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# MONGOLIAN ECONOMY

NOVEMBER, 2014, ISSUE №19 (077)

## STOCKS

IPO: ICEBREAKER OF THE MARKET

## MICRO-FINANCE

EXPANDING NON-BANK FINANCIAL SERVICES

## OPINION

MONGOLIAN STOCK EXCHANGE REFORM AND FUTURE PROSPECTS

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## EDITOR'S NOTE



Four years ago, everyone said it was impossible for Mongolia to develop its financial market. Mongolia's financial sector only had banking services to offer, they said—other parts of the sector were too weak to be called a service. Developing insurance and investment funds, many cried, were too far from reality. The country lacked the proper legal environment, as well as professional human resources—and accounting standards were just dream, never to come true.

Times have changed. Although stock market development has yet to make a breakthrough, the financial sector has shown radical change in recent years.

Mongolia is celebrating the 20th anniversary of the establishment of its first financial regulatory institution. Mongolian Economy's latest issue presents the facts and statistics on securities regulation and monitoring operations, and detailed information on how to improve the latest results.

In the early 1990s, during government privatization, 475 factories and enterprises were first listed for public trade, with few restrictions. This later formed the basis of today's Mongolian Stock Exchange. After 20 years, the time has arrived for cleanup, regulation and responsibility. Since 2011, both the Mongolian Stock Exchange and the Financial Regulatory Commission (FRC) have been trying to bring order to companies that have been operating carelessly without abiding any laws or rules. Currently there are 304 companies whose shares are registered at the Financial Regulatory Commission, of which 200 are listed on the Mongolian Stock Exchange and participating in trade. The cleanup process is still in full swing at the Exchange. When the dust settles, only companies that are responsible and transparent will keep their place at the Exchange.

With the government's decision to distribute 1,072 shares from Erdenes Tavantolgoi to every citizen in 2012-2013, the number of brokerage and dealer companies rose overnight. Reduction is part of the FRC's cleanup. In addition, the insurance sector, also monitored by the FRC, has seen major positive change as well.

Savings and credit cooperatives earned a bad reputation a decade ago, when many went bankrupt without returning people's lifesavings. Now such cooperatives are regaining their status, by making quality service their priority, under the oversight of the FRC. Officials are promising that savings and credit cooperatives won't face bankruptcy again—not in the new regulated environment. And non-bank financial institutions have seen expansion, nowadays helping an ever-growing number of people meet important monetary needs. Last but not least, the implementation of the Securities Market Law and the Investment Fund Law are sure to bring positive results. Read all the details in our latest articles.

The future for Mongolia's economically vital financial market is shining bright. However, it depends on many factors to continue its development. The current legal framework and ongoing government development must strengthen in tandem with the financial knowledge of Mongolian citizens.

DEPUTY EDITOR I. OTGONJARGAL

The "Best Magazine of 2013" as awarded  
by the Mongolian Journalists Association



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- Altantulkuur bookstore
- Nomin supermarkets
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- Bileg store
- Grand Plaza supermarket
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- Grand plaza
- Metro mall
- Sky supermarket
- Ulaanbaatar store
- Max mall

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## MONGOLIA

## Stockholders



Although 780,000 Mongolians have an account at the Securities saving organisation, only 10,000 are active participants in the stock market, involved in trading and receiving yields. The vast majority have little participation in the market. The uninvolved include those who earned stocks through the red and blue voucher programmes in early 1990's, when formerly state-owned companies privatised through auctions and the vouchers were used to buy shares. Decades removed from privatisation, however, most are unaware whether or not they have shares. Interested shareholders can withdraw money from their account at the Mongolian Securities Clearing House and Central Depository.

## New custodian banks



The Financial Regulatory Commission (FRC) has given permission to Golomt Bank and Trade and Development Bank to become custodian banks. Khaan Bank is in the process of requesting permission to become a custodian. Custodians hold

in safekeeping assets and securities, and arrange the settlement of any purchases, sales or deliveries of such securities. Custodians pay dividends and other payments and ensure shareholders' rights and interests. There are advantages to custodian banks in terms of enhancing interest of foreign investors to dive into the Mongolian capital market, safeguarding capital and investment funds, and preventing illegal expenditures of investment funds.

## Delisted



The Financial Regulatory Commission has removed a total of 165 companies and brokerages from its listings. Previously, trading of companies Tsastu, Chimbai, Raznoimpex, Tuul Bayan, Monel and Modlog had been suspended while awaiting a final verdict. According to the judicial decision, the FRC has officially delisted the companies from the Mongolian Stock Exchange listing according to resolution 375 as of the 21st of October.

## Foreign currency auction

The Foreign Exchange Auction is a policy instrument of the Bank of Mongolia (BOM) designed to improve the transparency and efficiency of the foreign exchange market and to stabilise foreign exchange rates. The BOM holds foreign exchange

auctions on Tuesdays and Thursdays (if the day falls on an official holiday, then on the preceding business day). Eligible bidders in the auction are restricted to domestic commercial banks. The BOM provides necessary information for domestic market participants to maintain stability of the foreign exchange market and to prevent high fluctuations of the foreign exchange rate.

## Insurance

As of the third quarter this year, private insurance sector capital has reached MNT 135.1 billion, 1.2 times more growth compared to the same period last year, according to a new report on the insurance sector released by its supervision agency, the Financial Regulatory Commission. The total active capital of insurance companies reached 49 percent, a year-on-year increase of three percent. FRC officials say this demonstrates the improvement of control and inspection within the sector. However, there are some troubling trends. Income from driver's responsibility insurance makes up 18 percent of total insurance income; yet reimbursement of driver's insurance accounts for 34 percent of total reimbursement insurance. The insurer's loss ratio reached 42 percent, about 1.6 percent higher than during the same period last year.

## Students

For the 20th anniversary of the establishment of Mongolia's financial control and regulatory



agency, the FRC and the Non-Banking Financial Institution Association have collaborated to announce the "Seeking intelligence" academic research forum for all Ulaanbaatar universities and college students. The forum aims to evaluate student research and study projects, to develop students' creative thinking and deepen their practical and theoretical knowledge. Students who are studying and interested in learning banking, finance, microfinance, marketing, management and the economy are welcome to join.

## New Bankers Association logo



The Mongolian Bankers Association approved their new logo design after their board meeting of the 23rd of October. The brand new logo was created to be conceptually geometric, eternal, and complete. With rounded angles and an appearance of shaped flexibility, the logo's form expresses solidarity and harmony. The overall circular coin shape presents the Association as a professional union of many banks, organisations and financial institutions.

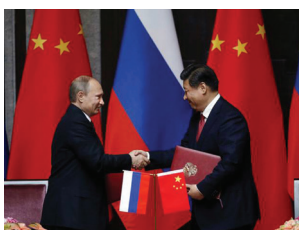
## WORLD



### Shanghai-Hong Kong stock connect

An exchange link is to open this week between Hong Kong and Shanghai, a big step for mainland China toward attracting foreign capital and opening domestic stocks to global investors. The newly allowed direct trading of Shanghai shares has a start date of November 17th, and an initial set cap of USD 2.1 billion per day. The current restrictions on over 500 Shanghai-listed shares are to be eased to allow foreign trading. The Stock Connect will boost global use of the yuan and increase Shanghai's status as an international financial center. In advance of the opening, the much anticipated link has already lifted the two bourses and increased the strength of the yuan.

### Neighbors sign gas deal



Presidents Vladimir Putin and Xi Jinping have signed a major trade agreement that will see China become the world's largest consumer of Russian gas. The gas is to be supplied through Russia's western or 'Altay' route, able

to pump 30 billion cubic meters per year once fully operational. With construction on an eastern Siberian pipeline already underway, the gas to be delivered to China will be larger than the current volume exported to Europe. The Memorandum of Understanding is one of 17 agreements signed by the Chinese and Russian presidents during November's Asia-Pacific Economic Cooperation summit in Beijing, their fifth meeting together this year. The gas pipelines are to encircle and bypass Mongolia on its western and eastern borders.

### Turquoise Hill update



Kay Prisetly is to step down as CEO of Turquoise Hill Resources Ltd., the company responsible for the Oyu Tolgoi copper, gold and silver mine. Chairman David Klingner is also stepping down. The corporate restructuring comes after over a year's worth of delays on the phase two, USD 5.4 billion underground expansion of the mine. Stock prices slid in the week after the Mongolian Parliament's early November vote that led to Prime Minister N.Altankhuyag's ouster. Quarterly earnings of Turquoise Hill (NYSE:TRQ) show a decrease of two cents per share, despite increased revenue in Q3 2014 totaling USD 466 million after royalties. In Q3 2013, the

mine generated no income, and posted losses of nine cents per share. Before TRQ dropped too far in November, however, the recent news of R.Amarjargal's apparent selection by his party as the new PM appeared to rally shares back into positive territory for the year. With Ch.Saikhanbileg now a lock for PM, TRQ shares are expected to stabilize.

### US at APEC and G20

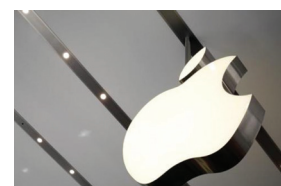
US President Barak Obama's "pivot to Asia", when initiated in 2011, was to be a new cornerstone of American foreign policy by making Asian regional concerns a top priority. Yet with crises elsewhere in the world, the pivot has seen a lack of focus, amounting insofar to the expansion of US naval presence in the region, in locations from Australia to the Philippines. The heightened US presence comes in the face of increased Chinese expansion and maritime disputes in the China seas. In an apparent policy move focused on Chinese containment, 60 percent of US Navy warships are to be stationed throughout the region by 2020, according to the Pentagon. However, at November's Asia-Pacific Economic Cooperation forum in Beijing and the G20 summit in Brisbane, Australia, the US looks to redirect its policy toward growing its economic and diplomatic relationship with Asia.

### Asia top performer in world stocks

With the global economy still staggering out of a recession, Asian stock markets have become the best 2014 performers, with

average gains well above the 10 percent benchmarks of the US, Europe, and other emerging-market regions, according to the Wall Street Journal. Strong continued economic growth and positive reforms have led to skyrocketing gains in the Philippines, Thailand, and Indonesia, with India reaching a high of 32 percent amidst a climate of optimism thanks to popular new Prime Minister Narendra Modi.

### Apple could buy entire Russian stock market



Apple Inc., maker of the iPhone and iPad, has single-handedly surpassed the Russian stock market in worth, at USD 652 billion to USD 531 billion in respective valuations, according to Bloomberg News financial data. The Russian economy has taken a recent hit due to political conflicts with Ukraine and the West that have led to a dramatic stock market slump—an over 30 percent drop in 2014, at a loss of USD 231 billion. If Apple stock, also posting higher valuations than Singapore and Italy, were to be sold in its entirety, there would be enough money to purchase every listed share on the Russian stock market, with enough left over to buy every Russian citizen an iPhone 6. Apple gains are expected to increase, while Russia is likely to face a recession as western sanctions continue and the worldwide price of oil remains low. ■

## MESSAGE OF THE CHAIRMAN

On the occasion of the 20th year anniversary of the establishment of the financial regulatory institution in Mongolia, I would like to extend my sincere greetings to you on behalf of the Financial Regulatory Commission staff members and myself for your contribution toward development of the financial sector and close cooperation in the industry. In 1994, the Parliament of Mongolia approved the first Law on Securities Market, which was the starting point for establishment of the Securities Exchange Commission of Mongolia. The Securities Market law approval was also an invitation for market participants to enter into this new market. The Securities Exchange Commission of Mongolia had responsibilities to regulate capital market stakeholders, supervise, protect investor's rights and provide information for relevant stakeholders. The Financial Regulatory Commission of Mongolia was established on November 2005 under the Law on the Legal Status of the Financial Regulatory Commission by the Parliament of Mongolia and under the resolution 45. Approval of the Legal Status of the Financial Regulatory Commission provided a ground to extend the Securities Exchange Commission activities into insurance, microfinance activities.

