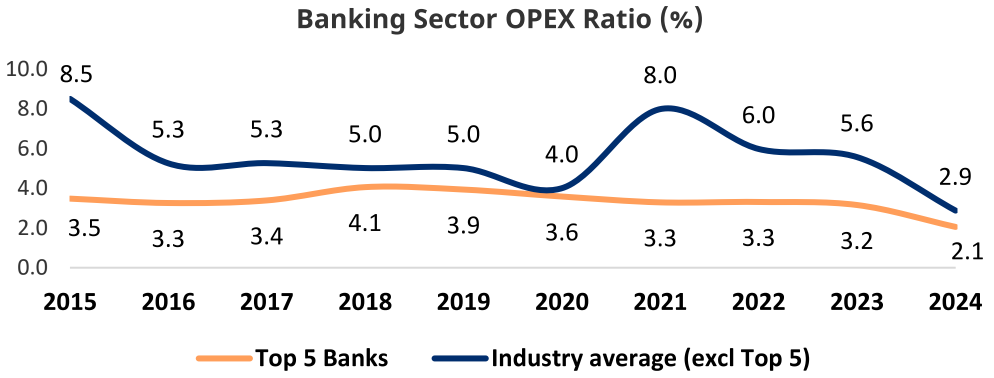
ENHANCING OPERATIONAL EFFICIENCY (1/2)

- Larger banks in Cambodia benefit from economies of scale, achieving better operational efficiency and profitability compared to smaller banks, which face higher cost pressures and inefficiencies. Consolidation could help reduce operating costs, improve profitability, and enable banks to invest in digital transformation and risk management, ultimately strengthening the sector's resilience and competitiveness.

Operational Efficiency and Profitability in Cambodia's Banking Sector (1/2)

- Larger banks benefit from **economies of scale**, spreading **fixed costs** over a broader asset base to achieve **greater operational efficiency** even in the wake of global headwinds. In contrast, smaller banks face higher **cost pressures**, impacting **profitability** and **competitiveness**.
- **From 2016 to 2023**, Cambodia's Top 5 banks consistently outperformed smaller peers in operational efficiency, maintaining an average **CIR** of **47%**, compared to **66%** for smaller banks—highlighting a notable gap in profitability and cost management. During the same period, the **average OPEX ratio** stood at **3.4%** for the Top-tier banks, while smaller banks reported a higher average of **5.8%**.
- **In 2024**, both the CIR and OPEX ratios for the Top 5 banks and the broader industry **dropped significantly** as banks have increasingly turned to **cost rationalization strategies**, aiming to **preserve margins** and enhance **resilience** in a more challenging **macroeconomic environment**.
- The smaller banks' inability to achieve the same **economies of scale** as the Top 5 banks results in **higher operating costs relative to the size of their balance sheets**. This disparity highlights the **substantial pressure** on smaller banks' profitability.
- The consequences of these **inefficiencies** are evident where larger and mid-sized banks in Cambodia consistently **outperform smaller banks in profitability**, benefiting from **economies of scale**, **cost control**, and **stronger brand positioning**.





Source: NBC and YSC Research

***Cost-to-income ratio (CIR)** = Operating expenses / Operating income (net interest income + non-interest income)
***Operating expense (OPEX) ratio** = Operating expenses / Average interest earning assets
***Industry average =** is the average of all the commercial banks excluding the Top 5 banks

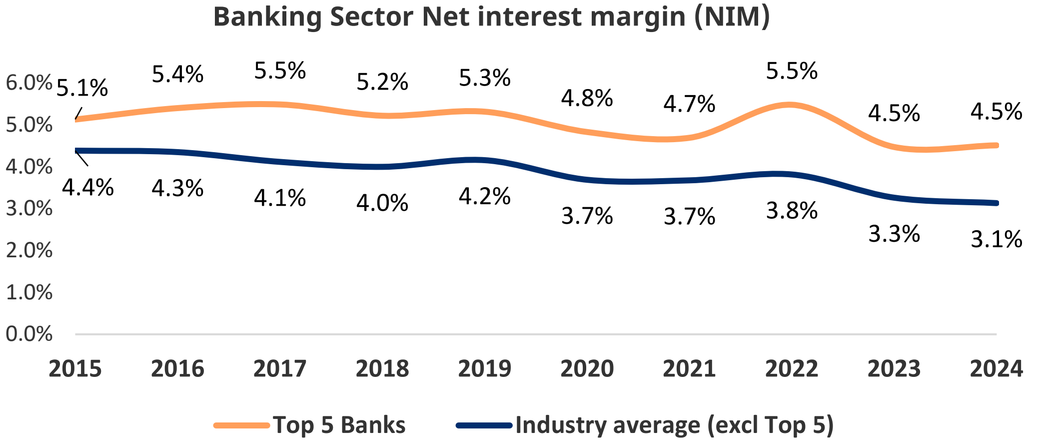
ENHANCING OPERATIONAL EFFICIENCY (2/2)

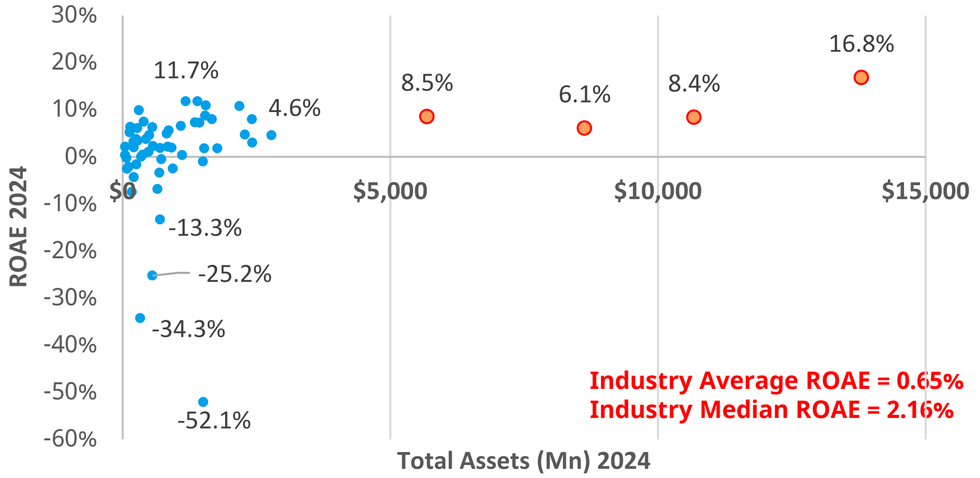
Operational Efficiency and Profitability in Cambodia's Banking Sector (2/2)

- For instance in 2024**,** the **Top 5 banks** had demonstrated a significantly stronger financial performance relative to the broader industry. The group reported an average **NIM of 4.5%**, outperforming the **industry average of 3.1%** by **143 basis points**.
- Moreover, the Top 5 banks in 2024 recorded an average **return on average equity (ROAE) of 8.9%**, markedly higher than the **industry average ROAE of 0.7%** and a **median of 2.2%**. This stark divergence highlights the **superior profitability** and **operational resilience** of the leading banks, particularly in a year characterized by macroeconomic pressures and sector-wide margin compression.
- Smaller banks, facing challenges **beyond scale**, struggle to match this performance, highlighting their **vulnerability to economic pressures**. While larger banks are **not immune to difficulties**, but their size and stability enable them to better navigate adverse conditions.
- **While sector fragmentation fosters competition**, it also presents structural inefficiencies, reducing **overall banking sector resilience, competitiveness and profitability**.

Strategic Implication:

a) Banking consolidation could help **reduce operational costs**, enabling banks to invest in **digital transformation**, **risk management systems**, **expanded lending capacity**, and ultimately **enhanced profitability**.





Source: NBC and YSC Research

***Net interest margin (NIM)** = Net interest income / Average interest earning assets
***Return on average equity (ROAE)** = Bank's net income / Average shareholders equity
***Industry average =** is the average of all the commercial banks excluding the Top 5 banks

LIQUIDITY AND FUNDING ADVANTAGES (1/2)

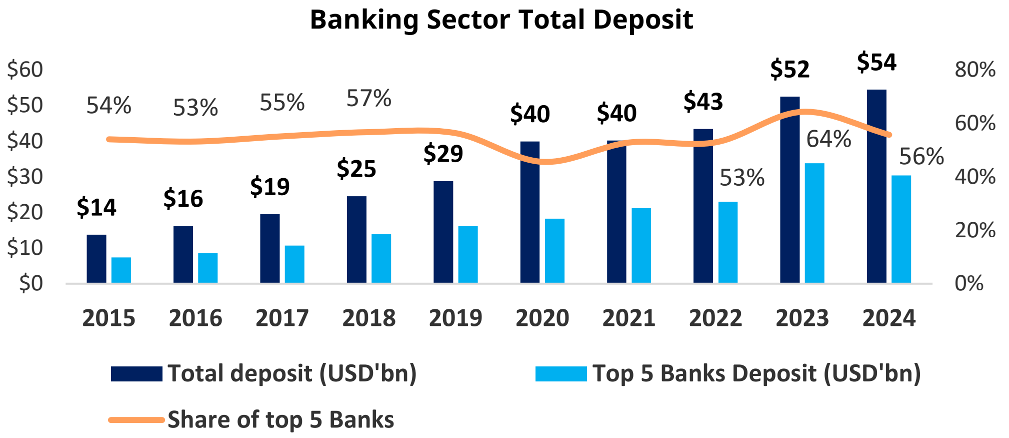
- The Top 5 banks in Cambodia dominate the deposit market, capturing on average 55% of total deposits between 2015 and 2024, benefiting from stable funding and lower lending costs compared to smaller banks, which rely heavily on non-deposit funding. Smaller banks' high leverage and elevated LTD ratios exacerbate financial instability, while consolidation with larger, well-capitalized banks can improve funding stability, efficiency, and overall financial resilience, strengthen the banking sector and support long-term economic stability.

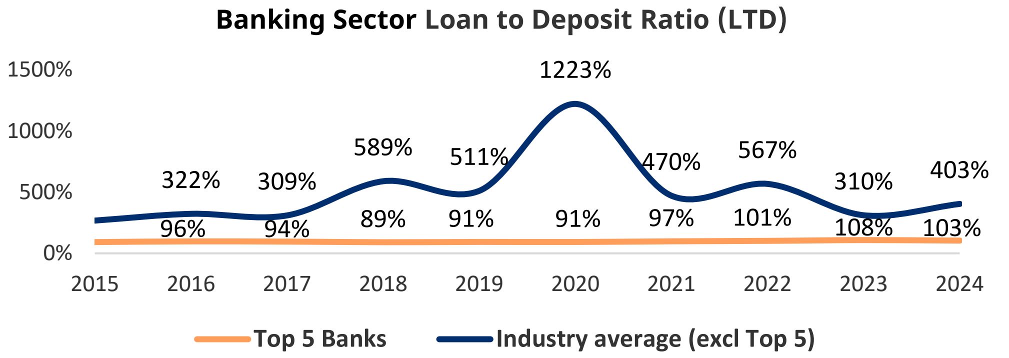
Liquidity and Funding Dynamics in Cambodia's Banking Sector (1/2)

- The **Top 5 banks** in Cambodia have consistently captured an average of **55%** of total banking deposits between 2015 and 2024, reaching **64%** in 2023. This trend highlights that larger banks are well-positioned to attract deposits from a broad **customer base**, benefiting from their extensive **branch networks**, strong **online presence**, and ability to serve diverse customer needs. This broad deposit base provides them with **cheaper funds**, lowering their **lending costs** and enhancing their financial position.

