

Bank of Mongolia. The national flag hangs on top of Mongolia's central bank, also known as Mongolbank (photo by Batdorj Baasandorj).



MONGOLIA

FINANCE SECTOR FACT SHEET

The Asian Development Bank (ADB) has a long history of supporting Mongolia's finance sector. The first engagement was in 1991, just after Mongolia joined ADB, when advice and capacity building was provided to the Mongolian Stock Exchange for its operations. Since then, ADB has supported Mongolia's finance sector through \$130 million in lending programs, \$109 million in technical assistance (TA) projects, and \$96 million in private sector investments.

Mongolia's finance sector, despite several improvements, is still very fragile. The economy's heavy reliance on the mining sector exposes the finance sector

to risks from global price fluctuations in commodities. Risks have been rising and the finance sector currently suffers from a high level of nonperforming loans. This is preventing banks from making new loans necessary for economic recovery.

Many improvements have been made in terms of the capacity and range of financial products and public services, and the strength of the financial framework. But challenges exist in improving financial access, ensuring financial support for small and medium-sized enterprises (SMEs), and further enhancing sound regulatory oversight.



Fresh bread. A baker shows off the bread she made in a bakery in Mongolia (photo by Eric Sales).

FINANCIAL INCLUSION

One of the most vital areas of assistance needed within the finance sector is supporting access to finance.

The banking sector accounts for the majority of financial assets; however, a large portion of the population remains unbanked without proper access to financial services. This is particularly true for people living in rural and *ger* (substandard peri-urban settlement) areas.

Providing a full range of financial services at reasonable cost to the poor and rural populations poses a major challenge for Mongolia. The vast size of Mongolia and poor infrastructure add to impediments preventing the population from reaching financial service providers.

Most businesses in Mongolia are micro, small, and medium enterprises (MSMEs), many of which have difficulties accessing credit and financial services. Although MSMEs make up 90% of registered businesses and provide about 50% of all jobs, up to 90% of the country's 36,800 SMEs and most microenterprises do not have regular access to finance from banks. This limits their chances of employment, their opportunity to grow, and their ability to contribute their full potential to the economy.

Many factors impair access to finance in Mongolia, not just for MSMEs, but also for rural and low-income populations. These groups are hindered by their lack of acceptable collateral for loans and high loan lending interest rates. Their

lack of long-term funding also poses liquidity constraints among banks and nonbank financial institutions (NBFIs).

The finance sector also suffers from an inadequate credit information base, burdensome requirements faced by borrowers when applying for credit, and underdeveloped loan underwriting capabilities at banks and NBFIs. Financial literacy is also weak, and an adequate regulatory framework for financial consumer and investor protection does not exist.

ADB is supporting access to finance in several areas through direct lending and technical assistance, such as in projects that aim to help Mongolia's SMEs sustain their businesses and thereby foster growth, diversify the economy, lessen dependence on the mining sector, and create jobs.

In 2015, ADB approved a loan and TA project to improve the quality of the Credit Guarantee Fund of Mongolia.¹ Backing the country's credit guarantee system helped to support the lending capability of commercial banks and expand financing for SMEs in sectors not related to mining.

In 2013 and 2014, ADB provided loans to the private sector through Khan Bank, Xac Bank, and TenGer Group for the support of MSMEs and leasing finance.² ADB is also helping Mongolia develop high-value agricultural products to support the rural economy, by helping agribusiness enterprises develop supply value chains to deliver premium products in international niche markets.³

To facilitate better access to finance among poorer households particularly those in rural areas, ADB has supported transformational mobile banking services.⁴ A project has enabled the implementation of a regulatory system for mobile telephone-based financial services to facilitate competition and improve market behavior to expand financial services.

Access to financial services of rural households is often only available through NBFIs such as savings and credit cooperatives. While this sector is relatively small in comparison to the overall finance sector, its services are vital. ADB has improved their capacity nationwide and enhanced the regulatory and supervisory framework to support expansion of the provision of basic financial services to households.⁵

Financial literacy and the protection of financial consumers are important parts of ensuring overall access to finance. The

Bank of Mongolia, Financial Regulatory Commission, Ministry of Finance, and Authority for Fair Competition and Consumer Protection, as well as several financial consumer protection industry associations all are involved in financial consumer protection.