As a result of this change, Bank of Mongolia's Non-Banking Financial Institutions and Savings and Credit Cooperatives Department, Specialized State Inspection Authority's Insurance Supervision Department merged into Securities Exchange Commission of Mongolia. Unification of these departments established a consolidated non-banking financial supervision and regulatory statutory institutions in Mongolia.

During the era of the Securities Exchange Commission of Mongolia, there were 29 broker and dealers companies in 19 provinces and 3 cities. However, as of now, there are 2540 legal entities operating in the securities industry, 17 insurance companies and 3552 professional intermediaries operating insurance sector and 362 Non-Banking Financial Institutions, 142 Savings and Credit Cooperatives are being regulated by the Financial Regulatory Commission of Mongolia.

It is our pleasure to inform you that, this year we have become a full signatory member of the International Organization of Securities Commissions (IOSCO) as well as International Associations of Insurance Supervisors (IAIS). Becoming a member of the IAIS and a full signatory of the IOSCO highlights that Mongolian financial sector development has progressed significantly and it also requires that FRC needs to strengthen its responsibilities in the future.

Once again, I would like to extend my heartfelt greetings to you on the occasion of 20th anniversary of the financial regulatory, supervisory institution establishment and wish you happiness and health in your life



CHAIRMAN OF THE FINANCIAL  
REGULATORY COMMISSION  
OF MONGOLIA

BAYARSAIKHAN.D

## STOCKS

# IPO: ICEBREAKER OF THE MARKET



Photo by B. Byamba-Ochir

On the trading floor of the Mongolian Stock Exchange.

BY B. ENKHTSETSEG

Despite the severe Mongolian cold, young retailer Bold is outside almost every day, shouting as loud as he can for the attention of passersby, trying to sell his handmade wooden carvings and furniture at the Narantuul flea market. His dream is to expand his current small business and establish a small factory. Years later, this young man could become the chairman of the board of a huge public company, fruitful to many, known to the whole country as well as the world as a leader in Mongolian brand products. Every success starts with a dream.

The dream remains a dream, however, when many hurdles stand between reality and opportunity. Today, Mongolian business makers mostly choose bank

loans when starting or expanding their operations, due to the relatively easy process of applying for a bank loan. Yet many are unaware of the risks—such as high interest rates, back pay, and the ever-increasing exchange rate gap—that wait for them once they sign on the dotted line.

## Going public

Commonly referred to as an initial public offering, or IPO, going public is a financing alternative that most company CEOs consider, but few choose to pursue. IPOs are an icebreaker, the first sale of stock by a private company to the public. Investment is equal in value to bank loans, and often better in many ways, as public companies can achieve long-term financing with no interest rate pressure.

Going public for the first time is like riding a skateboard. If you have a certain level of skill, timing, preparation and luck, you'll go much further and faster than you could ever have hoped. But if your timing is wrong, you run out of luck, or you ignore your coaching, you could wind up bruised and on the ground.

Several IPOs on the Mongolian Stock Exchange (MSE) can be pointed to as successes. BDSec first issued their stocks on the primary market in 2008, and saw their total raised capital reach MNT 750 million. Meanwhile, their market capitalization was worth up to MNT one billion. After two subsequent sales of shares since their initial offerings, BDSec's market cap now stands at MNT 27.4 billion.

The higher the market capitalization ►

► (market cap), the easier it is to buy and sell large blocks of stock without disturbing the market. Hermes Center raised MNT 2.3 billion in 2008, and had a market cap of 7.8 billion at the time. This figure has been doubled to reach over MNT 14 billion.

Despite the success, the securities market of Mongolia has not seen any big IPO for the past few years aside from BDBSec's extra stocks. These days, Mongolian companies do not even dare to consider an IPO in such a time of economic difficulties. But many experts say that this is the time that should be dedicated to preparing an IPO, so that it can be launched when the appropriate economic conditions arrive.

### Legal environment open, and waiting

“In terms of laws, resolution and regulations, there is no barrier in the stock market to do an initial public offering and other kinds of securities”

said, T.Jambaajamts, Acting Director of the securities market department of the Financial Regulatory Commission.

Last year, the Mongolian Government passed a new version of the Securities Market Law. The Law is a milestone in the 22 year history of the capital market in Mongolia. Its aim is to attract the required investments to develop Mongolia, and to provide conditions for better financial liquidity that would be comparable to other Asian stock exchanges. The key developments of the new Law are the dual listing approval, depository receipt (DR), custodian banking activities, and stronger control of all the activities by the State regulatory authorities. With the law passed, Golomt Bank and Trade and Development Bank of Mongolia are now permitted to supply custodian services, removing the need for individual custodians. The FRC informs that these two banks are now undergoing technical preparation. Despite the open opportunity now for dual listings, no company has made the

attempt to be registered as such.

One would think the milestone law would inspire more private companies to become public. On the contrary, companies have refrained, worrying over a would-be lack of any investors to buy their shares. The Investment Fund Law, passed last year, is seen as a key measure to bring more potential players into the market. One of the biggest players in the stock market, investment funds are led by professional investment managers, which may potentially offer better returns and more adequate risk management. Pension funds are especially important to stock markets worldwide, where large institutional investors dominate. There are over 300 pension funds that collectively hold about USD 6 trillion in assets. Pension fund investment is legally open for business. Although, the law was approved a year ago, Mongolia has not had any kind of fund fully established as of today. Only two companies have obtained permission to launch an investment fund. The Mongolian stock market has expanded its number of players, although it may take time for investment fund development to get up and running.

T.Jambaajamts, Acting Director of the securities market department, FRC, says that in the beginning, undoubtedly, foreign investors will show a greater interest in investment fund business. They are particularly interested in building investment funds that invest in gold, real estate, stock and government bonds. However, the unstable investment environment and poor macroeconomic indicators still frighten away investors.

### Privatisation boost

What the stock market needs today is not investors to attract but products to show off. While private companies dare not break the ice, privatising a state-owned company through the MSE is thought by many to be the most fruitful way to promote the stock market, while simultaneously decreasing government shares in state-owned companies. With only four chosen for public trading on the MSE out of 22 state-owned companies, according to listings valid for 2014-2016, many are hoping for more. ►►



Photo by B. Byamba-Ochir

### Raised through initial public offering

№	Symbol	Company name	Issued shares	Listed Date	Raised through initial public offering			Market cap as of an IPO announced day	2014/11/06 closing price	Market Cap by 2014/11/06
					Total number of shares	First price offer at the market per share / MNT/	Total raised /MNT/			
1	MRX	"Merox" JSC	65 005 000,00	2014-01-14	26 000 000,00	100,00	2 600 000 000,00	6 500 500 000,00	100	6 500 500 000,00
2	ETR	"E-Trans Logistic" JSC	46 200 000,00	2012-04-09	7 700 000,00	120,00	924 000 000,00	5 544 000 000,00	90,9	4 199 580 000,00
3	MDR	"Mongolian Development Resource" JSC	13 750 000,00	2010-06-30	13 750 000,00	1 000,00	13 750 000 000,00	13 750 000 000,00	520	7 150 000 000,00
4	HGN	"Khukh Gan" JSC	101 317 557,00	2008-07-30	30 395 272,00	105,13	3 195 456 280,00	10 651 519 216,21	117	11 854 154 169,00
5	NKT	"Naco Tulsh" JSC	11 000 000,00	2007-11-29	9 000 000,00	100,00	900 000 000,00	1 100 000 000,00	285	3 595 480 485,00
6	RMC	Remicon JSC	127 642 623,00	2008-05-19	50 480 202,00	100,02	5 048 820 200,00	12 766 285 154,39	100,81	7 931 676 765,84
7	HRM	"Hermes centre" JSC	78 543 001,00	2008-05-16	23 562 900,00	100,00	2 356 290 000,00	7 854 300 100,00	179	14 059 197 179,00
8	OLL	"Olloo" JSC	9 700 497,00	2007-09-12	5 820 299,00	100,00	582 029 900,00	970 049 700,00	111	1 076 755 167,00
9	HBO	"HBOII" JSC	5 000 000,00	2007-05-02	4 000 000,00	100,00	400 000 000,00	500 000 000,00	391	3 610 598 788,00
10	BDS	"BDSec" JSC	10 000 000,00	2006-06-22	7 500 000,00	100,00	750 000 000,00	1 000 000 000,00	2499	27 489 000 000,00
11	JTB	"Genco Tour Bureau" JSC	100 000 000,00	2006-01-17	78 895 885,00	104,69	8 259 239 676,00	10 468 530 362,52	86,5	8 650 000 000,00
12	MSH	"Mongol Shiltgeen" JSC	10 000 000,00	2005-05-25	1 000 000,00	800,00	800 000 000,00	8 000 000 000,00	649,96	6 499 600 000,00
		Sum					39 565 836 056,00	79 105 184 533,12		102 616 542 553,84

► The director of the state property management department at the State Property Committee, D.Bolormaa, says: "We intend to decrease the state share of some companies through investment and partnership formation. It is better to evaluate the value of companies first and then make them public. It will be of no value now if we offer to sell some companies with bad governance—desperate for technological renovation and near the edge of bankruptcy—on the Mongolian stock market. We wouldn't find investors to buy stock in these companies."

According to D.Bolormaa, those four companies chosen and in preparations to be traded on the MSE from next year are said to be those with the best governance of all the 22 listed state-owned companies.

#### IPOs are the future

But the Mongolian stock market has a lot to do apart from just looking forward to a state privatization program. Public offerings of private companies are the core of the stock market. In order to promote IPOs, related regulators submitted a programme to parliament, designed to support companies undergoing an IPO as well to release them from taxes in stages. The

#### Companies, offered extra shares

№	Symbol	Company name	Listed number of shares	Listed Date	Total Raised		
					Quantity	Price Offer	Total
1	BDS	"BDSec" JSC	6 000 000,00	2014-01-15	6 000 000,00	1 931,00	11 586 000 000,00
2	SHG	"Sharyn gol" JSC	1 707 404,00	2011-10-13	1 648 257,00	11 117,00	18 301 439 069,00
3	SIL	"Silicate" JSC	16 222 300,00	2011-05-06	16 222 300,00	225,00	3 650 017 500,00
4	SHG	"Sharyn gol" JSC	1 292 596,00	2011-01-13	-	-	-
5	HBO	"HBOII" JSC	2 234 268,00	2010-08-25	570 358,00	174,00	99 242 292,00
6	NKT	"Naco Tulsh" JSC	1 615 721,00	2010-08-25	1 180 195,00	229,00	270 264 655,00
7	BDS	"BDSec" JSC	1 000 000,00	2008-06-12	900 014,00	3 000,00	2 625 346 500,00
8	HBO	"Хай би ойл" ХК	2 000 000,00	2007-11-29	2 000 000,00	100,00	200 000 000,00
9	MIB	"Монинжбар" ХК	10 000 000,00	2007-01-16	10 000 000,00	100,00	1 000 000 000,00
		Sum					37 732 310 016,00

companies that have performed an IPO now pay taxes of 10 and 25 percent of total profit. But according to the new programme, IPO listed companies will be freed from 100 percent of taxes for three years, and another 50 percent cut in the subsequent three years.

