

Policy Brief on ESG and BANK and FINANCIAL INSTITUTIONS (BFIs) in CAMBODIA— A Follow-Up Study

December 2023

1. INTRODUCTION

Bank and financial institutions (BFIs) in Cambodia have been shifting their focus from shareholders to stakeholders, incorporating socially responsible behavior by modifying their governance structures. This transition reflects a change from profit-oriented to socially-oriented institutions. There is a growing recognition and emphasis on ESG and sustainability among BFIs in Cambodia. The Royal Government of Cambodia (RGC) has mandated the Code of Bank in Cambodia to regulate the banking and financial sector in a more sustainable manner. Additionally, the Cambodia Sustainable Finance Initiative (CSFI) endorses first Cambodia Sustainable Financing Principles, known as CSFP, to further develop principles that guide BFIs in Cambodia. However, it is important to note that CSFP is more voluntary in nature rather than mandatory. Furthermore, the introduction of Green Bonds in the Cambodian financial market has been observed.

The objectives of this report are to assess the progress made in implementing the recommendations outlined in the 2021 Report and to document examples of good ESG practices in the banking and financial sector in Cambodia. A qualitative approach was employed to gather stories and narratives highlighting the ESG practices among BFIs in Cambodia. Purposive sampling was used to select key individuals and institutions for in-depth meetings and interviews. The National Bank of Cambodia (NBC), the Association of Banks in Cambodia (ABC), ACLEDA Bank, Bank of China (BoC), and various NGOs are among the organizations scheduled for meetings and interviews in September 2022.

2. KEY FINDINGS AND DISCUSSIONS

- Despite the existence of a Memorandum of Understanding (MOU) in 2016, a **detailed work plan outlining specific activity has not yet been disclosed.** The 2021 Report suggests that NBC, ABC, and Ministry of Environment (MoE) collaborate to develop a comprehensive joint work plan. This plan would serve to identify and outline key initiatives aimed at integrating environmental and social compliance within the banking and financial sector.
- **ESG practices have been observed among BFIs in Cambodia until now.** Out of the 34 banks that submitted their 2021 Annual Reports to NBC, only 28 reports

are available for public download and review. Among the reports analyzed, 6 of them do not provide any information regarding their CSR or other associated initiatives.

- **While the Environment and Natural Resource Code 2023 introduces some aspects related to ESG compliance, there is currently no yet specific guideline or orientation provided for financial institutions in this regard.** The inclusion of the term "sustainability risk assessment" within the Code implies a connection to the concept of ESG, but an official definition is not clearly stated. This initial introduction is a positive development, but the Code does not elaborate on the subsequent measures that would translate this assessment into practical implementation.
- **The National Bank of Cambodia (NBC) has shown a growing commitment to ESG considerations and related compliance measures through formal attention and significant efforts.** While the tripartite MoU on the Cambodia Sustainable Finance Initiative (CSFI) involving the NBC exists, recent developments indicate that the NBC has been actively pursuing ESG and related compliance matters.
- **Significant progress has been made in raising awareness and providing technical training on ESG matters among BFIs.** Recent findings indicate that there have been formal initiatives and efforts to disseminate knowledge and training on ESG to member banks.
- **The term ESG is relatively new to BFIs in Cambodia, but there has been some inclusive and partially related performance in terms of CSR so far.** The participants in the study expressed a lack of understanding regarding the specific components of ESG and how they are applicable to the banking and financial sector. However, they were familiar with the concept of CSR and recognized it as a way to contribute to society in the areas where they operate.
- **Among BFIs, there is often confusion between CSR and ESG.** There is a rising concern regarding the impact of corporate activities on environmental and social well-being. The interviewed participants tend to perceive CSR and ESG as interchangeable concepts and struggle to distinguish between them. This lack of clarity can be attributed to a limited awareness and information sharing within their organizations, as well as the absence of comprehensive guidance from regulatory bodies such as the NBC, ABC, and MoE.
- **The practical implementation of the social (S) and governance (G) aspects of ESG is more prevalent compared to the environmental (E) aspect.** ESG encompasses these three distinct areas. The RGC has imposed comprehensive and effective obligations on private BFIs, aiming to establish a standardized system and performance. This ensures that banking and financial services in Cambodia are recognized regionally and globally for their efficiency, legality, and ability to facilitate transactions and operations both domestically and internationally.
- **The limits of substantial long-term outcomes regarding ESG practices among**

BFIs can be attributed to the generic and non-binding nature of the Cambodia Sustainable Finance Principles (CSFPs). These principles were found to be very broad and voluntary, providing little concrete foundation for effective implementation. The study revealed that the responses of bank members to the CSFPs demonstrated limited progress. Instead, banks continued to focus on routine CSR activities without making significant adjustments to align with the CSFPs.