- Between **2015 and 2024**, the **Top 5 banks** maintained an average **LTD ratio** of **96%**, while the industry-wide LTD ratio over same period is **497%**, peaking at **1,223%** in 2020. This reflects the **excessive reliance** on **non-deposit funding** by smaller banks**.**

- These shifts indicate a growing reliance on non-deposit borrowing, with **total bank borrowings** increasing at **a CAGR of 18%**, reaching **$15.48 billion in 2024.** Of this total, **69% originates from smaller banks**, while the Top five banks account for only 31%. This trend exposes the sector, particularly smaller banks, to significant liquidity risks. However, some smaller banks' borrowings are medium- to long-term loans from either the **parent company or shareholders**, which **helps mitigate liquidity risk**. This presents a **unique market situation** in Cambodia. Nevertheless, there is a pressing need for **improved liquidity risk management**, **diversified funding sources**, and **stronger regulatory oversight** to ensure the **long-term financial stability** of Cambodia's banking sector.





Source: NBC and YSC Research

***Loan to Deposit (LTD) ratio** = the ratio of total loans to total deposits
***Industry average =** is the average of all the commercial banks excluding the Top 5 banks

LIQUIDITY AND FUNDING ADVANTAGES (2/2)

Liquidity and Funding Dynamics in Cambodia's Banking Sector (2/2)

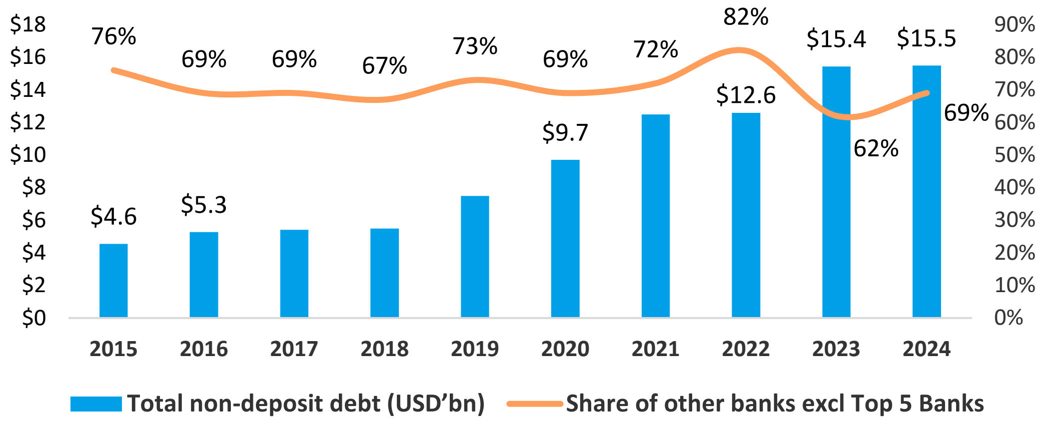
- High leverage and elevated LTD ratios pose considerable risks, as **non-performing loans (NPLs)** can push highly leveraged banks into further borrowing, exacerbating **financial instability**. Between **2018 and 2024**, the reliance of other banks (excluding the Top 5 banks) on **borrowed funds** increased from **18%** to **27%** of total assets in 2022 and to **25% of total assets in 2024**, raising **funding costs** and increasing **market vulnerability**. Unlike customer deposits, these borrowings are **costlier** and more **volatile**, which **erodes profitability.**

- In contrast, the **Top 5 banks** reduced their reliance on borrowed funds from **25%** of total assets in **2015** to **15%** in **2024**, strengthening their **funding stability** through **customer deposits**. This allowed them to ensure **greater liquidity** and **lower risk exposure**, contributing to their superior performance in terms of **profitability** and **financial resilience**.

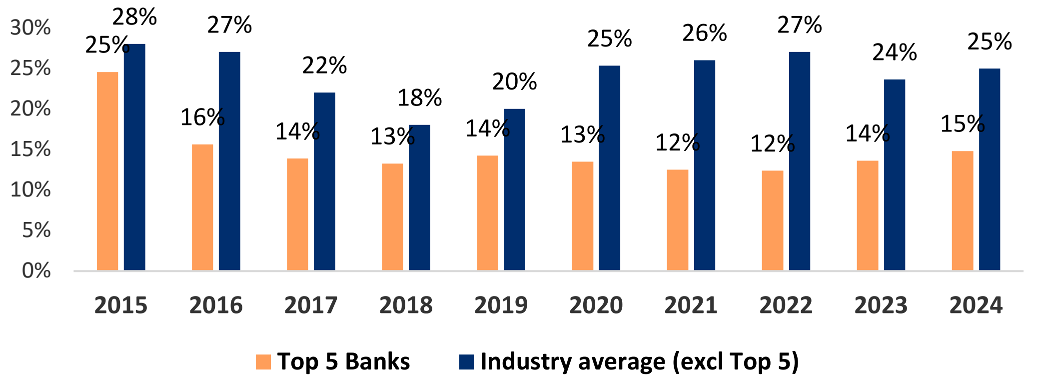
Strategic Implication:

a) **Smaller banks** are more vulnerable to rising **interest rates** and **borrowing costs**, which compresses their **profitability**.
b) **Larger banks**, with more **stable funding structures**, can offer more **competitive lending rates** and carry **lower financial risk**.
c) A more **consolidated banking sector**, led by well-capitalized larger banks, is critical to enhancing **risk distribution**, improve **efficiency**, and strengthen **Cambodia's financial system**, fostering long-term economic stability.

Banking sector non-deposit debt (USD'bn)



Total non-deposit debt as % of total assets



Source: NBC and YSC Research

***Industry average =** is the average of all the commercial banks excluding the Top 5 banks

STRENGTHENING RISK MANAGEMENT

- Cambodia's credit market has grown rapidly, with a CAGR of 20% between 2015 and 2024, reaching $61.5 billion in total credit, but concerns over underwriting standards and sustainability persist. Rising NPL ratios among smaller banks, coupled with weak capital buffers and limited risk diversification, create significant systemic risks, highlighting the need for consolidation to strengthen the sector's resilience and improve financial stability.

Risk Management and Systemic Stability in Cambodia's Banking Sector

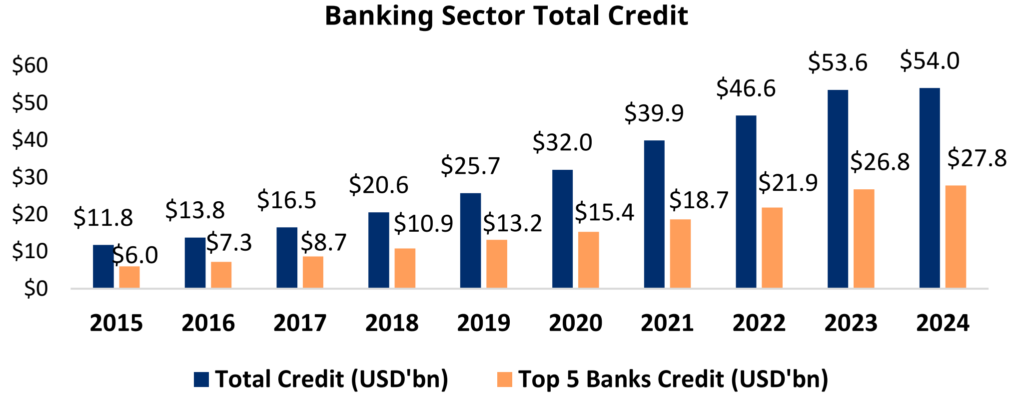
- Cambodia's credit market has grown significantly, with a **CAGR of 20%** between **2015 to 2024**, reaching **$61.5 billion** in total credit by 2024. The **Top five banks** control about **50%** of this market, indicating strong demand and their dominant role. However, despite their large share of the market, smaller banks are reporting **higher NPL ratios** than the Top five, raising concerns about their **underwriting standards** and the **long-term stability** of both the banking sector and the credit market.

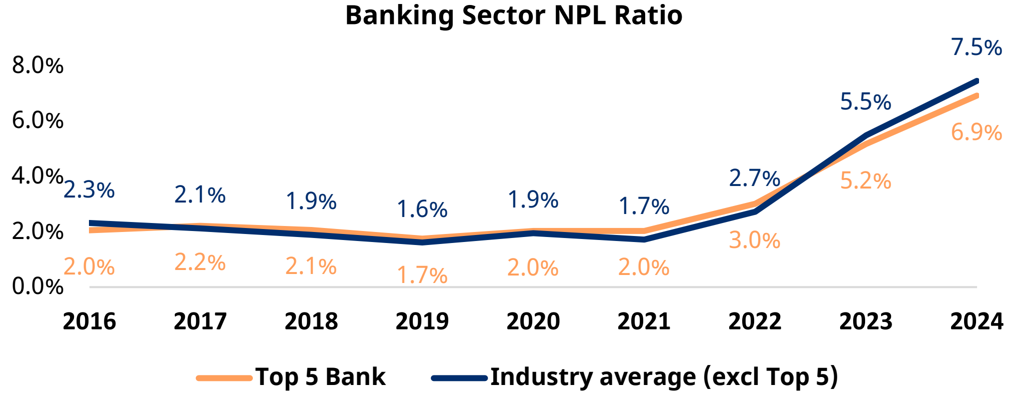
- For example, in **2024**, the **average NPL ratio** among the **Top 5 banks** was **6.9%**. In comparison, **smaller banks** reported a much higher **NPL ratio of 7.5%** in **2024** (with some individual banks NPL exceeding **36%**). These banks' **limited capital buffers** and lack of sufficient **risk diversification** make them more vulnerable to **financial instability**.

- The combination of **rapid loan growth**, **rising NPLs**, and weaker **risk resilience** among smaller banks creates a significant **systemic risk**. In the event of an economic downturn, distress in a few institutions could erode **market confidence** and lead to **liquidity strain** across the entire sector.

Strategic Implication:

a) A **fragmented banking system** heightens **systemic risk**, as weaker banks may struggle with **capital adequacy** and **loan losses**. A more **consolidated system** with stronger **capitalized banks** would be better positioned to absorb **economic shocks** and provide greater **financial stability**, reducing sector-wide vulnerabilities.





Source: NBC and YSC Research

BRAND RECOGNITION AND PUBLIC TRUST

- Larger banks in Cambodia benefit from strong brand recognition and public trust, leading to increased deposits and low-cost funding, supported by their extensive branch and ATM network. This infrastructure not only enhances market reach and customer convenience, but also improves operational efficiency, positioning these banks as key players in driving financial inclusion and economic growth.