"To attract investors, there should be promotion. The question—why should we enter the Mongolian stock market?—needs to be answered and given a clear explanation as to what are the advantages and opportunities there to consider. Companies will do an IPO if they are offered a friendly environment," says, D. Dayanbilguun, CEO of BDSec.

He added that if the stock market of Mongolia turns into a zero tax environment and declares to the world that the market has become an investor friendly environment with promises to remain so for the future, Mongolia will become as competitive as other stock markets around the world.

While many experts feel that a company's achievement is the result of the concept, the product, or the service, inadequate financing of the venture severely prohibits the growth of a successful company. IPOs are a realistic option that companies must consider when expanding into the future. ■

BY BAYARTOGTOKH

This year marks the 20th anniversary of the establishment of Mongolia's financial regulatory institution, the Financial Regulatory Commission, formerly the Securities Exchange Commission. To celebrate the occasion, Mongolian Economy magazine invited D. Bayarsaikhan, Chairman of the Financial Regulatory Commission of Mongolia, to talk about the past, present and future of the sector.



Photo by B. Byamba-Ochir

## GUESTS

# PROGRESS IN MONGOLIA'S FINANCIAL MARKET

**It has been 20 years since the establishment of the Mongolian Securities Exchange Commission. What important role has the commission played in the history of Mongolia's financial market?**

The Mongolian Securities Exchange Commission, the first regulatory institution in the financial sector, was established in 1994. It has been 20 years since then. During this time the economy of Mongolia has faced major changes. Related to such changes, capital assets in the financial market grew as well. This required increased responsibility and monitoring from the regulatory institution. The Securities Exchange Commission fulfilled its duties very well during its operational period of time. It brought beneficial results to society too. The Commission was established during a period of privatization, approved the very first Securities Law, and developed associated regulations and rules. This brought about the era, as we used to say, of big privatization, where people were given pink and blue vouchers for purchasing shares of formerly state-

owned companies. During this period about 475 shareholding companies were established. These formed the basis for the current stock exchange. At that time, the Microfinance Department from the Central Bank and the Insurance Department from the General Agency for Specialised Inspection were supervised by the Securities Exchange Commission, which later meant the establishment of the current Financial Regulatory Commission.

**Both the economy and society have witnessed major changes over the past two decades. Would you sum up a few of the changes in your field?**

The private insurance sector, which our agency supervises, is a viable example. During the establishment of the Commission there were 21 insurance companies operating. Their financial competence was weak, their market was idle, and they were vulnerable to risks. Today, there are 16 companies that are capable of taking on risks and competing in the highly competitive market. This is just one example of what has changed in

the past 20 years. As for the Commission, it is traditionally not allowed to regulate the operation of any commercial banks. Recently, it has been granted approvals for banks. I think this is also one of the developments we are talking about. As banks request for insurance or custodian operation licenses, banks begin to enter the Commission's regulatory activities. Corporate governance is also one of our subsectors. The Commission approved the national governance codex. Additional changes related to governance were added to the Company Law. Mongolia was also once one of the countries with no regulated insurance system. Regulated driver's responsibility insurance was legalized within the last three years. Basically, a regulated insurance system was established. Sector associated laws were revised and reformed in the past six years. The law on non-bank financial institutions (NBFIs) was revised and handed to the associated institutions. The Securities Market Law and Investment Fund Law are being implemented.

**What stage is Mongolia's securities** ▶▶

► **market in within the global legal environment?**

Both the Securities Market Law and the Investment Fund Law were implemented last January. Since then, the associated regulations and rules have been approved and implemented. The approval of these laws has brought Mongolia's securities market to a stage where it is recognised internationally. As result, Mongolia has become a full member of the International Organisation of Securities Commissions. This means that Mongolia is able to cooperate with other member countries equally and can more openly exchange information. Mongolia's legal environment is accepted internationally.

“About 95 percent of the financial market consists of the banking system. This is called a banking dominated system. Importantly, a stable and multi-based financial system must be created. This should include a developed stock market and insurance system.”

**How do you see the short and long term prospect of the financial market? With the current pace, how near are we to our ideal market?**

About 95 percent of the financial market consists of the banking system. This is called a banking dominated system. Importantly, a stable and multi-based financial system must be created. This should include a developed stock market and insurance system. Recent studies suggest that Commission regulated institutions have been showing growth. This has been continuing for the last 10 years. The insurance sector's indexes show increases as well. NBFIs are showing profits too. Besides supporting successful sectors, weaker parts of the market must be developed as well. This would ensure a balanced market. Yet financial market development depends on many aspects. For example, the knowledge of citizens has to be improved. The Commission, in cooperation with the Asian Development Bank and other organisations, is implementing a project to enhance citizens' knowledge of the financial market. We are expecting

positive results.

**Shares of certain companies, sold at the stock market, are often centralised in one hand, say many. In other words, one person holds the majority shares of certain companies. Wouldn't this situation make the securities market idle?**

Stock exchanges have their own registration requirements. According to Mongolian Stock Exchange (MSE) requirements, 25 percent of a listed company's shares have to be sold publicly. However, in reality that is not the case. Most Mongolian companies are run by families. They often are not fully encouraged to participate in the market. Such companies, with up to 90 percent of their shares centralised in certain hands, will have to fulfill the before mentioned requirement. To do so, they will have to issue more shares or expand or divide their shares in order to activate sales. After that they must pay attention to their products. State-owned companies should be privatised through the MSE, since it is more effective, concerning corporate governance. The government should take this into consideration. The advantage of being transparent is that the company is able to attract more investment.

**Traded companies Monel and Ulaanbaatar have been withdrawn from MSE listings. Is this a cleanup?**

Listed companies are not there for keeping. The market should be for those companies that have good corporate governance, share dividends frequently with the public, have transparent operations, and have active participation in the market. Companies such as Monel and Ulaanbaatar, that have inactive trade or whose shares have fallen mostly into a single hand, or whose owners have requested for withdrawal—they leave the market. We have taken legal steps and settled the issue. In addition, we have cancelled licenses of many brokers and dealers. With state-owned Erdenes Tavan Tolgoi's 1,072 shares to be distributed, many brokers and dealers companies, without considering any risks, were established. Now that the trade is put on hold, they are not able to manage their costs. Some of them haven't traded a single share in a year. For that reason, some licenses were cancelled according

to the legal requirements. At one time, broker and dealer companies had reached upwards of 90. Now the number has decreased to 60. For those companies that have closed, their removal was solved basing on the fact that they did not have their board meeting, or their owners requested to close. Otherwise, the Commission will not close, stop trade, or close down any company by force.

**Recently, Golomt Bank and Trade and Development Bank were granted special licenses to operate as custodian banks. Will other commercial banks follow in their footsteps?**

Legally, it is an open possibility. However, it comes with great responsibility. Not any institution can take on this challenge. This requires multifaceted services such as keeping securities and distributing dividends, to name a few. It is different from a commercial bank's daily basics. So it must be handled with caution and care. According to recent information I've received, Khaan Bank is applying for a custodian license. Khaan Bank has many branches throughout the country. This means the service will reach more customers. The custodian market is based on the securities market. Thus banks that have both financial and HR capacity and have met the requirements should be able to obtain the license.

**Early next year two investment funds are expected to be established. What changes could this bring to the development of the financial market?**

Two management companies have received their approval from the Commission to establish investment management companies, with the purpose to establish investment funds. The Investment Fund Law states open funds must receive a special license, while closed funds are to be registered. Legally, the environment has become freer. The most important thing is that market participators must apply to professional organisations. In addition, if there are more such funds with very good research and clear goals to participate in the market, there would be a good example set. As stated in the Investment Fund Law, the money from the participants will be placed in the custodian bank. This is one of the key infrastructure issues to attract foreign investment. ■

## MICRO-FINANCE

# EXPANDING NON-BANK FINANCIAL SERVICES

BY S. ZAYA

Banks lend to those who have money and collateral. Non-bank financial institutions give opportunities on rather flexible conditions for those who cannot meet the requirements of banks—although compared to loans from big banks the amount is rather small. As such, non-bank financial institutions (NBFIs) have become an ideal loan source for people with low- to middle- incomes.

Although use of NBFIs services has increased over the past few years, often the people who have the greatest need are those with the least knowledge of those services. In rural areas, especially, knowledge is lacking, and must be improved. Parliament first approved a law on non-bank financial institution services in 2002. Operational licences have since been given by the Financial Regulatory Commission (FRC) of Mongolia. Currently, NBFIs offer 10 types of services, including granting loans, transferring money, issuing payment guarantees, investing in short term facilities, and advising clients. NBFIs use mostly their own assets—up to 70 percent of their total working assets are usually their own. As of the third quarter 2014, 351 NBFIs are in operation in Mongolia, with assets of MNT 489.9 billion in total. Of these, 15 organisations have the most assets, making up to 60 percent of the total floating capital. The NBFIs work with 518,600 customers, with a total credit balance of MNT 293.9 billion. In addition, 87.4 percent of total granted loans are regular, while 6.6 percent of loans are overdue and 6.1 percent are default.

It takes time before someone can get a loan from a standard bank. NBFIs operate on the spot. In doing so, such



Photo by B. Byamma-Ochir

A non-bank financial institution.

organisations assess collateral much higher than banks do. Although NBFIs offer quick service, they ask for high interest. Granting loans are the primary service of NBFIs, with currency exchange second.

## Expansion outside Ulaanbaatar

The Financial Regulatory Commission sets the minimum for the equity fund when giving a licence to a NBFIs. For example, if a person wants to open a NBFIs in Ulaanbaatar, the equity fund should have at least MNT 400 million in monetary assets. In smaller cities such as Baganuur, Bagakhangai, Nalaikh, Erdenet or Darkhan, the assets should be MNT 200 million, while in more rural provinces the requirement is MNT 50 million, and MNT 20 million in soums. The Commission has set different sums depending on the region in order to expand NBFIs micro-services in rural

areas.

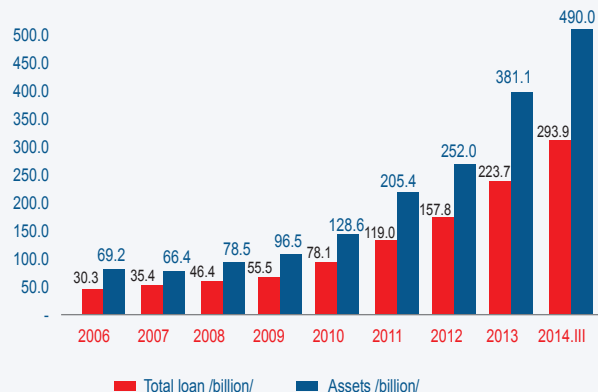
While there are about 26 NBFIs in rural provinces, most citizens lack knowledge and information about how to use their services. To combat this lack of understanding, the FRC, in cooperation with the Asian Development Bank, organised events to promote and introduce the essentials of NBFIs to citizens of over 70 soums in 9 provinces. After the events, many citizens expressed their interest to open their own NBFIs. "There are people with MNT 20 million, 50 million in rural areas," said N.Oyunchimeg, director of the microfinance department in the FRC. "They often don't know what to do with their money. When introduced to the market, they show a great interest in entering it."