However, gaps and overlaps exist in the financial consumer protection mechanism, leading to a lack of clear avenues for households to address concerns properly protecting their rights. ADB has bolstered overall financial consumer protection by minimizing gaps and overlaps, encouraging coordination, and facilitating agreements among agencies to clarify and redefine responsibilities.⁶ Technical assistance has supported the steps to establish an alternative dispute resolution framework.

ADB has also supported the delivery of adult basic financial education messages via national television dramas and text-in systems.

FINANCE SECTOR DEVELOPMENT

A stable and strong finance sector is a core requirement for a robust economy, job creation, and overall development in Mongolia. The finance sector needs proper market infrastructure, a solid financial stability mechanism with regulatory oversight, a liquid bond market, and support for vigorous private sector finance. The sector should operate in conformity with global standards for proper governance and risk management.



Mongolian togrog bills. A bank teller counts bills with 20 Mongolian togrog denomination (photo by Batdorj Baasandorj).

Financial Market Infrastructure

In 2013, ADB approved a loan project to support the modernization of the payment system.⁷ The project not only strengthened the interbank payment system infrastructure, but additionally upgraded the retail payment system, and

established a proper legal and regulatory framework.

An efficient interbank system as well as a separate retail payment system help reduce the cost of financial service

delivery, and supports branchless banking and use of noncash mobile payment methods, thereby enhancing access to finance by rural and poor households.

¹ ADB. 2015. *Report and Recommendation of the President to the Board of Directors: Loan Supporting the Credit Guarantee System for Economic Diversification and Employment Project*. Manila.

² ADB. 2013. *Report and Recommendation of the President to the Board of Directors: Proposed Senior Loans to Xac Bank and TenGer Group for Supporting Micro, Small, Medium-Sized Enterprises and Leasing Finance in Mongolia*. Manila; and ADB. 2014. *Proposed Senior Loan to Khan Bank for Supporting Micro, Small, and Medium-Sized Enterprises*. Manila.

³ ADB. 2015. *Proposed Loans for Additional Financing and Administration of Technical Assistance Grant Mongolia: Agriculture and Rural Development Project*. Manila.

⁴ ADB. 2009. *Transformational Mobile Banking Services*. Manila.

⁵ ADB 2010. *Proposed Grant Assistance Mongolia: Promoting Inclusive Financial Services for the Poor*. Manila (financed by the Japan Fund for Poverty Reduction).

⁶ ADB. 2016. *Supporting Financial Sector Development and Stability*. Manila (cofinanced by the Republic of Korea e-Asia and Knowledge Partnership Fund).

⁷ ADB. 2013. *Report and Recommendation of the President to the Board of Directors: Proposed Loan Payment System Modernization Project*. Manila.

In 2009, ADB approved a multifaceted TA that extends broad support to the finance sector. The core work included strengthening of corporate governance, risk management, and internal control system of banks.⁸

Capital Markets

A developed government bond market can provide various benefits for the economy. With a deep and liquid market

for government bonds, governments can reduce funding costs and strengthen the effectiveness of monetary policy.

Aside from these macroeconomic benefits, the development of a government bond market also contributes to the development of related financial markets. ADB has assisted in the development and further deepening of Mongolia's bond market.⁹ Meanwhile, a fully functioning capital market also relies upon a stock market to

allow private sector companies to raise long-term capital.

To partially help implement the government's privatization program, the Mongolian Stock Exchange was launched in February 1992. ADB assistance was instrumental in providing policy and technical advice during the exchange's creation, and ADB has further supported its development over the years through technical assistance.¹⁰



Garment production facility. The Agriculture and Rural Development Project helps agribusiness enterprises develop supply value chains to deliver premium products that command high prices in international niche markets (photo by Tsogtbaatar Khishigdorj).