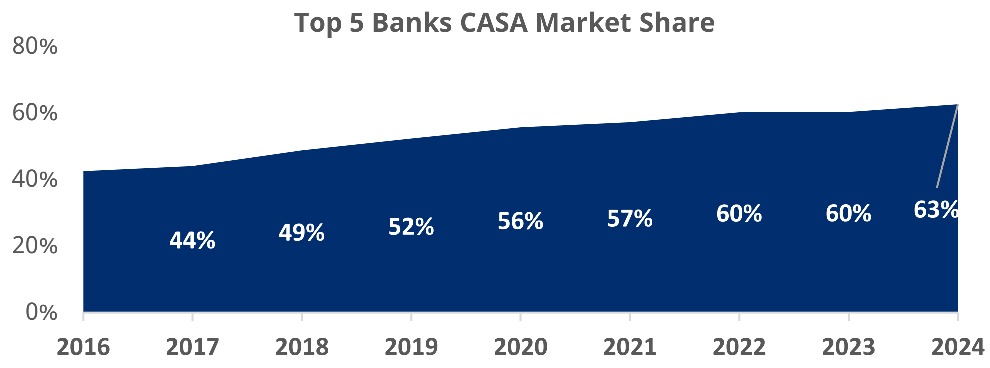
Brand Recognition, Dominance and Trust

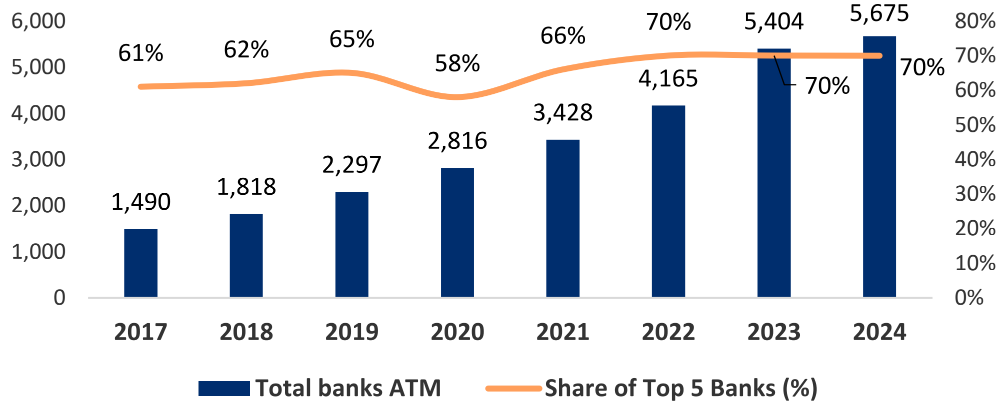
- Larger banks benefit from strong **brand recognition** and **public trust**, particularly during periods of **economic uncertainty**. Customers tend to view these banks as more **stable**, leading to a greater preference for depositing funds, which in turn enables these banks to secure **low-cost funding**.
- The dominance of the top five banks is evident in key operational metrics:
  - The top 5 banks hold **over 62%** of the **CASA market** in 2024.
  - Controlling **46%** of Cambodia's **1,745 branches**, enhancing their **market reach**.
  - These banks operate **70%** of the country's **5,675 ATMs** across **25 provinces**, which strengthens **accessibility** and **customer convenience**.
- This extensive **infrastructure** attracts more deposits, improves **operational efficiency**, and reinforces **financial stability**, positioning **larger banks** as key players in Cambodia's banking sector.

Strategic Implication:

a) **Increased accessibility and financial inclusion**: Larger banks would expand the branch and ATM network, improving access to banking services and fostering financial inclusion in underserved areas.

b) **Support for economic growth and infrastructure development**: Larger banks are better equipped to fund large-scale infrastructure projects, driving economic development and business growth.





Source: NBC and YSC Research

DRIVING TECHNOLOGY AND INNOVATION

- Larger banks in Cambodia leverage advanced technologies like blockchain, AI, and data analytics to drive efficiency, security, and customer experience, strengthening their market leadership. Their dominance in digital payment adoption and technological innovation enhances financial inclusion and positions them as key drivers of Cambodia's digital banking transformation, boosting the fintech sector and attracting global partnerships.

Technological Leadership and Innovation in Cambodia's Banking Sector

- Larger banks in Cambodia leverage **financial resources** to invest in cutting-edge technologies such as **blockchain**, **AI**, and **data analytics**, driving improvements in **efficiency**, **security**, and **customer experience**. Their ability to innovate at scale strengthens their **competitive position** and reinforces their **market leadership**.
- A **2023 survey** by Cambodia Development Resource Institute (CDRI) on **MSME digital payment adoption** showed that the **Top 5 banks** ranked among the **Top ten most-used digital payment applications**, reflecting their dominance in Cambodia's rapidly evolving **fintech** and **digital banking sectors**.
- This technological advantage boosts **customer trust**, accelerates **financial inclusion**, and enhances **operational resilience**, positioning larger banks as key drivers of **digital transformation** in Cambodia's banking sector.

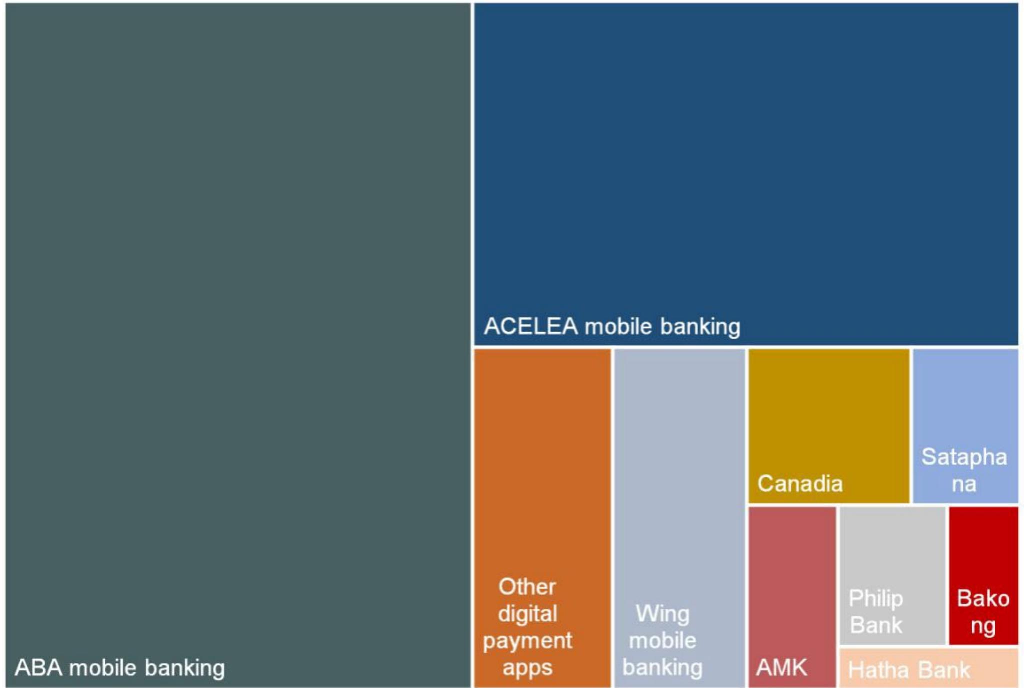
Strategic Implication:

a) **Enhanced technological innovation: L**arger banks would enable greater investment in **blockchain**, **AI**, and **data analytics**, boosting **efficiency**, **security**, and **customer experience**.

b) **Strengthening fintech and digital landscape**: Larger banks would boost Cambodia's fintech sector, expand digital payments, and increase access to digital financial services.

c) **Competitive Advantage in Global Digital Banking:** larger banks adopting new technologies could position Cambodia as a digital banking hub, attracting global fintech partnerships and international investments.

The Top 10 E-Payment applications adopted by firms



Source: Cambodia Development Resource Institute (CDRI)

003 Why Cambodia Needs Larger Banks

CAMBODIA'S HIGH CREDIT-TO-GDP RATIO: IMPLICATIONS FOR FINANCIAL STABILITY

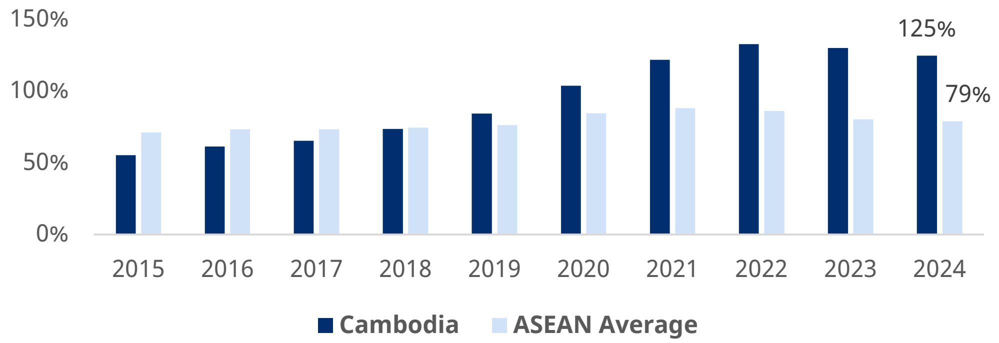
- Since 2008, Cambodia has seen significant growth in private sector loan volumes. The domestic credit-to-GDP ratio has consistently outpaced the ASEAN average since 2018, reaching 133% in 2022. While this growth presents opportunities, it also raises concerns about overleveraging, debt sustainability, and increasing NPLs, exposing the economy to financial vulnerabilities and external shocks that could strain the banking sector's stability.

Cambodia's Private Sector Loan Growth and Financial Sector Potential Challenges

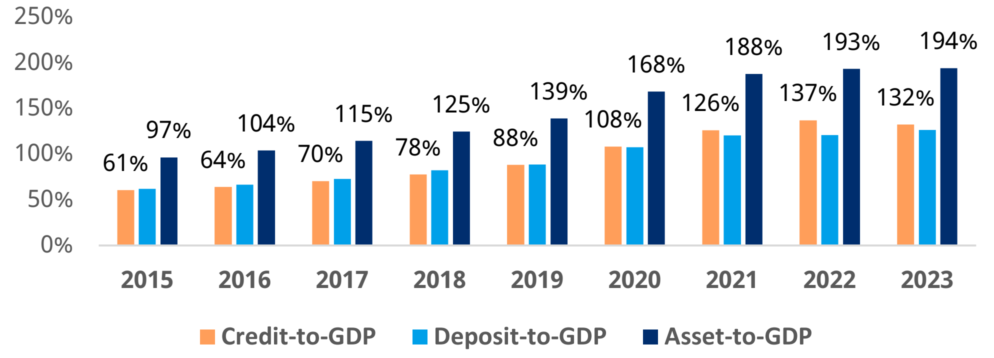
- Since the global financial crisis in 2008, Cambodia has experienced significant growth in **private sector loan** volumes. The **domestic credit to the private sector (% of GDP)** has consistently outpaced the **ASEAN average** since 2018. In 2022, Cambodia's ratio stood at **133% of GDP**, compared to the regional average of **86% of GDP**, indicating substantial economic and financial shifts within the country. This surge in credit growth reflects both **opportunities** and **challenges** for Cambodia's economy and financial system.

- Some of the challenges include;
  a) **Overleveraging and Debt Sustainability:** The high credit-to-GDP ratio raises concerns about **overleveraging** among businesses and the overall **sustainability of debt**. With such a significant proportion of the economy dependent on credit, there is an increasing risk of financial vulnerability if economic conditions deteriorate. If businesses or consumers struggle to meet their obligations, it could lead to widespread financial instability.
  b) **Credit Quality and Non-Performing Loans (NPLs):** Rapid credit growth can sometimes lead to a deterioration in credit quality, increasing the risk of NPLs, which could strain the banking sector.
  c) **External Shocks:** Given the size of credit relative to the economy, Cambodia might be more vulnerable to external financial shocks, which could affect borrowers' ability to repay loans and banks' stability.