Over the past two years, the number of NBFIs has increased by 200. The customers, previously up to 50,000, has reached 500,000. ▶▶

General information on non-bank financial institutions



Total credits and assets of NBFIs (billion/MNT)



## Revising the outdated law

Despite the progress, development of NBFIs has been slow due to obstacles present in current Mongolian law. To develop the market, the law needs revisions to update the original 2002 measures. The FRC has drafted such a revision, which has been handed to the government for review. Unfortunately, parliament has postponed the draft bill several times.

According to the draft, NBFIs are to be divided into three categories; foreign currency, credit, and organisation. The equity assets and requirements will differ depending on the category.

Currently, the equity asset for a NBFIs is low. With the new law, the amount will be renewed. The Mongolian Non Banking Organisation Association has requested to increase the level of equity assets, because an increased establishment of NBFIs might have a negative effect on the market and its reputation. N.Oyunchimeg remains optimistic about the draft bills potential.

“If the new law is approved, the scope of NBFIs will expand. In addition, regulations will be more flexible. Suitable regulations, monitoring, and limitations will be created.”

With the current law, one NBFIs that operates both credit and currency services must purchase two separate licences. The new law will give only one licence under the category non-bank financial institution.

In 2006, there were 132 non-bank financial institutions. Now the number has reached 351. Their floating capital increased by 10 times, making up now about 2.7 percent of total assets in the banking sector. Equity assets, which were MNT 25.6 billion in 2006, have increased to MNT 234.4 billion as of 3rd quarter of 2014—today they account for 58.7 percent of total equity assets in the banking sector.

Although, NBFIs have clearly established their own value and niche in the marketplace, legal revisions and reform are crucial to expanding the sector. ■

## MICRO-FINANCE

# FROM QUANTITY TO QUALITY

BY S. ZAYA

Savings and credit cooperatives (SCCs) differ from other non-bank financial institutions in that their status is non-profit. As a credit union, SCCs supply social and economic needs based on the collected members' own savings, investment and financing decisions. Worldwide, SCCs have nine defining principles, which serve in Mongolia too.

From those principles, SCCs are defined as a voluntary group, cooperating with other counterparts, maintaining financial stability, and ensuring fair economic participation, distribution and independence among its members.

Mongolia has had problems with savings and credit cooperatives dating back to 2005, when a number of SCCs went bankrupt, resulting in the loss of many

livelihoods. Those SCCs were corrupt and irresponsible, promising high interest rates and working for their self-interest—violating the basic principles of SCCs. Today the question is: have SCCs improved in the past nine years? There's certainly been major change. In 2005, there were 900 registered SCCs. By the end of last year, that number had been reduced to 141. In the first half of 2013, ▶▶

► SCC active capital was MNT 71.8 billion, while in 2014 the number reached MNT 76.8 billion.

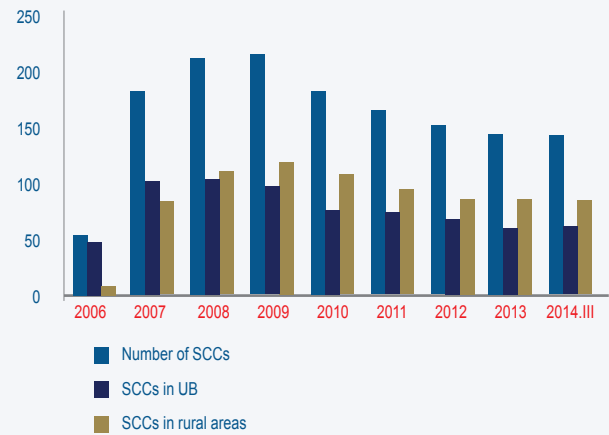
As SCC groups are democratic, member driven, self-help cooperatives, their funds stay amongst and work for their members. For that to happen as it should, members agree to save their money in the SCC and to make loans to each other at reasonable rates of interest. Members are the owners, and it's the members who decide how their money will be used and for the benefit of whom. In addition, members are helped with financing to supply their everyday needs: like starting a business, running a livestock operation, establishing a farm, furnishing a house, or improving their children's education.

Parliament passed the Savings and Credit Co-operative Law on October 27, 2011. The Financial Regulatory Commission (FRC) is the parliament mandated supervising agency that grants special permission to the establishment of an SCC. An SCC is legally prohibited to operate if the FRC grants no permission or declines to give one. Moreover, SCCs are prohibited to save money from other sources and to make loans to nonmembers.

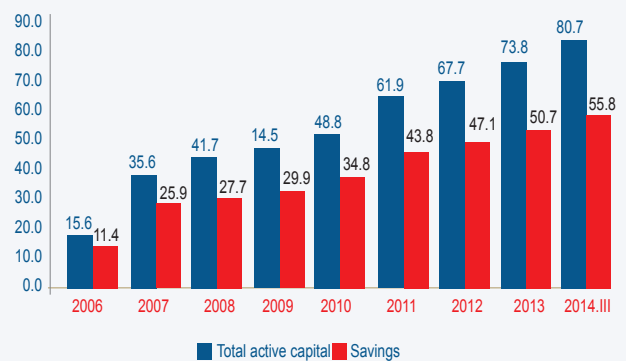
After approval of the law, the "Promoting Inclusive Financial Services for the Poor" project, financed by the Japan Fund for Poverty Reduction, was jointly implemented by the Financial Regulatory Commission and the Asian Development Bank. The overall objective of the Project is to improve access to financial services for the poor and vulnerable non-poor households in Mongolia through market strengthening and capacity building of savings and credit cooperatives, and provision of basic financial education to households nationwide. In accordance with the project, an SCC evaluation system was defined and a capacity evaluation was performed. "As a result, we have created a new model SCC that covers distances and member training," said N.Oyunchimeg, director of the microfinance department at the FRC. Within the framework of the project, they have prepared trainers and evaluators, as well as 1,000 volunteer employees, through 39 training seminars. Nine operating principles were also developed. The FRC follows up with constant distance control and on-site inspection, and is now in preparation to start



Savings and credit cooperatives, general information



Sum of total active capital and savings



inspections based on risk. "Reserve funds, saving and protection funds and stabilization funds are getting formed to prevent risk, and are being financed from year-end income of SCCs. Thus, the concept of SCC bankruptcy has vanished, as fully regulated and inspection-certified cooperatives have stepped up the next phase of development," says, N.Oyunchimeg.

Though the number of cooperatives has declined over the past decade, membership in the remaining cooperatives has steadily been increasing. FRC data from third quarter 2014 shows over 28,750 members. The belief in SCCs as viable institutions has been restored for many, say FRC officials.

Likewise, SCC membership increased by 5.5 percent, while active capital grew by 9 percent compared to the last quarter of 2013. Current active capital reached MNT 80.8 billion, with 77.2 percent of it belonging to loan packages. If we look at loan quality, 94.5 percent is normal, 2.7 percent is overdue and the rest is categorized as non-performing. The savings of all SCCs represent 0.6 percent ►

- ▶ of the banking sector, while 97 percent of SCC savings have definite terms, and the rest is demand deposit.

There are over 57 cooperatives operating in Ulaanbaatar city, and an additional 84 in throughout the rest of the country. Many lack of information about SCCs. Thus, TV programs, documentaries, handbooks, and brochures have been prepared to promote public awareness.

The Mongolian Confederation of Savings and Credit Cooperatives, established in 2007, protects the common rights and interest of SCCs, and represent its members on state and international agendas. Currently 104 SCCs have joined the union. SCCs are on the rise, and current development and regulations by the FRC have done much to restore confidence to the general public. ■

## REGULATION

# BRIEF OPERATIONAL INTRODUCTION OF THE FINANCIAL REGULATORY COMMISSION

The Financial Regulatory Commission of Mongolia (FRC) is a governmental organization that has the responsibility to ensure the stability of the financial markets, regulate financial services, monitor implementation of relevant legislation, and protect the rights of investors and clients of the financial markets. The FRC was established by the Parliament of Mongolia in 2006.

The FRC annually reports to the Parliament of Mongolia on the implementation of the law, including the financial and organizational activities, and the Parliament of Mongolia monitors whether the activities of the FRC are consistent with the relevant legislation. Moreover, the FRC submits its annual report to the Government of Mongolia and the Bank of Mongolia.

With the respect of providing financial stability as well as developing, regulating and supervising the financial market, the Bank of Mongolia, the Ministry of Finance and the Financial Regulatory



Commission signed a Memorandum of Understanding in 2006. Also, in accordance with the Law on Bank of Mongolia, the FRC has become member of the Financial Stability Council. With this respect, the FRC prepares its policy papers on the financial matters and regularly reports to the Parliament of Mongolia.

The FRC has the responsibility to provide financial stability in the market; with this respect, the FRC monitors market participants, conducts analysis on the potential risks of the markets, and, when it is necessary, conducts necessary preventive action.

The FRC has the obligation to set ▶

▶ and enforce the relevant rules and regulations in accordance with the Legal Status of the Financial Regulatory Commission of Mongolia in order to provide financial stability in the market.

The Law on Legal Status of the Financial Regulatory Commission mandates that the FRC has the responsibility to enforce laws and regulations in the market relevant to entities licensed by the Commission. In case of misconduct or violations of the laws and regulations, the FRC has the power to conduct on-site inspections and take action to clear the violations.

Within its power the FRC has the legal right to settle disputes between license holders and consumers. The revised Securities Market Law introduces a dispute resolution body at the FRC to resolve disputes among regulated entities, issuers, investors and/or customers. This introduces a non-judicial dispute resolution mechanism which may offer benefits in terms of efficient and fast dispute resolution determined by experienced market professionals.

Decisions by the FRC and complaints are monitored through the Supervisory Board, which was established by the Parliament of Mongolia. The supervisory Board submits its report to the Parliament of Mongolia on the first quarter of the year.

In the framework of exchanging market information as well as providing mutual assistance, the FRC signed several Memorandums of Understandings (MoUs) with key international and national authorities. For instance, the FRC became a full signatory of the International Organization of Securities Commissions MoU, and a member of the International Association of Insurance Supervisors. Also, bilateral MoUs were signed with the Hong Kong Securities Futures Commission and Financial Services Agency of Japan this year. In the past, the FRC signed MoUs with following financial regulatory authorities: the Financial Services Commission of the Republic of Korea, the Agency of the Republic of Kazakhstan on Regulation and Supervision of Financial Market and Financial Organizations, the China Securities Regulatory Commission, and the Polish Financial Supervision Authority.

The FRC has defined its market strategic policy on regulated industries such as securities and insurance, microfinance markets. Also, the Financial Regulatory Commission's operational strategic plan for 2012-2016 was approved on April 22, 2012.

This market policy paper has defined the Financial Regulatory Commission's mission to: "Develop a stable financial market that is in line with the international best standards which is accepted by international stage".

In international practice, the financial regulatory bodies have key objectives to regulate, enforce supervisory duties, provide financial stability in the market, protect investors' rights, and reduce systemic risks. These key regulatory objectives have been specifically placed in the operation plan of the FRC which are being enforced by the market participants.

## Securities Market

To have a strategy to enforce and implement the International Organizations of Securities Commissions principles and standards; by enforcing these principles and standards, the FRC will strengthen its relevant market laws and regulations.