- **There is a sense of optimism regarding the implementation of ESG practices among BFIs, but the existing incentives for implementation appear rigid.** The participants interviewed expressed that ESG added value to their operations, but acknowledged that it necessitated significant investment in terms of financial resources and human capital. In the context of voluntary adoption, providing incentives is crucial to recognize and reward those who proactively embrace ESG initiatives.
- **The commitment of the Ministry of Environment (MoE) to promote ESG practices and ensure compliance within the banking and financial sectors has made some progresses but not been substantial.** Despite the tripartite MoU signed in 2016, there have been limited tangible outcomes from the MoE in terms of raising awareness and integrating ESG practices into the operations of BFIs. There are limited formal assignments, guidance, or meetings to facilitate progress in this area.
- **ARDB has demonstrated a positive and encouraging start in the realm of green lending. However, the focus of this practice has primarily been on expanding its own product offerings rather than ensuring strict adherence to ESG compliance by both the bank and its clients.** While green lending may not have yet gained recognition as a standardized ESG practice, it does indicate that certain BFIs are moving towards prioritizing environmental protection and nurturing the planet. To further strengthen its ESG practices, ARDB should enhance its internal systems and processes to foster the integration of ESG principles throughout the organization.
- **To establish a clear framework for ESG-based BFIs, it is essential to incorporate key components into the internal systems of financial institutions.** These components include policies, strategies, and plans, dedicated units responsible for ESG implementation, allocated annual budgets, monitoring and reporting mechanisms, as well as supportive and incentive systems for clients. These elements are crucial for creating a comprehensive and effective ESG framework within the financial institution.

3. RECOMMENDATIONS

- In light of the absence of a **specific guideline for sustainability risk assessment**, it is essential to address this gap and establish subsequent guidelines or instruments that offer clear direction and instructions to financial institutions.
- NBC should review the MoU and collaborate with ABC and the MoE to investigate **policy and performance alternatives concerning ESG practices for**

BFIs. It is advisable to involve an external consultant to develop a range of options and suggest strategies for effectively implementing ESG principles in Cambodia's banking and financial sectors.

- Consistent with the provisions of the 2016 MoU, the NBC, the ABC, and the MoE should give paramount importance to **raising public awareness and enhancing capacity building on ESG practices among BFIs and the general public.**
- **NBC, ABC, and MoE are urged to develop explicit policies or guidelines outlining ESG requirements for the banking and financial sector – a minimum standard** shall be developed. These guidelines should promote best practices and establish a robust monitoring system to ensure adherence and compliance.
- **NBC, ABC, and MoE are urged to explore incentives to promote and strengthen ESG principles in the banking and financial sector.** This could include fiscal policies or benchmarking practices sourced from the region. By studying successful models in neighboring regions, the NBC, ABC, and MoE can gain insights into designing and implementing effective fiscal policies or benchmarking practices.
- **NBC and ABC shall schedule regular meetings with MoE to ensure continuous progress in providing guidance, training, and policy formulation for BFIs regarding ESG practices.** These meetings shall be held at three-month intervals to maintain momentum in advancing ESG initiatives. The meetings will allow stakeholders to exchange updates, discuss emerging trends, and discuss challenges related to ESG practices.
- **ABC shall be considering the establishment of an ESG Foundation to generate funds for capacity building and raising awareness about ESG practices.** The foundation can be funded through membership fees or donations from participating banks or stakeholders. The funds can be strategically allocated to support ESG integration within the banking sector, including capacity building through training programs and educational materials.
- **NBC and ABC, in collaboration with MoE when and where necessary, shall consistently monitor the ESG performance of their member institutions.** This will help identify areas for improvement and provide targeted guidance. The NBC and ABC should establish a regular monitoring mechanism to assess the ESG performance of their member banks, involving periodic assessments, data collection, and analysis of key ESG indicators.
- **NBC and ABC shall be urging BFIs to register with the Cambodia Securities Exchange (CSX) to facilitate capital mobilization and enhance credit ratings.** This will create opportunities for BFIs to diversify their funding sources and attract investments aligned with sustainable and green initiatives.

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