Domestic credit to private sector (% of GDP)



Cambodia Banking metrics relative to GDP



Source: NBC, World Bank and YSC Research

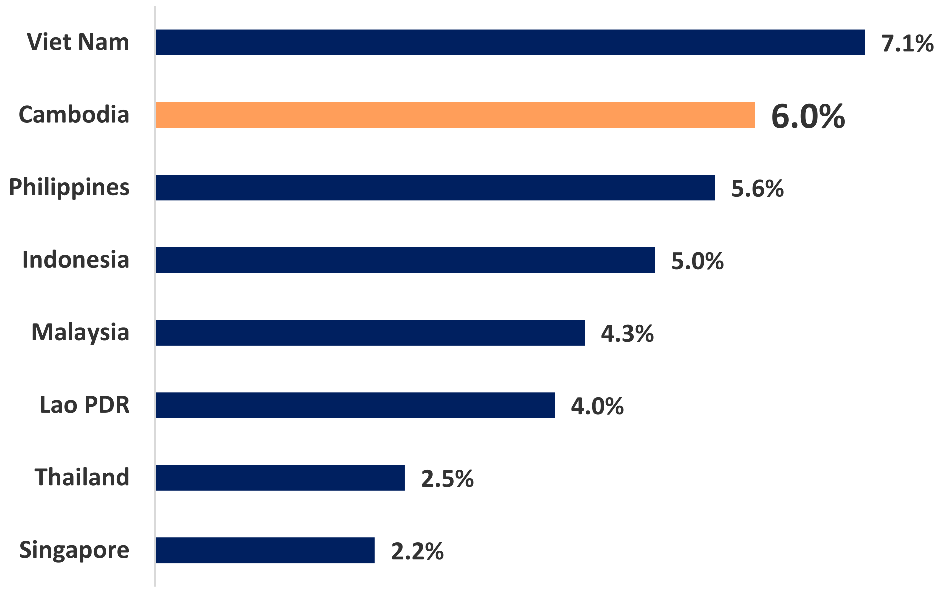
STRONG ECONOMY, WEAK RETURNS: THE CASE FOR BANKING SECTOR CONSOLIDATION

- Cambodia's strong economic growth, with an average **7% GDP growth** from 2010 to 2019, has positively impacted various sectors, including banking. However, the **decline in banking profitability** in 2023 is primarily due to the **fragmented nature** of the sector, with many small, inefficient banks, highlighting the need for **banking consolidation** to improve **profitability** and **long-term stability**.

Cambodia's Economic Growth and Fragmented Banking Sector

- Cambodia has emerged as one of Southeast Asia's fastest-growing economies, with an impressive average **real GDP growth rate** of over **7%** from 2010 to 2019, prior to the **COVID-19 pandemic**.
- This economic growth has had a positive **ripple effect** across various sectors, including the **banking sector**. However, the decrease in the overall banking sector profitability appears experience in 2023 and 2024 stem more from the **fragmented nature of the industry** rather than **broader economic challenges**.
- The Cambodian banking market remains highly fragmented, with numerous small, inefficient banks contributing to intensified competition and operational inefficiencies. This fragmentation has led to a deterioration in credit quality, driven by pressure on these banks to achieve growth. The rapid credit growth up to 2022 came at the cost of poorer credit quality since these banks may have had to reach out to borrowers with weaker credit profiles or extended credit amounts approaching borrowers' repayment capacity or at higher loan-to-value (LTV) ratios.
- As a result, the sector is experiencing a sustained increase in NPL ratios, highlighting the growing risk to financial stability.
- While Cambodia's rapid economic growth supports various sectors, the **banking industry's structural inefficiencies** need to be addressed to improve **profitability** and **stability** in the long term through banking consolidation**.**

2024 GDP Growth Rate Across Southeast Asia (IMF's WEO April 2025)



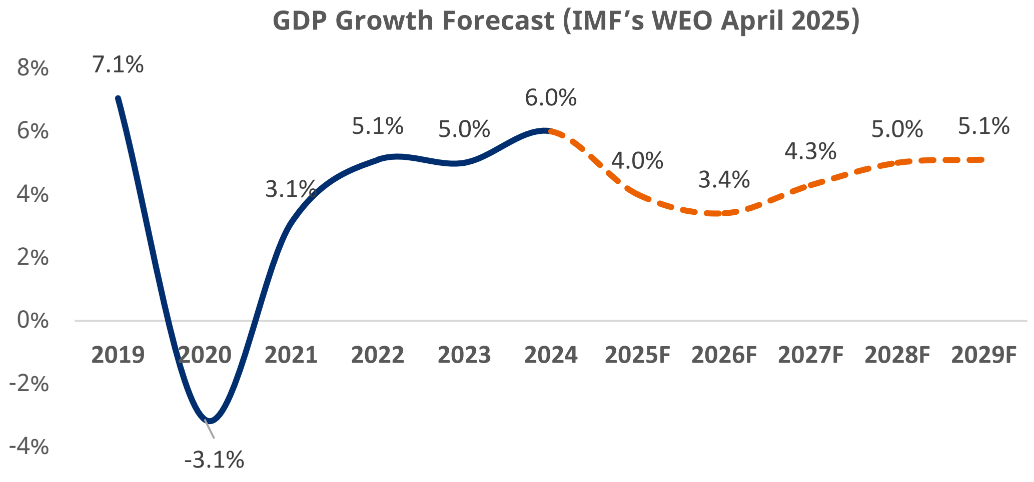
Source: NBC, World Bank and YSC Research

TOWARDS 2030: BUILDING A STRONGER FINANCIAL SYSTEM THROUGH BANK CONSOLIDATION

- Cambodia's goal of becoming an upper middle-income nation by 2030, with a projected GDP of $71 billion, will drive increased demand for banking services, making **bank consolidation** crucial. Larger banks can play a key role in supporting this growth by offering **enhanced services**, strengthening **financial infrastructure**, and contributing to a **more resilient and efficient financial system** for sustained economic progress.

Cambodia's Economic Transition and the Role of Banking Sector Expansion

- Cambodia aims to achieve upper middle-income status by 2030, with a projected **GDP of $71 billion**, marking a significant shift in its economic trajectory. As demand for banking and financial services grows, **consolidation** will be crucial to form larger, more capable banks that can **support this expansion**.
- This economic transition, characterized by **increased industrialization, urbanization, and economic diversification**, will require more innovative and flexible banking products and services. Additionally, **rising living standards** and increased purchasing power will drive greater demand for enhanced banking offerings. Thus, presenting a golden opportunity for **larger banks to play a pivotal** role in facilitating this transition.
- This is because **larger banks** offer several **strategic advantages**:
  - **Lower Cost of Credit**: Operational efficiencies and lower funding costs, driven by a strong deposit base, enable larger banks to offer more competitive lending rates.
  - **Innovative Financial Products:** They can develop more advanced products, such as risk-hedging solutions, to meet the evolving needs of businesses in a more diversified and more sophisticated economy.
  - **Efficient Fund Mobilization:** With a broader range of investment products in addition to traditional deposits, larger banks can better channel capital into growth opportunities.
- **Enhanced Lending Practices:** Improved credit scoring models and stronger underwriting standards reduce the risk of borrower over-indebtedness, supporting more sustainable lending growth



Source: IMF and YSC Research

004 Summary of Key Findings, Opportunities and YSC's Commentary

SUMMARY OF REPORT FINDINGS

- Our analysis shows that the Cambodian banking sector is facing challenges such as **fragmentation**, **slow growth**, **shrinking margins**, **rising NPLs**, and **downward pressure on ROE**. We also identified that several **smaller banks** are a **burden on sector-wide performance** and may pose a **systemic risk** to **financial stability**. These factors highlight the need for **improved efficiency**, making **consolidation** a logical step forward to address these issues.

- **Optimizing Operational Efficiency:** Our analysis also suggests that banks should consider **strategically closing or downsizing underperforming branches** and transitioning more customers to **digital platforms**. This approach would help reduce **costs**, **optimize operational efficiency**, and **boost profitability**, while simultaneously **enhancing customer experience** through more accessible, **technology-driven services**. A shift towards **digital banking** aligns with both **cost-efficiency** and **customer satisfaction**, which are crucial for **long-term competitiveness**.

- **The Role of Banks in Driving Consolidation:** While the Cambodian banking sector is often seen as a small, developing market, this presents a **significant opportunity** for consolidation. The fragmented nature of the market creates potential for **strategic M&A**, which can **unlock significant value**. By **restructuring operations** to achieve greater **scale and scope**, banks can **leverage synergies** and enhance their **competitiveness** within this fragmented landscape. Each bank—whether large, medium, or small—will play a pivotal role in driving the consolidation of Cambodia's banking sector through mergers and acquisitions (M&A), with varying objectives. For larger banks, consolidation serves to:
    - **Expand horizontally** in the face of slow organic growth,
    - Acquire **niche markets dominated** by smaller or mid-sized competitors, and/or
    - Increase scale to reinforce **market leadership.**

- For medium-sized banks, consolidation provides an opportunity to become more **competitive, efficient, and profitable** by achieving greater **operational scale**. Smaller banks, **under pressure**, may pursue consolidation to:
    - **Integrate** into a larger, more competitive and efficient entity, or
    - **Exit the market** through M&A.

- By targeting **synergies** in **market expansion**, **operational efficiency**, **technology**, and **talent acquisition**, banks can enhance **growth**, **profitability**, and **overall competitiveness**.

YSC'S PERSPECTIVE ON BANKING CONSOLIDATION IN CAMBODIA

- YSC views **banking consolidation** as a key opportunity to **streamline operations**, **optimize resources**, and **enhance profitability**. While it presents challenges, consolidation helps banks **improve efficiency**, **expand offerings**, and **build long-term growth**. This process strengthens market presence and positions both large and small banks to be **more resilient**, **competitive**, and **customer-focused**, fostering a more inclusive banking sector**.**

- **Internal Research for M&A Readiness:** YSC believes it is critical for individual banks to conduct thorough **internal research** to assess their **strengths**, **weaknesses**, and **capabilities**. This **self-assessment** will enable banks to define their **strategic priorities** and make more informed decisions when considering **potential M&A targets**. Additionally, banks should identify **potential M&A targets** that complement their existing operations, strengthen their **competitive position**, and offer **synergies** such as **cost savings**, **technological advancements**, or **access to new markets**. This approach will help banks align their **M&A strategy** with **long-term growth objectives**.

- **Engaging Third-Party Experts:** YSC recommends that banks engage **third-party experts** to supplement their internal research and assess potential synergies with target banks. The first step should involve a thorough evaluation of **financial performance**, **cultural compatibility**, and the **operational efficiencies** that can be realized through the M&A. This independent evaluation will help both parties understand the **value proposition** and **long-term benefits** of consolidation. The first bank to take this step will likely uncover valuable opportunities, with the internal team collaborating with experts to identify and leverage synergies. This approach offers a **cost-effective way** for banks to explore the **potential of M&A**.

- **Role of NBC in Driving Consolidation:** YSC believes the NBC should play a **proactive** role in **facilitating bank consolidation** by offering **targeted incentives** to ease integration challenges and strengthen the sector's resilience. For instance;
  - NBC could support this process through **regulatory flexibility** for **"merged banks"—**such as temporarily extending deadlines for **capital adequacy ratio (CAR) adjustments,** and relaxing requirements on **solo CAR** during the transition period. These measures would reduce the immediate **financial pressure** on merging institutions, enabling them to focus on **streamlining operations** and **achieving synergies**.
  - Additionally, **strategic workforce reductions**, though sensitive, are often a necessary component of successful mergers. Allowing such measures can help **eliminate redundancies**, **improve cost efficiency**, and **enhance competitiveness**. By supporting these transitional adjustments, NBC can help **position the banking sector** for **long-term stability**, **growth**, and **profitability**.
  - In the **long term**, the NBC should consider supporting the creation of a **mega size bank** through the merger of medium- to large-sized institutions or by integrating smaller banks into a **dominant player.** This strategy would position the new entity to compete more effectively in **Southeast Asia**. The regional market presents significant growth opportunities, such as expanding regional branches and cross-border banking operations, which would strengthen Cambodia's banking presence and further integrate it into the regional financial system.