- Strategy to reform intermediaries market
- Strategy to reduce systemic risks and take preventive actions
- Strategy to learn international best practices on the securities issuers

## Insurance Market

- To introduce risk based approach on the supervision of the insurance market
- To have a strategy to transfer some of the FRC duties non-governmental organizations and find relevant stakeholders who can implement

## Microfinance Market

- To have strategy to implement inclusive financial policy and to prepare regulatory model.
- To have a strategy to improve legal environment of the microfinance industry
- To have strategy to assess legal environment of transferring duties non-governmental organizations

These are the strategies of the sectors, and these strategies have defined the operational strategy of the FRC, and these are currently being enforced.

The FRC has been operating legal environment of Mongolia as well as in the framework of the international standards. The FRC is preparing rules and regulations that are suitable to current conditions of the market; its policies and regulations are flexible for market participants. The FRC is working hard to create transparent and diversified economic structure in Mongolia. ■



## INTERVIEW

# AN UNDERDEVELOPED STOCK MARKET POSES BIG RISK

We talked with Ganzorig Ulziibayar, President of ACI Mongolia Financial Markets Association. Ten years ago he founded the Association with other experts in the field to work as a leadership body to enhance knowledge and skills in Mongolia's financial marketplace. He also serves as President of Mandal Financial Group, Chairman of United Mongolian Corporation (UMC Group), on the Monetary Policy Committee of the Bank of Mongolia, and on the Capital Market Policy Committee of the Financial Regulatory Commission (FRC). He graduated the Institute of Commerce and Business majoring in Accounting, and completed postgraduate studies in Financial Management at the Maastricht School of Management in the Netherlands.

### **What are the responsibilities and priorities of the FRC's Capital Market Policy Committee?**

The most important issue facing the Mongolian economy is the development of the stock market. The stock market is the best mechanism to supply rightful resource distribution. Unfortunately, due to the current development process of stock market, rightful resource distribution has become a vulnerable issue. The lack of a mechanism to rightfully distribute resources will affect negatively Mongolia's competitiveness. But also it may worsen the current situation. It's very dangerous if we take our economy further down the road to a situation of a few wealthy individuals and a huge number of poor. If this already formed economy goes into resource crisis, there will be no chance to undo the situation unless a revolution is made. In market driven

modern markets, only the stock market can achieve the appropriate resource distribution. This is why stock market development is very important in Mongolia. Policymakers have always paid too little attention to the development of this sector. On the contrary, the Financial Regulatory Commission is the only state organization striving for the development of this market. Our Association and the participants of this market, we have always been well aware and supportive of the FRC's operation and activities, because in general, an underdeveloped stock market poses big risk. Thus, it is highly necessary for its development to become the top priority. It is been not long since the Capital Market Policy Committee was established by the FRC. The main goal of the committee is to ensure the development of the stock market and its appropriate ▶▶

► development advance. But most importantly, it needs to develop very fast. The committee has to clarify what barriers are there and what policy measures are needed to take in order to develop the stock market. We committee members will do our work consult with the FRC. There are many activities that we have planned.

**Capital Market Policy Committee meetings are held once every two months. If necessary, emergency meetings can happen. What issues are priorities for Committee members to discuss at the next meeting?**

The Committee will express its own direction, suggestions and requests on any policy and measure which are being taken by the FRC for the development of the stock market. Our suggestion and guidance reaches parliament and other levels of government through the FRC. We are working quite fast, though the Committee was established not long ago. At our first meeting, we produced a guideline aiming to have more attention toward solving problems that interrupt the stock market in order to foster its development. The guidelines have been approved by the FRC and now is in the hands of parliament. If the stock market develops, other markets will follow. For instance, the commodity market and agriculture will flourish. Furthermore it will result in many issues solved, such as small and medium sized enterprise production, fair resource distribution, employment and US dollar appreciation. Although the stock market development might get hampered during development of SME's and when solving the high US dollar rate. But we don't just give one time suggestions—we also do follow-ups. In collaboration with the FRC, we are working to give appropriate and honest information about the capital market to the public, to erase misleading understandings among the public. Due to past years crises involving savings and credit cooperatives, public awareness and trust in the capital market has dimmed. So it is important to correct the wrong understanding and lead to where it should be.

**What barriers does the Mongolian stock market face today? Have any positive changes been made to the legal environment of this sector?**

There are quite a few legal documents that have been renewed in correlation with the capital market. One of them is the renewed Securities Law. Related to the law, some other extra changes have been made following related laws. For instance, the Insurance Law has seen some changes, where insurance companies are now allowed to invest in the capital market. The next big change is that the Investment Fund Law has been renewed for the first time in Mongolian history. This includes capital guaranteed securities related regulations, special legal bodies related to articles—the first phase of legal reform has seen remarkably achievement over the past four to five years.

**What is the next phase?**

We need to create a legal environment immediately where private pension funds can be built up. This kind of fund will intensify capital market development if they come in as participants. Furthermore, it will establish a fair resource distribution infrastructure—a base condition that allows a capital market to develop. Currently, the legal environment is not that friendly. But we have passed the first level big work. If there's one point of emphasis, it's that parliament needs to cooperate more closely with the FRC. It was common to see not much attention and effort coming out of parliament members for the law related directly to the sector. There was also insufficient participation from parliament in terms of producing draft bills, which is something they have to do with the cooperation of the FRC. But over the past few years, their approach has been changing. Parliament members have begun to understand how important the capital market is. They are putting much more importance to draft bills submitted to the parliament session by the FRC. This is a good achievement.

**Government bonds are now listed and traded on the Mongolian Stock Exchange. How does that affect the market?**

Government bonds were first listed on the exchange at the end of the 1990s and in the early 2000s. However, they were never traded on the secondary market back then. But now it is on the secondary market. The most important

change is that it has reached a point where now they are constantly traded. As the result, the prime rate has settled in the market. Through the prime rate, the economy becomes well shaped, which gives business breathing room to plan. Having a government bond trade that is more stabilized and active is an important market step. Mongolian capital would have a long gone without that prime rate.

**Next year, there are two investment funds set to be established. What kind of benefits do you think they will contribute to stock market development?**

Any country's capital market development has a lot to do with investment funds. Following investment funds, a custodian service becomes a real need. The main goal of custodians and investment funds are to protect the rights of investors. They are not only professional players but also obliged to assist capital market participants. Currently, investors buy stocks and bonds by themselves, as individuals. However, when the custodian service is up and running, the whole process will be much easier to handle and the market will get easier to understand. Investment funds make professional decisions. This is the advantage. Mongolian operating brokers give advice to customers. A broker's duty is same everywhere. They have been following that duty. But in the meantime, conflicts of interest issues tend to come out from time to time. But these have been closed by the legal system. Until today, brokerage companies have been defining and carrying the development of the Mongolian capital market. Professional players are missing. Where once the capital market was the territory of only broker companies, soon, once brand new institutions such as investment funds and custodians enter the market, the capital market will become full. The process will also allow companies that have run brokerage businesses for many years to take a chance to increase their profit. Investment funds cannot be seen as competitors. On the contrary, market circulation will improve. Following the FRC rules and procedures related to investment funds will benefit the market. ■



Masa Igata, a Japanese national, is founder and CEO of Frontier Securities in Mongolia, with nearly a decade of experience in the Mongolian financial services market.

## OPINION

# MONGOLIAN STOCK EXCHANGE REFORM AND FUTURE PROSPECTS

First of all, I want to congratulate the Mongolian Securities Exchange Commission on its 20 year anniversary. Throughout the years, with the continuous efforts by regulators and market participants, the Mongolian stock market has grown leaps and bounds. However, the size of the market is still very small, and recent performance of the stock exchange has been not fully satisfactory. Of course, the country's weaker economic condition can be blamed. But, the industry itself should work harder to develop the market. Below are 10 proposals to activate the stock market as we go forward. I am sure that in another 20 years, the stock market will be much more actively traded, and will play a much greater role for Mongolian companies looking to finance their projects. Currently, the Mongolian stock market is only a bit player in financing, while banks dominate the leading roles. However, given the massive capital required in mining and infrastructure, the role of the stock market is of great importance; because of the unpredictable nature of the cash flow in those industries, it is more suitable to use the scheme of the stock exchange, rather than pursue traditional bank financing. Below I want to highlight 10 items that must be tackled to develop the Mongolian Stock Exchange (MSE), and explain them in detail one by one.

1. An increased Investor Education program
2. The establishment of ethical standards within the industry
3. The enhancement of

professionalism among regulators and market participants

4. The reform of state-owned enterprises
5. Provision of incentives to companies willing to be listed on the MSE
6. The introduction of a more competitive tax system to the stock exchange
7. The introduction of a scheme to increase liquidity in the market
8. An increased emphasis on corporate governance, transparency, and timely disclosure to companies listed on the stock exchange
9. The introduction of a friendlier legal framework to encourage professional fund managers to be able to operate in the stock exchange
10. Government encouragement for the privatization of SOEs

### 1. An increased Investor Education program

Well maintained investor education is essential in Mongolia as the stock market fluctuates and prices change. If investors have a lack of understanding about the risks associated with their securities, that may create huge problems once the fundamentals have changed and the stock price has collapsed.

### 2. The establishment of ethical standards within the industry

The stock market should be played with pre-determined rules, and if the rules are

violated punishment should be given by the authorities and the players should be reminded to act lawfully and ethically. The ethical standard is the guideline to protect all standards.

### 3. The enhancement of professionalism among regulators and market participants

The securities market develops every day, with new products launched daily. Regulators and market participants, especially broker dealers, should be updated regularly on current products, and understand the mechanism of the basic nature of these products. Otherwise investors may be given misleading information on the products they will be investing in.

### 4. The reform of state-owned enterprises

The reform of SOEs is essential before considering them to be listed on the stock exchange. They should ask themselves the meaning of being listed on the stock exchange. With new investors being invited in, SOEs should know that they need to meet the requirements set by minority shareholders. Also stakeholders should be given enough profits to share. Thusly satisfying stakeholders should be important for reformed SOEs.

### 5. Provision of incentives to companies willing to be listed on the MSE

Any company can look for financing either domestically or internationally, with options of either private or public financing. So companies should be »

▶ given incentives when they choose to be listed on the MSE. It is not clear what the incentives are today. Forcing companies to be listed on the MSE with rules is not a good strategy to attract other companies in the long run.

#### 6. The introduction of a more competitive tax system to the stock exchange

The tax burden to trade stocks should be competitive enough compared to other international markets. The higher tax for trading and the capital gain tax may need to be abolished or temporarily halted to encourage investors to enter into the market, even though I acknowledge that they are important sources of tax revenue.

#### 7. The introduction of a scheme to increase liquidity in the market

The extremely low float ratio of MSE listed companies is one of the reasons for low liquidity. Therefore, listing maintenance criteria should be applied to keep the listed on the stock exchange, so

that in case liquidities are low, measures can be taken to increase liquidity through secondary offerings or other measures.

#### 8. An increased emphasis on corporate governance, transparency, and timely disclosure to companies listed on the stock exchange

The importance of those concepts has been mentioned many times in the past. But unfortunately, they have not been implemented thus far. Clearer guidelines should be proposed and implemented in the market to make sure these concepts will be securely established.