FINANCE SECTOR STABILITY

Mongolia's financial system remains vulnerable to shocks. Thus, the government has prioritized the creation of a stable financial system, and ADB has supported this effort. Key to ensuring financial stability is the creation of a deposit insurance system. ADB led efforts to establish a deposit insurance framework for banks through the creation of the Deposit Insurance Corporation of Mongolia in 2013.¹¹

Since 1992, a key focus of ADB support has been to strengthen the regulatory framework for finance sector supervision. This assistance includes substantial and ongoing capacity development for

the Bank of Mongolia and the Financial Regulatory Commission, to allow them to more effectively supervise financial institutions.

The financial stability framework of Mongolia is evolving, and it is overseen by the Financial Stability Council (FSC). Established in 2013, the FSC consists of heads of the Ministry of Finance, the Bank of Mongolia, and the Financial Regulatory Commission. Through TA, ADB supports the FSC secretariat in building the analytical tools and capacity to perform rigorous macrofinancial monitoring and surveillance, and helps clarify its legal range of responsibilities and composition.

Mongolia is prone to commodity boom-bust cycles, and economic policy management responses have been not effective in the past. Such cycles have a detrimental impact on financial stability.

Through capacity development, policy advice, and training, ADB supported restructuring processes in the Bank of Mongolia to carry out policy decisions in monetary and foreign exchange. An effective public communication strategy was also developed within the Bank of Mongolia's Center for Public Education and Information.

⁸ ADB. 2009. *Proposed Technical Assistance to Mongolia for Policy and Institutional Support for Banking Sector Systemic Risk Management*. Manila (financed by the Japan Special Fund).

⁹ ADB. 2011. *Technical Assistance to Mongolia for Government Bond Market Development*. Manila.

¹⁰ ADB. 2008. *Mongolia: Capital Markets Development*. Manila.

¹¹ ADB. 2009. *Technical Assistance for Deposit Insurance Establishment*. Manila.

PRIVATE SECTOR FINANCE

As a catalyst for private investments, ADB provides direct financial assistance to public sector and nonsovereign private sector projects in the form of direct loans, equity investments, guarantees, B loans, and trade finance. Since its inception, ADB has approved a total of \$96 million for four private sector projects in Mongolia's finance sector.

ADB's Trade Finance Program (TFP) fills market gaps by providing guarantees and loans through partner banks in support of trade. In Mongolia, the TFP works with two banks and has supported almost \$235.9 million in trade involving 485 transactions as of December 2017. In addition to filling market gaps, the TFP's objective is to mobilize private sector capital. In 2017, 50.2% of the \$235.9 million in trade supported through the TFP was cofinanced by the private sector.



Production facility of clothes for import. The Agriculture and Rural Development Project also supports facilities that manufacture consumer goods for the international market (photo by Tsogtbaatar Khishigdorj).

Mongolia: ADB Operations in the Finance Sector

(as of 2017)

No.	Project Approval Number	Project Name	Net Amount (\$ million)	Milestone Dates	
				Approved	Closed
Loans					
1	3072	Payment System Modernization	20.00	26 Nov 2013	Ongoing
2	3533	Banking Sector Rehabilitation and Financial Stability Strengthening Program	100.00	30 May 2017	Ongoing
3	7259	Mongolia: Loan to Khan Bank	10.00	2 Aug 2007	16 Nov 2013
Technical Assistance					
4	2720	Strengthening the Supervisory and Restructuring Capacity of the Bank of Mongolia	1.00	19 Dec 1996	31 Dec 2001
5	7479	Transformational Mobile Banking Services	0.40	18 Dec 2009	31 Aug 2016
6	9320	Banking Sector Rehabilitation and Financial Stability Strengthening Program	1.50	30 May 2017	Ongoing
7	3397	Rural Finance	0.70	2 Feb 2000	31 Dec 2001
8	1536	Advisor to Mongolian Stock Exchange	0.10	17 Jul 1991	31 Dec 1993
9	7971	Government Bond Market Development	1.00	14 Dec 2011	30 Apr 2015
10	9000	Supporting the Credit Guarantee System for Economic Diversification and Employment	0.80	27 Nov 2015	Ongoing
11	7337	Deposit Insurance Establishment	0.50	27 Aug 2009	18 Mar 2013
12	9180	Supporting Financial Sector Development Stability	1.55	26 Sep 2016	Ongoing

Source: Asian Development Bank.



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