- By integrating these recommendations, YSC believe that Cambodian banks can effectively manage the challenges of **consolidation and capitalize** on the **opportunities** it presents for **growth**, **efficiency**, **profitability** and **long-term competitiveness**.

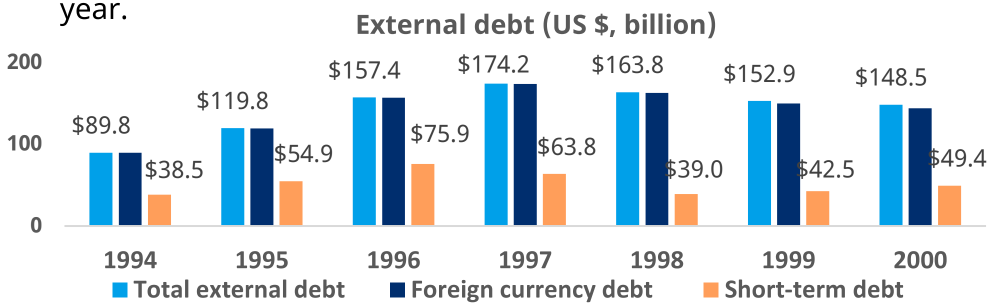
005 Case Study: M&A as a Tool for Banking Soundness

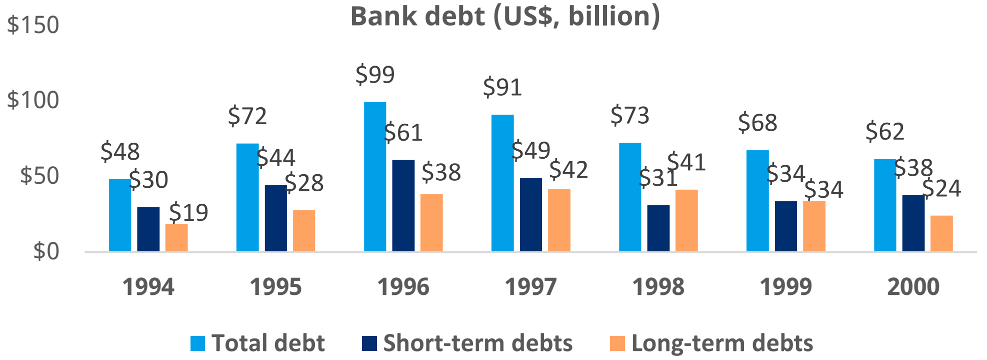
SOUTH KOREA BANKING CONSOLIDATION (1/2)

- Following the **1997 Asian financial crisis**, the **South Korean government** implemented several **incentives in August 2000** to promote **bank consolidation**. These included **tax breaks**, **financial support for restructuring**, and **relaxed regulatory requirements**. The goal was to create larger, more competitive banks that could effectively compete globally while maintaining **domestic financial stability**.

Factors that led to Banking Sector Consolidation

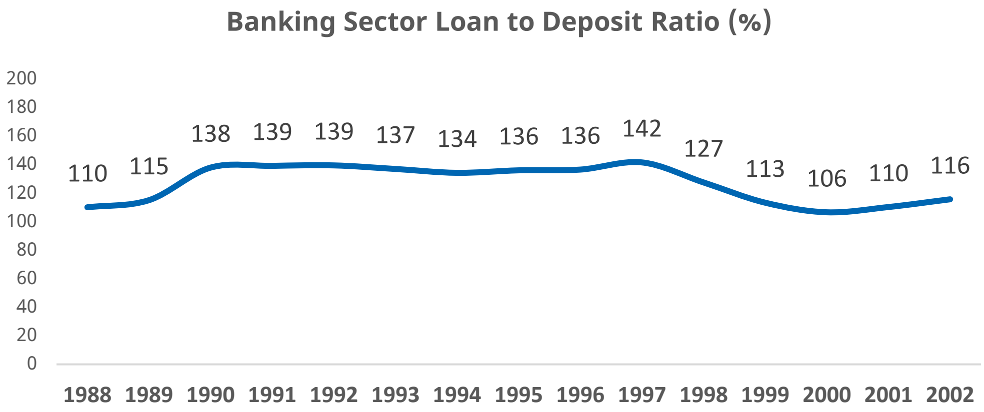
1. **Unsustainable External debt:** Since **1993**, rapid bank borrowings significantly increased **external debt**, exposing the **Korean economy** to **systemic risk**. By **1997**, South Korea's **short-term foreign debt** had reached around **$80 billion**, with **77%** of this debt held by banks, much of which needed to be **refinanced** within a year.





Factors that led to Banking Sector Consolidation

2. **Rising Loan to Deposit Ratio:** By the end of **1996**, South Korea's **loan-to-deposit ratio** stood at **137%**, rising to **141%** by **1997**, well above the typical **100%** ratio seen in most other Asian banking sectors. This indicates that banks were heavily reliant on **borrowed funds** to finance domestic lending, reflecting a **high leverage** ratio within the banking sector.



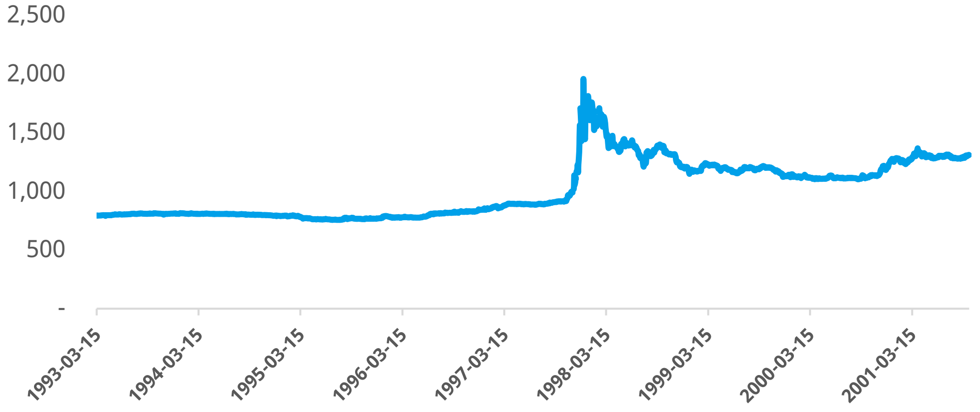
Source: Jong-Wha Lee, 2017; Kihwan, 2006; FRED, IMF, ADB and YSC Research

SOUTH KOREA BANKING CONSOLIDATION (2/2)

Factors that led to Banking Sector Consolidation

3. **Capital outflow:** The **1997 financial crisis** in **Korea** was triggered by a sudden and large-scale reversal of **capital flows** as foreign creditors rushed to withdraw their **short-term claims**. In the **fourth quarter of 1997**, **net private capital outflows** totaled **$26.1 billion**, or about **6%** of Korea's annual **GDP** for that year. The country's **foreign exchange reserves** were insufficient to cover **short-term external liabilities**, leaving the economy highly vulnerable to **liquidity shortages** in the event of a foreign capital withdrawal.

- This led to **currency** and **maturity mismatches** on the balance sheets of financial institutions, causing the **Korean won** and **asset prices** to **plummet** sharply.



Government Actions

- **Consolidation of Financial Institution:** Following the **1997 crisis**, the **Korean government** implemented **financial sector restructuring** to address structural weaknesses and restore **foreign investor confidence**. As an immediate response, the restructuring focused on **shutting down troubled financial institutions** and disposing of their **NPLs**.

- By **August 2000**, this process reduced the number of **Korean banks** from **33 to 22** and **merchant banks** from **30 to 9**, streamlining the sector and improving stability.

Type	Consolidation
Purchase and assumption	1) Daedong Bank → Kookmin Bank (Jun, 1998) 2) Dongnam Bank→ Korea Housing & Commercial Bank (Jun, 1998) 3) Dongwha Bank → Shinhan Bank (Jun, 1998) 4) Chungchung Bank → Hana Bank (Jun, 1998) 5) Kyungki Bank → KorAm Bank (Jun, 1998)
Merger	***Government-led mergers*** 1) Korea Commercial Bank, Hanil Bank → Hanvit Bank (Jan, 1999) 2) Kookmin Bank, Korea Long-Term Credit Bank → Kookmin Bank (Jan, 1999) 3) Chohung Bank, Chungbuk Bank → Chohung Bank (May, 1999) 4) Chohung Bank, Kangwon Bank → Chohung Bank (Sep, 1999) ***Voluntary merger*** 5) Hana Bank, Boram Bank → Hana Bank (Jan, 1999)
Sell-off	1) Korea First Bank → Newbridge Capital (US financial consortium) (Dec, 1999)
Government initiated	1) Hanvit Bank, Peace Bank, Kwangju Bank, Kyongnam Bank, Hanaro Investment Banking, nine member-bank subsidiaries → Woori Financial Holding Company (Apr, 2001)

Source: Jong-Wha Lee, 2017; Kihwan, 2006; FRED, IMF, ADB and YSC Research

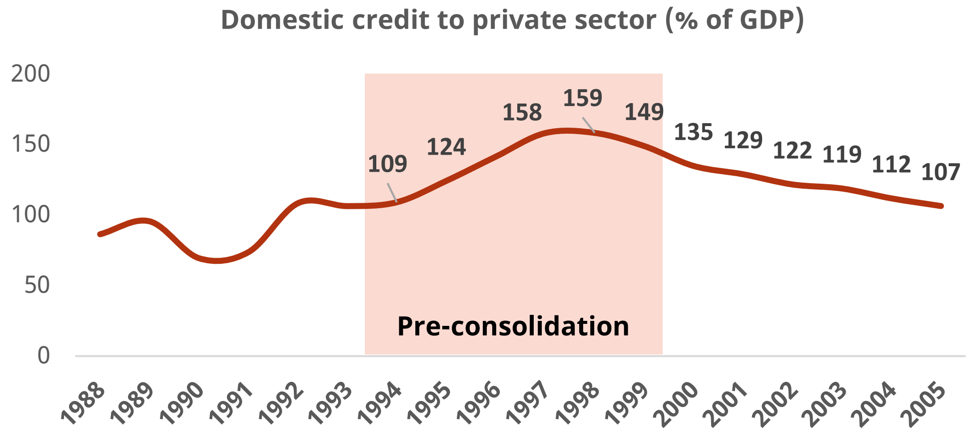
MALAYSIA BANKING CONSOLIDATION (1/2)

- In response to the **Asian financial crisis**, **Bank Negara Malaysia (BNM) in 1999** initiated a **strategic consolidation**, merging **54 financial institutions** into **ten anchor banks**. This move tackled rising **non-performing loans (NPLs)**, the vulnerabilities of smaller banks, and systemic weaknesses, marking a critical step in strengthening Malaysia's banking sector and ensuring its **long-term stability**.