#### 9. The introduction of a friendlier legal framework to encourage professional fund managers to be able to operate in the stock exchange

The introduction of the invest trust law and the new securities market law have provided good foundations for the stock market. However, regulations under the laws should be formalized. At the same time, the introduction of a custodian should be encouraged by giving

incentives to both foreign and local custodians.

#### 10. Government encouragement for the privatization of SOEs

The privatization of SOEs should be a good sign for investors to be attracted to the stock exchange, as this signals that the Government is willing foreign investors to invest in the stock market. This will also increase the liquidity of the market. Thus the privatization of SOEs should be planned as soon as possible.

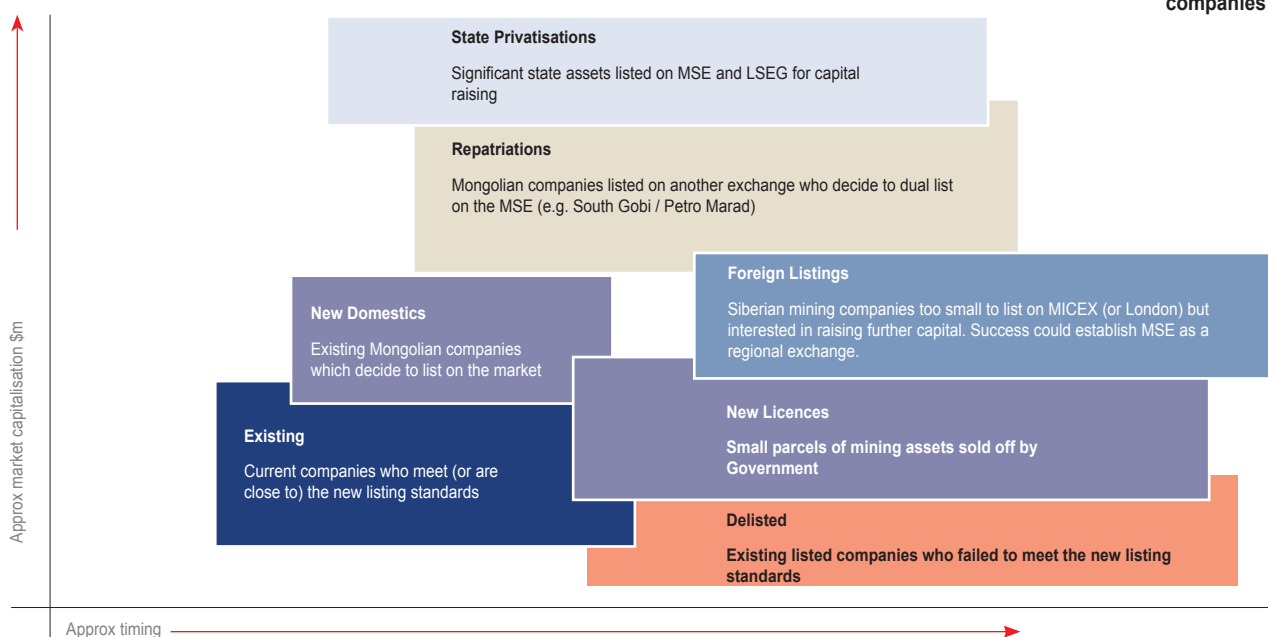
#### Conclusion

With the implementation of the above 10 measures, I would be much more optimistic about the prospects of the Mongolian capital market. (Please see the graphic image of future listed companies' composition below.) I am confident that this will happen by the 40th year anniversary of the Mongolian Securities Exchange Commission in 20 years, if the above 10 measures are completed in the near future. ■

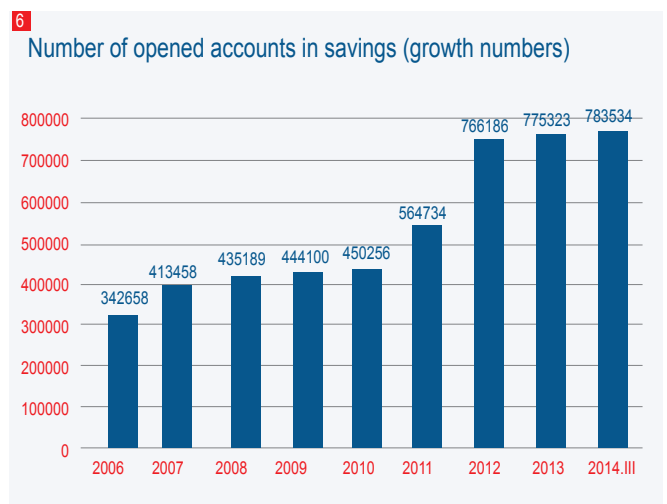
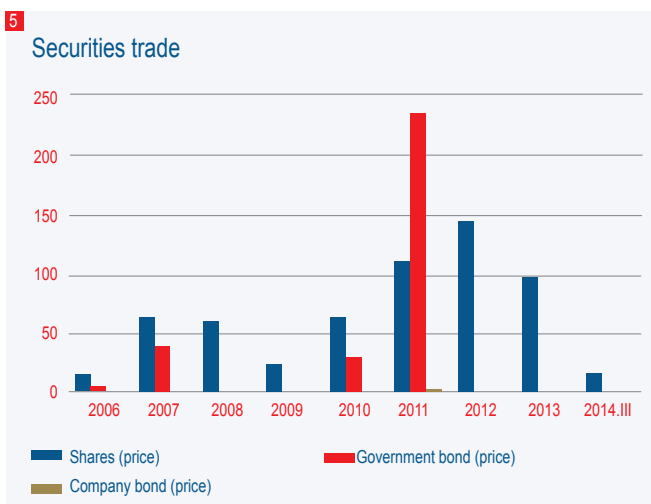
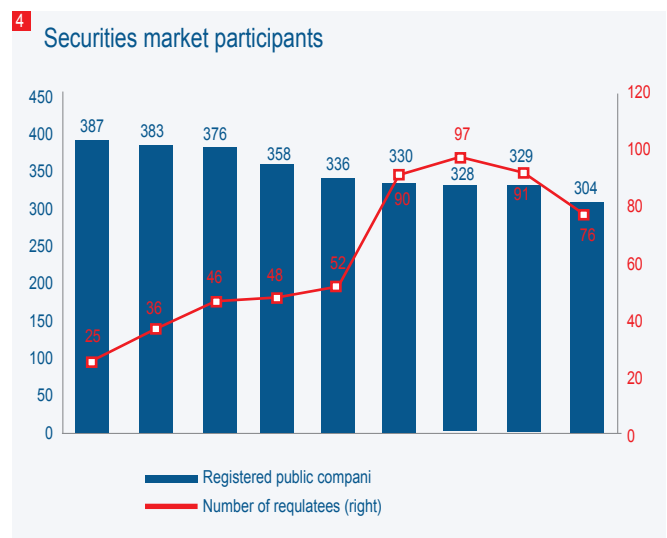
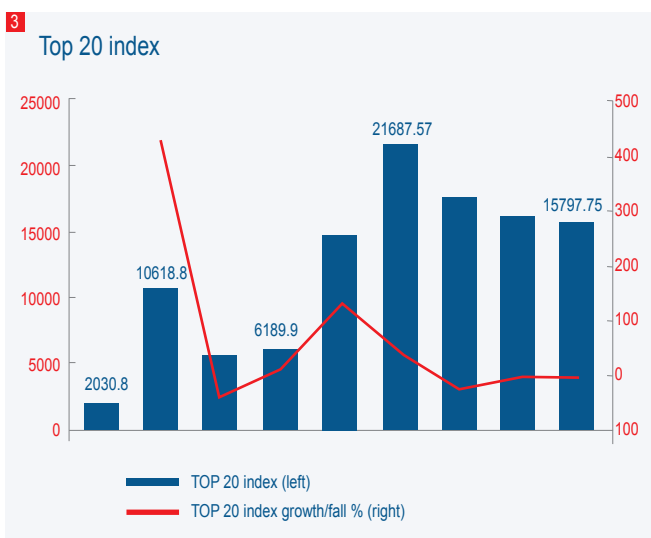
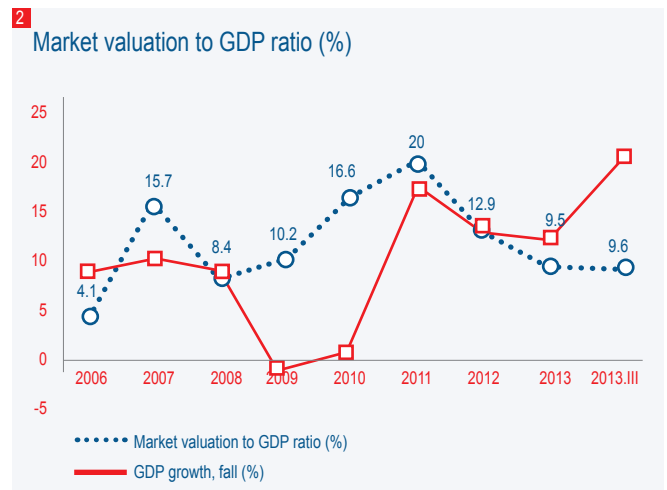
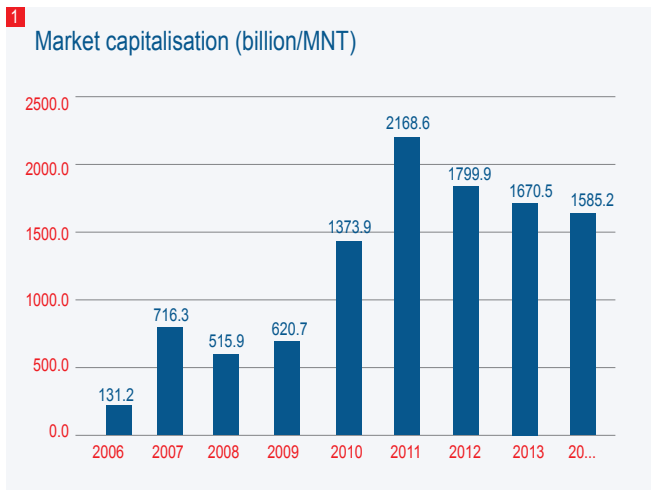
## PROFILE OF TARGET LISTED COMPANIES

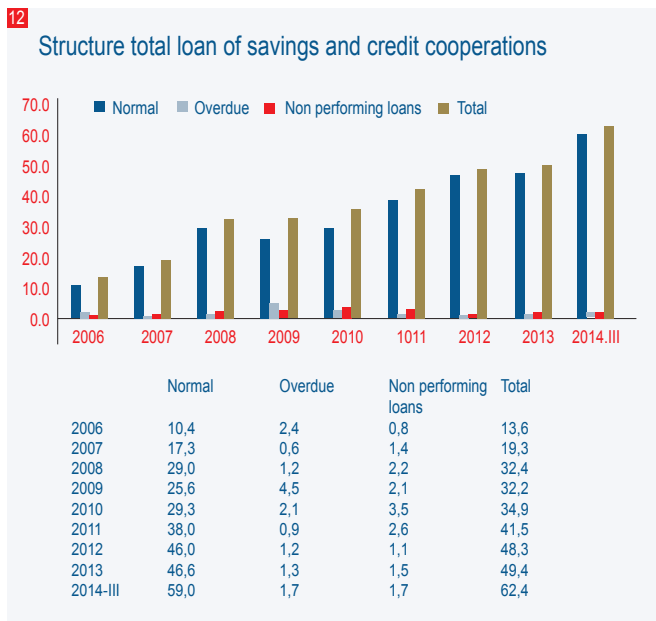
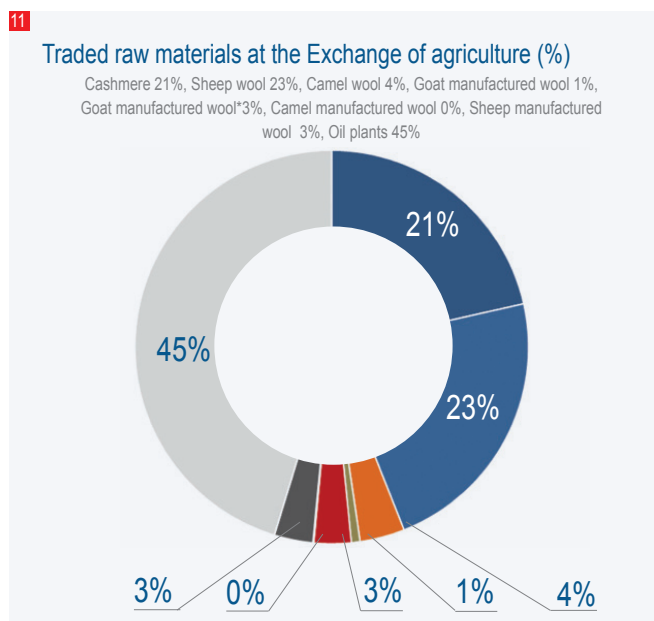
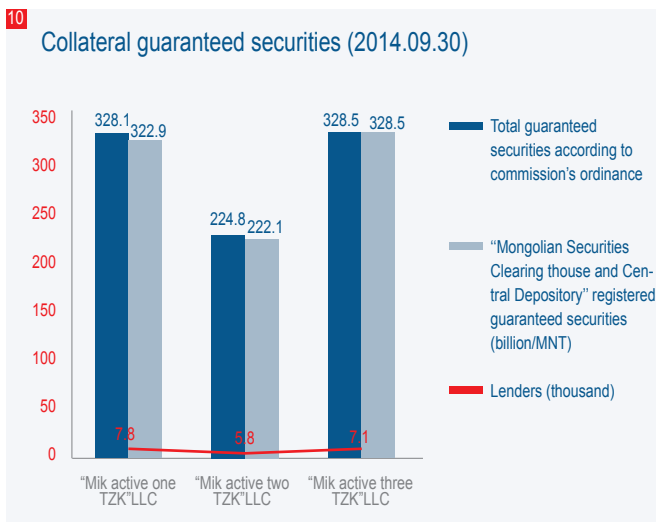
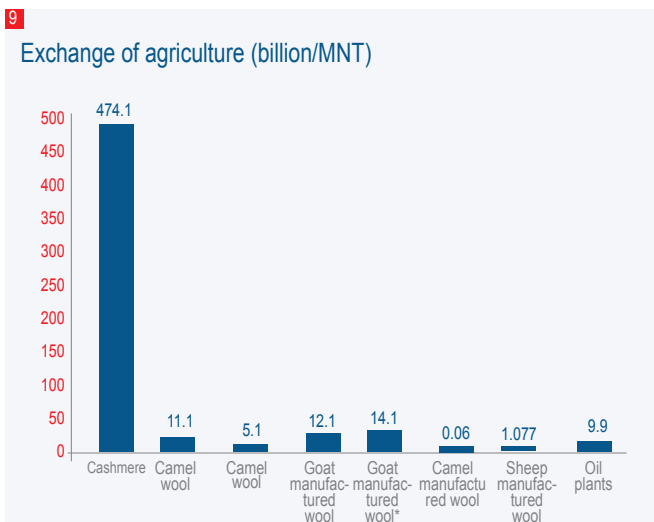
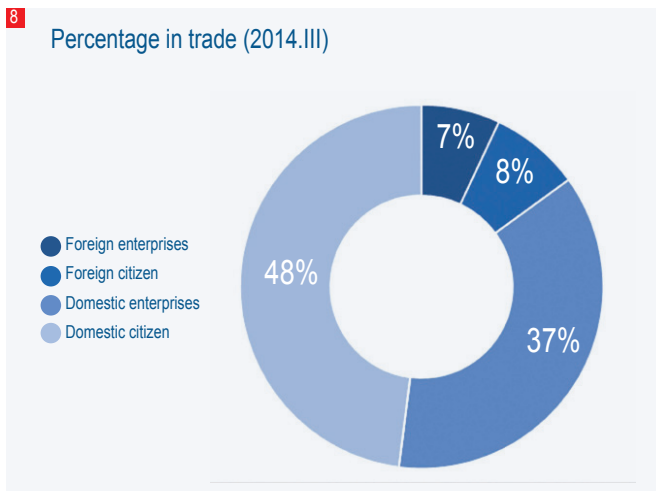
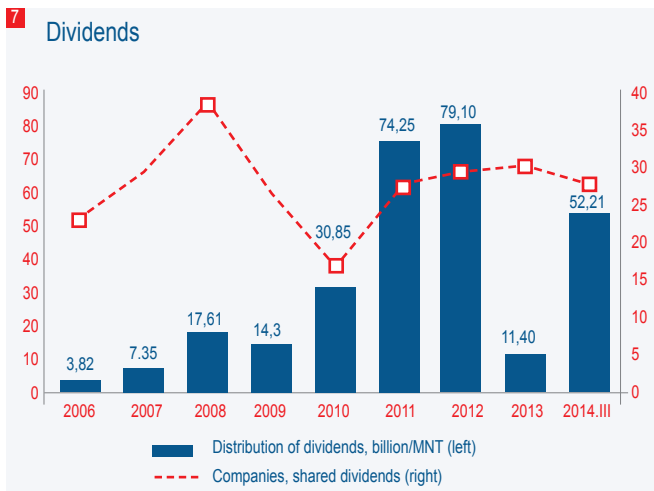
*Increasing the quality of the companies on the market is the key to attracting new investors*

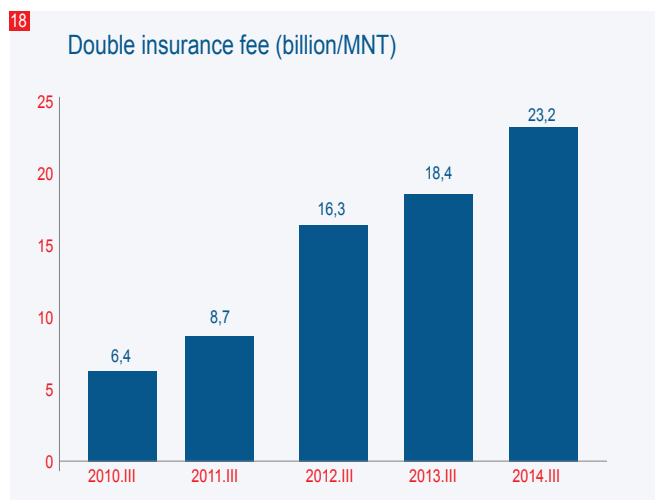
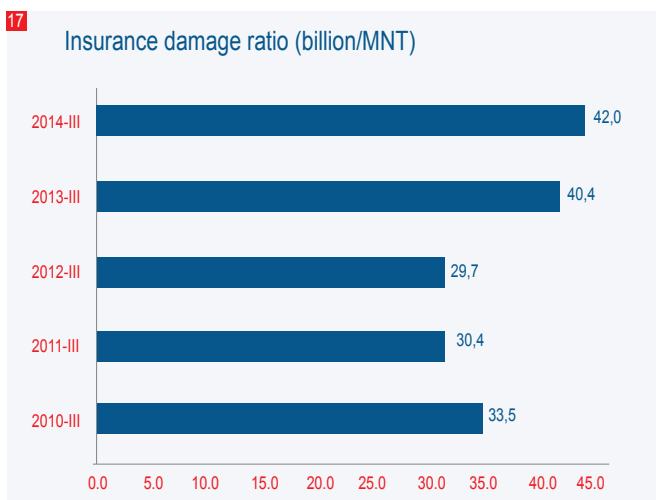
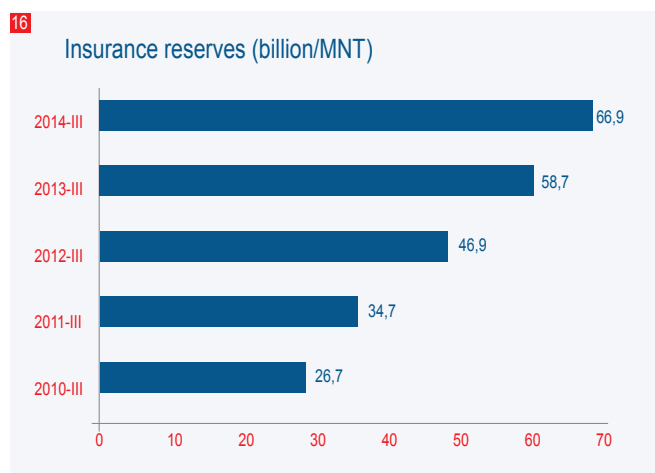
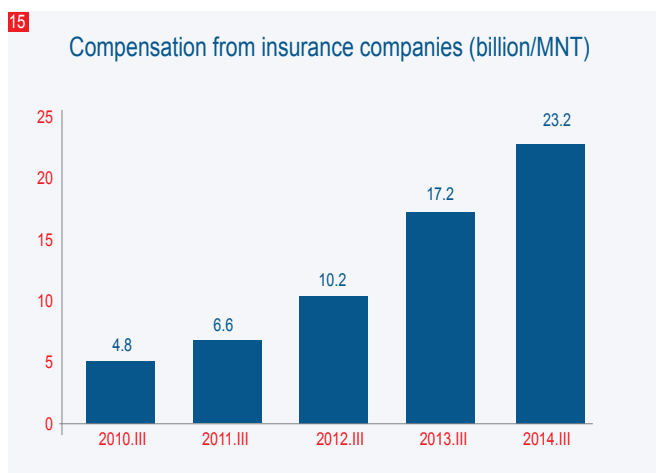
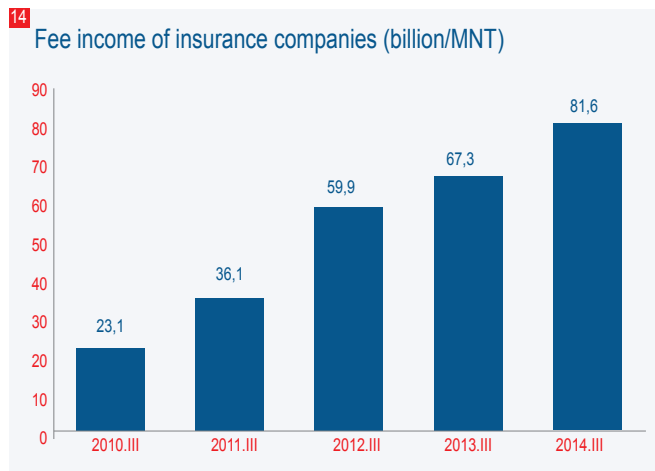
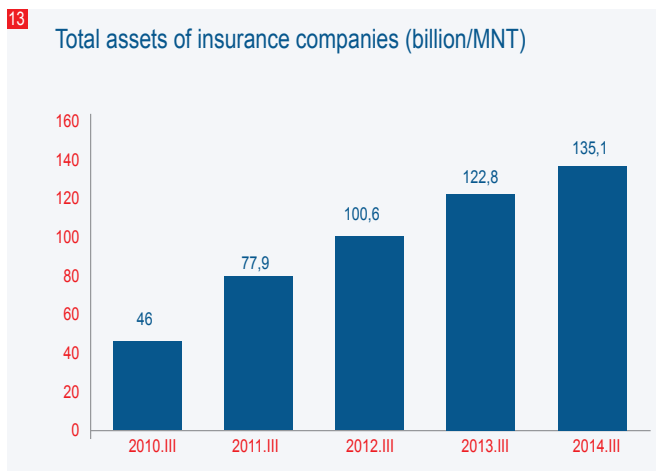
### Seven categories of targeted companies