Factors that led to Banking Sector Consolidation

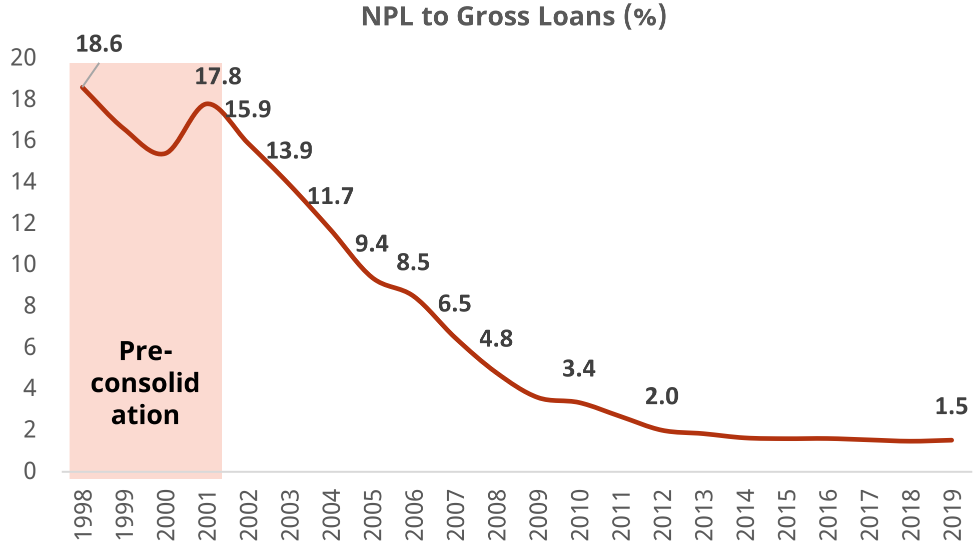
1. **Significant Credit Expansion**: Leading up to the **1997-1998 Asian Financial Crisis**, **Malaysia** experienced a sharp rise in private sector credit, with domestic credit to the private sector growing to **158% of GDP** from **109% in 1994**, raising alarms at **Bank Negara Malaysia (BNM)**.

- The rapid pace of credit growth suggested potential **overheating** in the financial system and increased **economic vulnerabilities**, particularly the risk of **asset bubbles** and **financial instability**. In response, **BNM** initiated **strategic consolidation** to address these systemic risks and stabilize the banking sector.



Factors that led to Banking Sector Consolidation

2. **High Levels of NPLs**: The **Asian Financial Crisis** caused a significant rise in **NPLs** within Malaysia's banking sector. The **NPL ratio** surged to approximately **18.6%** of total loans in **1998**, reflecting widespread distress in both the banking sector and the broader economy.



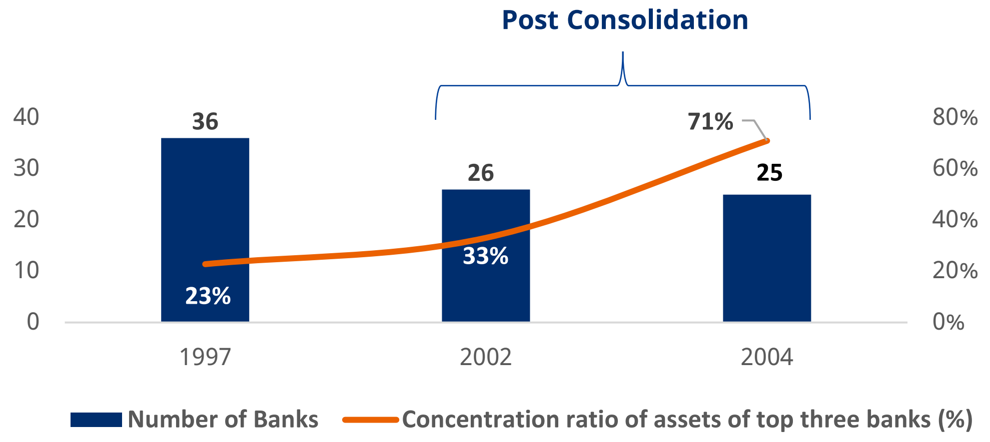
Source: Bank Negara Malaysia , ADB and YSC Research

MALAYSIA BANKING CONSOLIDATION (2/2)

Factors that led to Banking Sector Consolidation

3. **Banking Sector Fragmentation**: Before consolidation, Malaysia's banking sector was highly fragmented, with a large number of small banks. In **1997**, the **Top three banks** held only **23%** of the sector's total assets, reflecting structural weaknesses that hindered the **efficiency** and **competitiveness** of banks, both domestically and internationally.

- Following the consolidation, this ratio surged to **71%** by **2004**, significantly strengthening the sector's market position.



Government Actions

- On **29 July 1999**, **Bank Negara Malaysia (BNM)** met with major shareholders of domestic commercial banks and selected finance companies to discuss a **merger program** aimed at accelerating the rationalization and consolidation of Malaysia's banking system. The goal was to create **strong domestic banking groups** that would serve as the backbone of the banking sector.

- This consolidation was intended to position these banks to better meet the evolving demands of the **domestic economy**, address future challenges from **globalization and liberalization**, and contribute more effectively to **sustainable economic growth**.

Anchor Finance Company	Merger Partners
1. Mayban Finance Berhad	PhileoAllied Bank Bhd; Aseambankers Malaysia Bhd; The Pacific Bank Bhd; Sime Finance Bhd; Kewangan Bersatu Bhd
2. Public Finance Berhad	Hock Hua Bank Bhd; Advance Finance Bhd; Sime Merchant Bankers Bhd
3. Hong Leong Finance Berhad	Wah Tat Bank Bhd; Credit Corporation (Malaysia) Bhd
4. Alliance Bank Malaysia Bhd	Sabah Bank Bhd; International Bank Malaysia Bhd; Bolton Finance Bhd; Sabah Finance Bhd; Bumiputra Merchant Bankers Bhd; Amanah Merchant Bank Bhd
5. Bumiputra-Commerce Bank Bhd	Commerce International; Merchant Bankers Bhd; Bank Bumiputra
6. Perwira Affin Bank Bhd	BSN Commercial Bank Bhd; BSN Finance Bhd; Asia Commercial Finance Bhd; BSN Merchant Bank Bhd
7. RHB Bank Bhd	Bank Utama (Malaysia) Bhd; Delta Finance Bhd; Interfinance Berhad
8. Southern Bank Bhd	Ban Hin Lee Bank Bhd; Cempaka Finance Bhd; Perdana Finance Bhd; United Merchant Finance Bhd; Perdana Merchant Bankers Bhd
9. EON Bank Bhd	Oriental Bank Bhd; City Finance Bhd; Perkasa Finance Bhd; Malaysian International; Merchant Bankers Bhd
10. AmBank (M) Bhd	MBF Finance Bhd

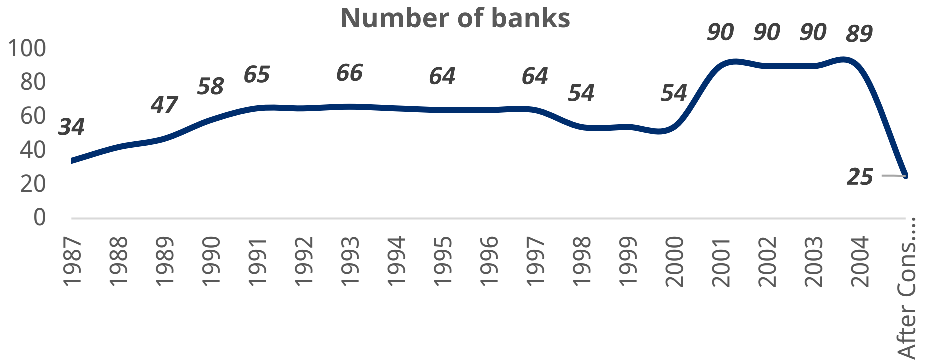
Source: Bank Negara Malaysia , ADB and YSC Research

NIGERIA BANKING CONSOLIDATION (1/2)

- In **2004**, the **Central Bank of Nigeria (CBN)** proposed consolidating commercial banks through **mergers and acquisitions** as part of a broader reform plan. This move was driven by the need for a more **robust, resilient**, and **competitive banking sector**, aiming to ensure **financial stability**, improve **sector efficiency**, and enable Nigerian banks to play key roles in both the **regional** and **global financial systems**.

Factors that led to Banking Sector Consolidation

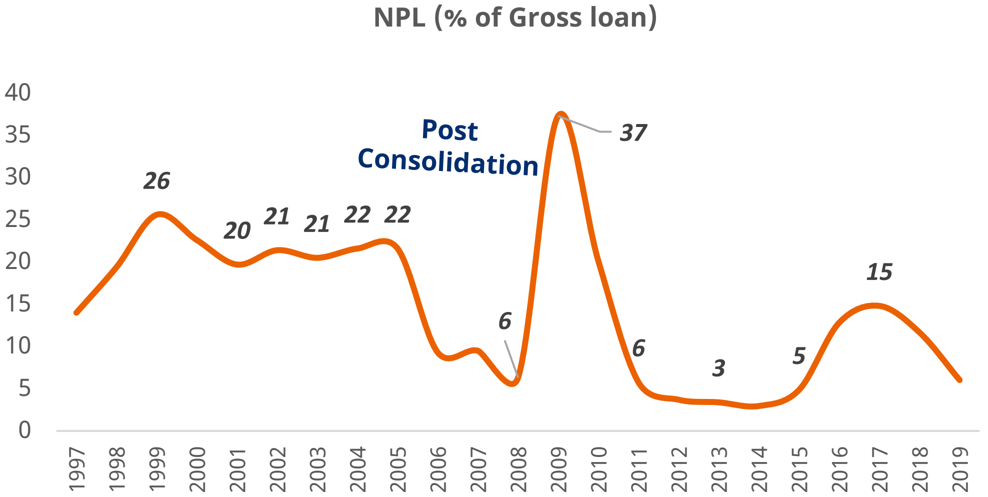
1. **Fragmentation in the Banking Sector**: Before consolidation, Nigeria's banking sector was highly fragmented, with many small banks unable to support large-scale economic activities. This fragmentation led to **inefficiencies** and a **competitive environment** that lacked **economies of scale**.



2. **Low Capital Base:** Many banks had a **low capital base**, making them vulnerable to **financial instability**. The **minimum capital requirement** prior to consolidation was **N2 billion ($15 million)**, which was insufficient to absorb losses or support operations that could drive **economic growth**, especially when compared to other **African countries**.

Factors that led to Banking Sector Consolidation

3. **Poor Asset Quality**: The Nigerian banking sector faced high levels of **non-performing loans (NPLs)**, reflecting inadequate **credit risk management** and **lending practices**, which posed a significant threat to the sector's **stability** and **viability**.



*The 37% NPL in 2009 was during global financial crisis

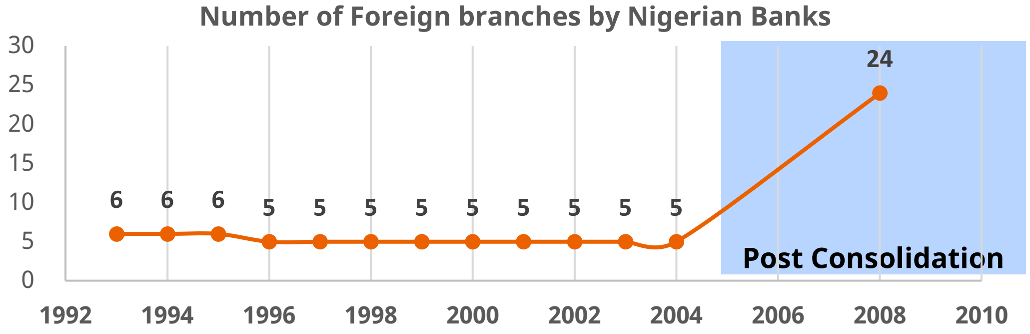
Source: Central Bank of Nigeria; Kihwan, 2006; FRED, IMF, ADB and YSC Research

NIGERIA BANKING CONSOLIDATION (2/2)

- The **Central Bank of Nigeria** aimed to build **stronger banks** capable of supporting **economic growth**, reducing **vulnerability to financial crises**, and improving the **international competitiveness** of Nigerian banks. This initiative aligned with global trends to ensure banks have a solid **capital base** to **sustain operations** and withstand **financial shocks**.

Factors that led to Banking Sector Consolidation

4. **Limited Scope for International Expansion**: Many Nigerian banks were too small to compete effectively on **regional** and **international stages** or engage in **global financial markets**, limiting their growth opportunities. To address this, the **CBN** aimed to create **stronger banks** capable of supporting **economic growth**, improving **regional competitiveness**, and enhancing the **international standing** of Nigerian banks.



Government Actions

- On **July 6, 2004**, the **Central Bank of Nigeria (CBN)** announced that banks were required to **increase their minimum capitalization** to **N25 billion** (approximately **$200 million**), a **13-fold increase** from the previous requirement. Banks were given **18 months** (instead of the usual 12 months) to comply, with full compliance expected by **end-December 2005**. This move was part of a broader effort to **consolidate banking institutions** through **mergers and acquisitions**.

Type	Consolidation
Merger	1) Access Bank, Marina Bank and Capital Bank→ Access Bank (2005) 2) United Bank for Africa, Standard Trust Bank Plc→ United Bank for Africa (2005) 3) FCMB, Co-operative Development Bank, Midas Bank, and Nigerian-American Bank→ First City Monument Bank (2005) 4) Oceanic Bank, International Trust Bank Plc→ Oceanic Bank International Plc 5) Skye Bank, Prudent Bank Plc, EIB International Bank Plc, Bond Bank Limited, Reliance Bank Limited, and Co-operative Bank Plc → Skye Bank (2005)
Acquisition	1) United Bank for Africa acquired Continental Trust Bank, Trade Bank, City Express Bank, Metropolitan Bank, and African Express Bank→ United Bank for Africa (2005) 2) Intercontinental Bank acquired Equity Bank of Nigeria, Global Bank Plc, and Gateway Bank of Nigeria→ Intercontinental Bank (2005) 3) Fidelity Bank acquired FSB International Bank Plc and Manny Bank Plc→ Fidelity Bank
IPO	1) First Bank of Nigeria Plc 2) Guaranty Trust Bank Plc 3) Zenith Bank Plc

Source: Central Bank of Nigeria; Kihwan, 2006; FRED, IMF, ADB and YSC Research

006: Case Study: Leveraging Bank Size for Competitive Advantage

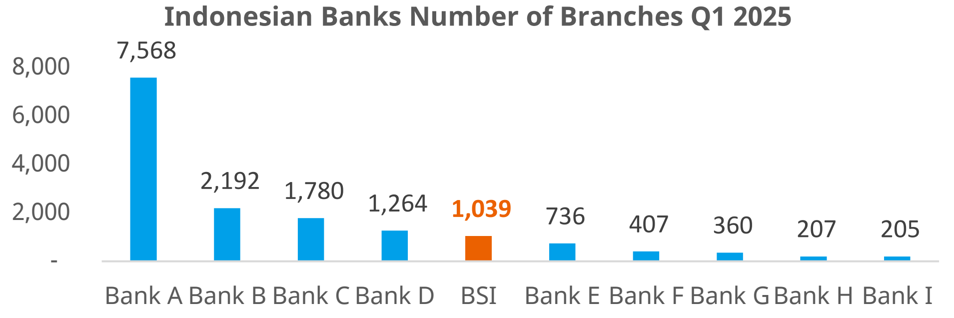
BANK SYARIAH INDONESIA (BSI)

- **Bank Syariah Indonesia (BSI)**, headquartered in **Jakarta**, stands as a prime example of leveraging size for **strategic advantage** in an emerging market. This case study examines BSI's journey to becoming **Indonesia's largest Islamic financial institution** and a **Top 10 Global Islamic Bank**, highlighting its successful merger, expanded service offerings, and strengthened capital base as key factors driving its growth and competitive positioning in the global Islamic banking sector.

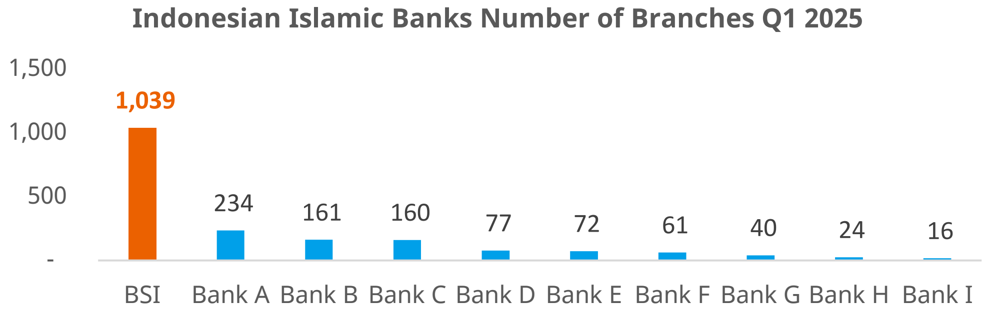
Background

- ***Establishment:*** The **banking industry in Indonesia** marked a significant milestone with the establishment of **BSI**, which officially launched on **February 1, 2021**. BSI was formed through the merger of **Bank BRI Syariah**, **Bank Syariah Mandiri**, and **Bank BNI Syariah**, combining the strengths of the three Islamic banks.
- **Ownership Structure**: Post-merger, **Bank Mandiri** holds **51.2%** of **BSI**, with **BNI** owning **25%**, **BRI** holding **17.4%**, and the remaining **6.4%** held by BRI Syariah's pension fund and public shareholders.
- **Asset Base**: The merged entity has total assets of **Rp214.6 trillion** (**US$14.6 billion**), placing it among the **Top 10 banks in Indonesia** and **Top 10 global Islamic banks** by market capitalization.
- **Operational Scale**: **BSI** operates **1,200 branches** and **1,700 ATMs** across Indonesia, employing **20,000 staff**, expanding its reach and service capabilities.
- **Strategic Objectives**: The merger aims to create a **robust Islamic bank** offering comprehensive services, enhancing **financial inclusion** and positioning **BSI** as a competitive player in the global **Islamic finance market**.

Post-merger evaluation



BSI is now the only Islamic bank in the Top 10 bank in Indonesia (based on no. of branches)



The largest amongst the other Islamic bank, well ahead in the capitalization

Source: BSI Annual Reports and YSC Research

ENHANCED OPERATIONAL SCALE

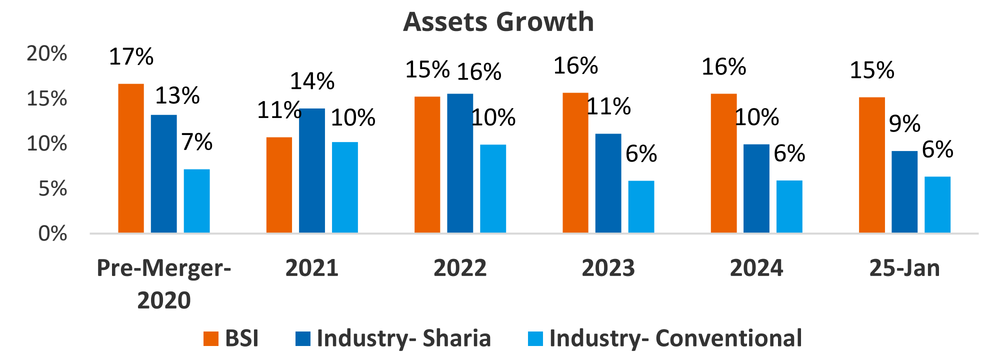
- Post-merger, **BSI** has consistently outpaced the broader banking sector in both **total assets** and **loan growth**. The merger has had a significant positive impact, driven **sustained growth** and accelerating BSI's market dominance, solidifying its position as a key player in Indonesia's dynamic financial market.

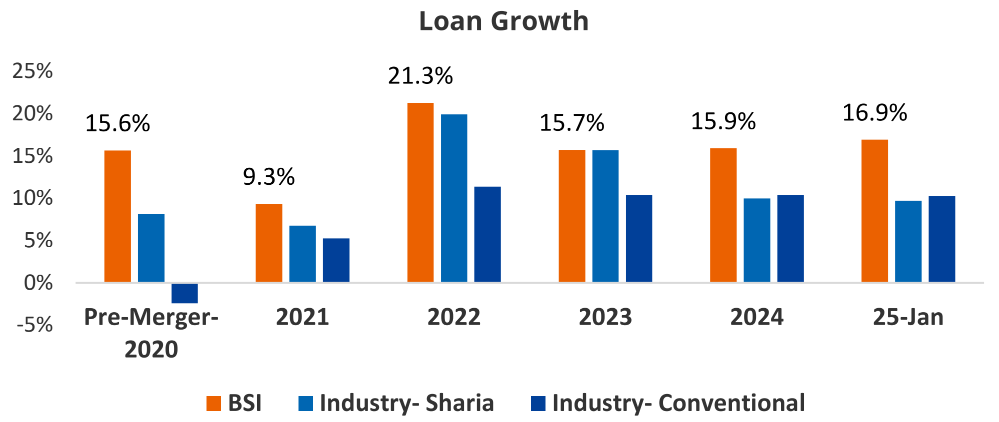
Post-merger evaluation

1. **Increase in Scale**: Post-merger, **BSI** has consistently outperformed the broader banking sector in terms of both **total assets** and **loan growth**. In **2024**, BSI's **asset growth** was **16%**, significantly outpacing the growth of the **Islamic banking sector**, which grew by only **10%**, and the **conventional banking sector**, which grew by just **6%**. This **sustained expansion**, driven largely by BSI, underscores the substantial positive impact of the merger on the bank's **market position** and growth trajectory.

- The merger has provided BSI with the ability to leverage its **enhanced operational scale**, **improved capital position**, and an **expanded customer base**, allowing it to outpace the overall banking sector. This **strategic scale** has enabled BSI to accelerate its growth and strengthen its position as a **dominant player** in Indonesia's rapidly evolving financial landscape, solidifying its role in both the **Islamic and conventional banking markets**.

Post-merger evaluation





Source: BSI Annual Reports and YSC Research

IMPROVED COST EFFICIENCY

- Post-merger, **BSI** significantly improved its **Cost-to-Income Ratio (CIR)** from **54%** to **50%**, reaching a low of **48.6%** in **Q1 2025**, outperforming its competitors. Additionally, the bank's **cost of funds** dropped to **1.6%** in **2022**, driven by its expanded size and customer base, highlighting the benefits of scale in enhancing operational efficiency and financial stability.