STATISTICS









ALGERIA, BAHRAIN, BRUNEI DARUSSALAM, COLOMBIA, CÔTE D'IVOIRE, EGYPT, GABON, GHANA, INDONESIA, JORDAN, KENYA, KUWAIT, MALAYSIA, MEXICO, **MONGOLIA**, MOROCCO, MYANMAR, NIGERIA, OMAN, PAPUA NEW GUINEA, PANAMA, PERU, QATAR, SENEGAL, SAUDI ARABIA, SOUTH AFRICA, THAILAND, THE PHILIPPINES, TUNISIA, TURKEY, UAE: ABU DHABI, UAE: DUBAI, UAE: RAS AL KHAIMAH

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## COOPERATION

# INTERNATIONAL COOPERATION OF THE FINANCIAL REGULATORY COMMISSION

In the past 20 years, the financial sector of Mongolia has developed significantly. As the Mongolian economy integrates into the world economy, it is an essential need to develop our financial market in line with the international requirement. At the same time, our economy is heavily dependent on mining sector growth while the economy of Mongolia has been growing in double digits in the recent years. As a result of these positive signs, companies are actively seeking to issue IPOs foreign stock exchanges, requesting the Financial Regulatory Commission (FRC) to allow dual listings in different stock exchanges. Based on these legitimate market demands, the FRC needed to develop and strengthen its financial market legal environment in line with international standards. With the support of international organizations, the FRC has created a financial legal environment that is suitable for the current needs of the financial market in Mongolia.

The current securities market legal environment is in line with international standards, which can be proven now that the Financial Regulatory Commission of Mongolia has become a full signatory to the International Organization of Securities Commissions Multilateral Memorandum of Understanding, which was signed on June 16, 2014.

By becoming a full signatory of this multilateral memorandum of understanding, it enables the FRC to exchange information and creates opportunity work with 180 other securities regulators around the world.

With the aim of developing the non-banking financial sector in a short term, as well as to reach international standard. Also, in order to strengthen the regulatory regime and enhance its staff member's



*The Multilateral Memorandum of Understanding with the International Organization of Securities Commissions, signed on June 16, 2014.*

capacity, the FRC has signed bilateral memorandum understandings with the following regulatory authorities: the Hong Kong Securities Futures Commission, the Financial Services Agency of Japan, the Financial Services Commission of Republic of Korea, the Agency of the Republic of Kazakhstan on Regulation and Supervision of Financial Market and Financial Organizations, China Securities Regulatory Commission, and the Polish Financial Supervision Authority.

In the framework of these bilateral MoUs, several projects are being implemented at the FRC, such as public financial education, enhancing the legal environment of regulated sectors, and improving the capacity of the FRC project, etc.

MON/004-Financial sector capacity building and training project, implemented by the Luxembourg Development Agency, funded by the Government of the Grand Duchy of Luxembourg, has been successfully implemented at the FRC for the

last four years. This project aims to strengthen the FRC's capacity through two main expected results, such as enhanced institutional and operational framework, and to strengthen regulatory and supervisory framework of the FRC. Besides this, the FRC has been implementing projects such as "Mongolian capital market capacity building project" in collaboration with the Japanese Financial Services Agency.

There are other projects also being implemented at the FRC such as "Improving the legal environment of micro-insurance", which was funded by the German International Cooperation, and a project aimed at promoting inclusive financial services of the poor, which is supported by the Asian Development Bank.

The FRC also became a member of the Alliance for Financial Inclusion (AFI) on June 2010. The Alliance for Financial Inclusion is the first global knowledge-sharing network designed exclusively for financial inclusion policymakers ▶▶

▶ from developing countries. With the support of this organization, the first legal environment for electronic money transaction and mobile banking law was introduced in Mongolia.

In the future, the FRC is looking forward to work with AFI in a direction of increasing households' income through enhancing the activities of the Commodity Exchange of Mongolia. For instance, FRC is planning to introduce derivatives as an instrument in the exchange.

In the framework of developing Ulaanbaatar City as regional hub financial

center, last September the FRC organized a regional seminar on Regulation and Supervision of Investment fund under the APEC Financial Regulators Training Initiative in collaboration with the Asian Development Bank.

Asia-Pacific regions 12 countries, 60 participants participated in this regional seminar, which was one of the biggest financial training events organized in Mongolia. A number of professional experienced experts taught courses in Ulaanbaatar, Mongolia, such as expert from the United States, Australia, South Korea and Malaysia.

With the purpose of the developing the Mongolian financial market in line with the international standards and in order to introduce new financial instruments technology at the market, the FRC is looking forward to work with the international organization to enhance the Mongolian financial market.

While taking this opportunity, I would like to express my sincere appreciation for international and governmental organizations those who support the FRC effort to develop the financial market in Mongolia. ■

## PROJECT

# FOR ADULT FINANCIAL EDUCATION

Public financial literacy can be improved learning from successes and lessons of characters of the TV series that focuses on financial education messages.

Within the framework of "Promoting Inclusive Financial Services for the Poor Project" a focus group study was conducted for the first time in Mongolia on adults financial education needs. Findings of the study compared against the results of World Bank survey on financial capabilities and consumer protection. Based on both survey analyses, a financial education marketing plan was developed for financial messages and channels to disseminate them to the public.

As a result of mentioned study, TV series was selected as the

most inclusive channel to deliver financial education messages to the community.

TV series aims at delivering financial messages to the public through its character's financial successes, as well as financial fraud in real life faced by the main characters, and how they are being solved or achieved to the good results. Two pilot episodes were evaluated by 213 target group population in Ulaanbaatar and in provinces, and based on that evaluation an additional 24 episodes have been produced. The "Saytan bolgoh damjaa" TV series will be broadcasted to the public via two national broadcasting TV networks in January, and outcomes will be evaluated by questionnaire and via cellular SMS messages. ▶



► **One of the components of the project aims at capacity building of SCCs and improved regulatory environment of SCCs**

It was revealed by research that insufficient public understanding of SCCs (Saving and Credit Cooperatives), weak regulatory environment, inadequate capacity of the sector, lack of public understanding about SCCs, and lack of savings lead to greater risk of poverty. Moreover, only 31 percent

of total households and 13 percent of poor households have access to financial services. These were the main background of project implementation. The total budget of the project is USD 2.5 million, financed by the Japanese Fund for Poverty Reduction via the Asian Development Bank. The project aims at improving access to financial services for the poor and vulnerable population through capacity building of SCC, which is the closest financial institution of target group, strengthening the regulatory environment of SCCs, and improving financial literacy of public. Training and regional discussions were

held in 5 regions involving 348 elected members and staff from 136 SCCs. The SCC regulatory and supervision system has been revised consolidating the feedback of the discussions. The project team emphasized that as a result of these activities more than 90 percent of all SCCs are operating in compliance with the law and regulation.

The most essential training needs were defined based on capacity assessment of SCCs that enrolled 93 SCCs and two sets of training modules developed on "SCC principles and best practices" and "SCC governance and members' participation". Trainers of these modules have been trained selectively from the management staff of the sector.

The Mongolian Confederation of Credit Unions (MOCCU) and the Mongolian Cooperative Training and Information Center (MCTIC) provided the IT equipment with total cost of MNT 60 million. This resulted in strengthened capacity of umbrella institutions to conduct training independently due to supported physical and human resource capability.

Internet based training and classroom training operations were conducted 39 times, and 973 elected reserve members and management staff from SCCs attended. Expected outcome of the project in the remaining period is 50 percent of population will obtain financial services and 30 percent of total population will watch the TV series.

The project outcomes have reviewed by the Asian Development Bank and the project progress was 75 percent by June 2014. This project activity launched in 2012 and will end by January 2016. ■



The "Saytan bolgoh damjaa" financial education TV series, coming soon to your living room television.



Securities Exchange Commission first Collective with US consultants (1995)



Government Bond first trade (1996) Government Bond first trade (1996)



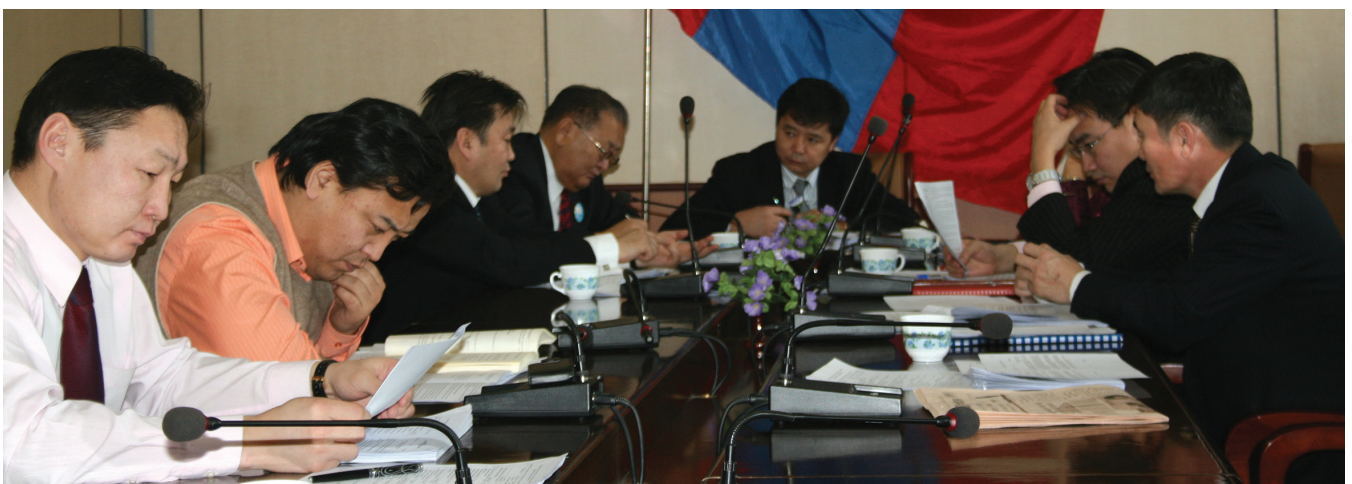
Securities Exchange Commission team (2004)



Securities Exchange Commission team (2004)



Parliament Speaker visit  
 From left hand side / Back line / G.Dawaasambuu FRC Administration Department Senior Referent, N.Udaanjargal FRC Administration Department Director, R.Bud Parliament member, N.Ganbyamba Parliament member, FRC former member, Ts.Bayarsaikhan Parliament member, D.Dugerjaw FRC member and vice director. From left hand side / Front line / B.Sharawsambuu FRC member and vice director, S.Demberel Parliament Speaker, D.Bayarsaikhan FRC Chairman



Financial Regulatory Commission Meeting