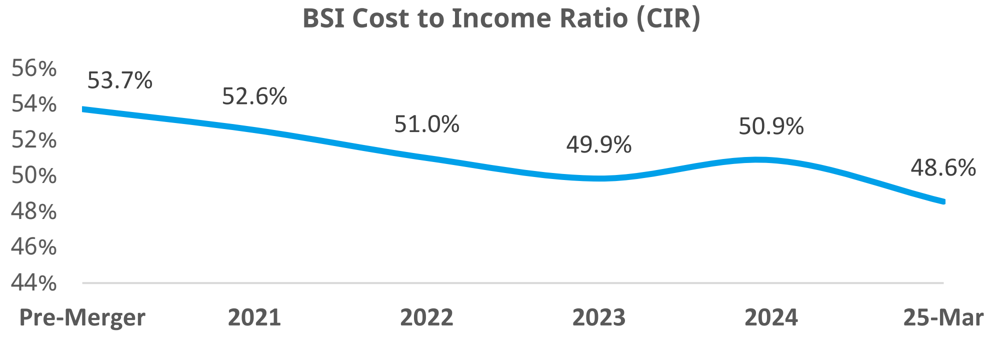
Post-merger evaluation

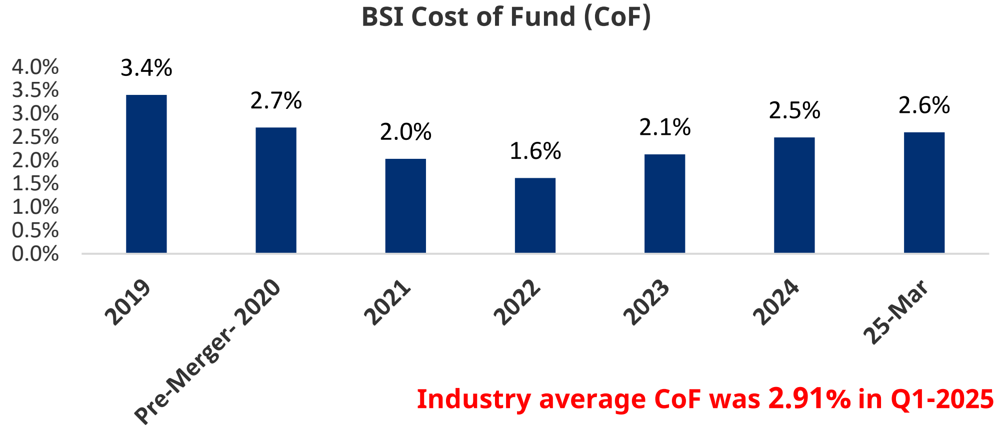
2. **Improved Cost Efficiency**: One of the most notable improvements post-merger is the **CIR**, a key indicator of operational efficiency. Prior to the merger, BSI's CIR stood at **54%**, but post-merger, it decreased to an average of **50%**, reaching an impressive **48.6%** in **Q1 2025**. This represents the **lowest CIR** among its competitors, highlighting the significant advantages of **scale** in managing **operational expenses** more effectively.

- Additionally, the bank achieved an **impressive cost of funds (CoF)** of **1.6%** in **2022**, and the current CoF of 2.6% is below the industry average of 2.91%, demonstrating its ability to attract **low-cost funding**. This is largely due to its expanded size and broader customer base of over **21.58 million customers**, which provides a more stable and diversified deposit base.

- These improvements in **cost efficiency** and **funding** are direct results of the merger, showcasing how leveraging scale can drive **significant operational gains**. For other financial institutions, this provides a compelling case for **mergers or acquisitions** as an effective strategy to enhance **cost efficiency** and gain a **competitive edge** in the industry.

Post-merger evaluation





Industry average CoF was 2.91% in Q1-2025

Source: BSI Annual Reports and YSC Research

HIGH PROFITABILITY AND RETURN

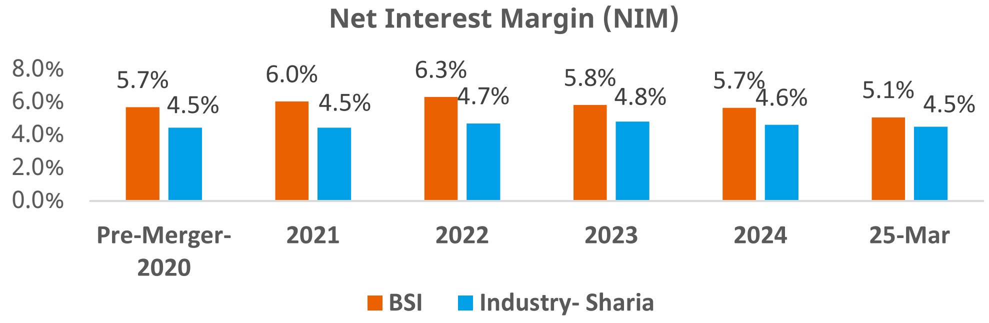
- Post-merger, **BSI** has significantly improved its **Return on Equity (ROE)** to **17.8%** and **Return on Assets (ROAA)** to **2.5%**, reflecting enhanced **profitability** and **operational efficiency**. These improvements, driven by strong **asset management**, **cost control**, and effective **revenue generation**, position **BSI** among the Top performers in the sector and highlight the success of its post-merger strategy.

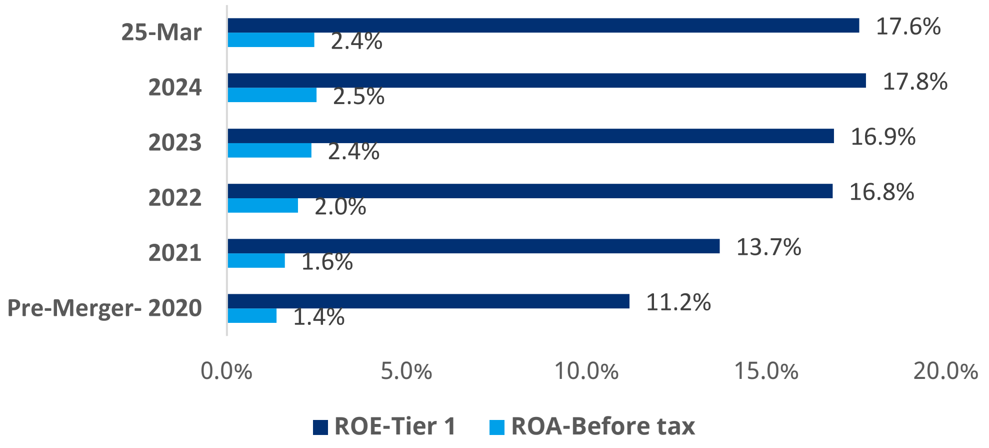
Post-merger evaluation

3. **High Profitability and Return Post-Merger**: Post-merger, **BSI** has demonstrated significant improvements in key financial metrics, particularly in **ROE** and **ROAA**, underscoring the bank's enhanced **profitability** and **operational efficiency**. In **2024**, **BSI** achieved a **ROE-Tier 1** of **17.8%**, marking a **6.6 percentage point** increase compared to pre-merger levels. Additionally, the **pre-tax ROA** reached **2.5%**, reflecting a **110 bsp** improvement. These metrics position BSI among the **Top performers** in the Indonesia sharia banking sector, demonstrating its ability to generate strong returns on both **shareholders' equity** and **assets**.

- The **highest-ever ROE** reflects the **successful post-merger strategy**, driven by improved **asset management**, **cost control**, and effective **revenue generation**. These strategic decisions have significantly enhanced the bank's **profitability**, showcasing the management's skill in capitalizing on the merger to optimize operational efficiency and maximize shareholder value.

Post-merger evaluation





Source: BSI Annual Reports and YSC Research

ROBUST RISK MANAGEMENT

- Post-merger, **BSI** has significantly improved its **risk management**, with **cost of credit** dropping from **2.60%** to **0.83%** in 2024, and **loan growth** increasing from **16%** pre-merger to **21%** post-merger. Additionally, **BSI's NPL ratio** has decreased by **100 basis points**, outperforming the industry average, indicating successful **credit evaluation** and **risk mitigation strategies** that have enhanced both **asset quality** and **financial stability**.

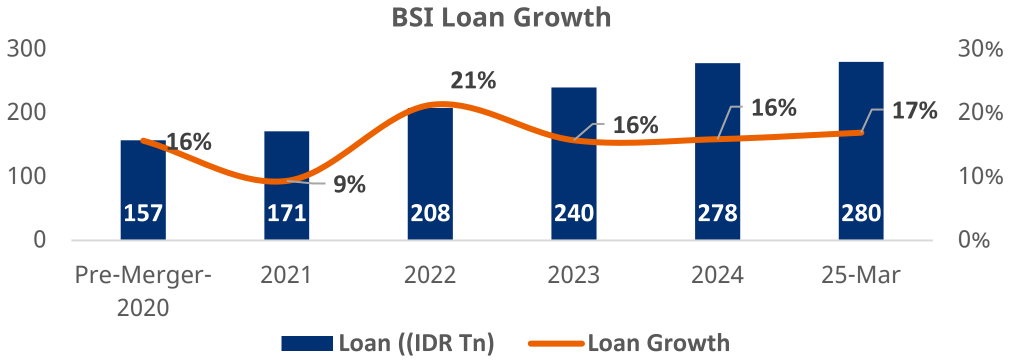
Post-merger evaluation

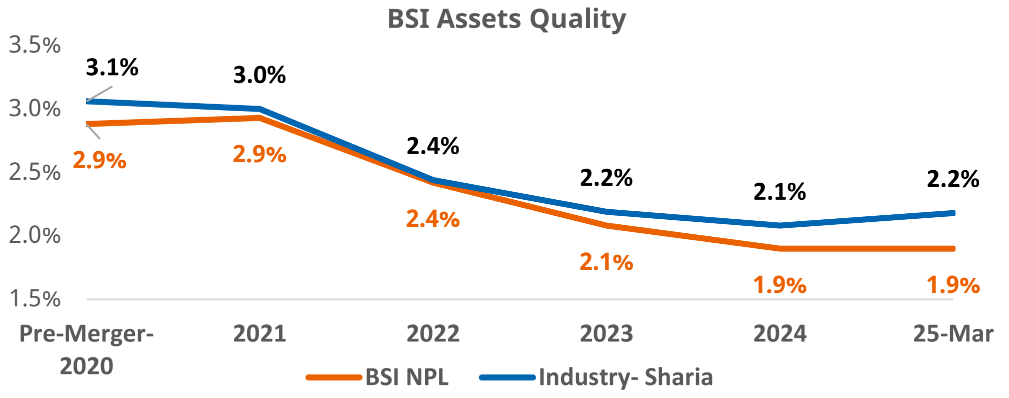
4. **Robust Risk Management**: The merger has enabled **BSI** to leverage its larger size and resources to develop more sophisticated **risk management frameworks**, resulting in improved **credit risk** and more stable financial performance. **BSI's cost of credit** has dropped significantly, from **2.60% pre-merger** to **0.83%** in **2024**, reflecting a more effective approach to managing loan risks and reducing credit expenses.

- Additionally, **BSI's loan growth** has seen a marked increase, from **16% pre-merger** to **21% post-merger** in **2022**, stabilizing at an average growth rate of **17.5%.** This suggests that the merger has enhanced BSI's capacity to expand its lending operations more aggressively, taking advantage of the **increased resources** to meet growing demand. The merger has not only expanded BSI's market capacity but also improved its lending efficiency, positioning the bank for stronger growth.

- Furthermore, **BSI's NPL ratio** has decreased by **100 basis points** post-merger, dropping from **2.9% pre-merger** to **1.9%** in **2024**, outperforming the industry average of **2.1%.** This reduction demonstrates the success of BSI's **credit evaluation** and **risk mitigation strategies**, resulting in a healthier loan portfolio and solidifying the bank's financial stability. The lower NPL ratio is a strong indicator of improved **asset quality** and reflects the effectiveness of BSI's post-merger **risk management framework**.

Post-merger evaluation





Source: BSI Annual Reports and YSC Research

Yuanta Securities

We Know **Asia**

Thank you

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