



Report and Recommendation of the President to the Board of Directors

Project Number: 47934
June 2014

Proposed Senior Loan Khan Bank Supporting Micro, Small, and Medium-Sized Enterprises (Mongolia)

This is an abbreviated version of the document approved by ADB's Board of Directors that excludes information that is subject to exceptions to disclosure set forth in ADB's Public Communications Policy 2011.

Asian Development Bank

CURRENCY EQUIVALENTS

(as of 27 May 2014)

Currency unit	–	togrog (MNT)
MNT1.00	=	\$0.0005
\$1.00	=	MNT1,819

ABBREVIATIONS

ADB	–	Asian Development Bank
BOM	–	Bank of Mongolia
CAR	–	capital adequacy ratio
CEO	–	chief executive officer
DEG	–	Deutsche Investitions- und Entwicklungsgesellschaft
FMO	–	Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden N.V. (Netherlands Development Finance Company)
HSIA	–	HS International (Asia) Limited
IFC	–	International Finance Corporation
MSMEs	–	micro, small, and medium-sized enterprises
NPL	–	nonperforming loan
ROAA	–	return on average assets
ROAE	–	return on average equity
SMEs	–	small and medium-sized enterprises

NOTES

- (i) The fiscal year (FY) of Khan Bank ends on 31 December.
- (ii) In this report, “\$” refers to US dollars.

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PROJECT AT A GLANCE

1. Project Name: Khan Bank for Supporting Micro, Small and Medium-sized Enterprise in Mongolia 2. Project Number: 47934			
3. Country: Mongolia		4. Department/Division: Private Sector Operations Department Financial Institutions Division	
5. Sector Classification:			
	Sectors	Primary	Subsectors
	Finance	X	Inclusive Finance Small and medium-sized enterprise finance and leasing
6. Strategic Agenda and Drivers of Change:			
	<i>Strategic Agenda</i>	Primary	Sub categories
	Inclusive Economic Growth		Pillar 1: Economic opportunities, including jobs created.
	Inclusive Economic Growth	X	Pillar 2: SME in finance and micro- finance
	<i>Drivers of Change</i>		
	Private sector development	X	Private sector investment
6a. Climate Change Impact:		6b. Gender Mainstreaming:	
Adaptation		Gender equity theme	
Mitigation		Effective gender mainstreaming	
Not applicable	X	Some gender elements	x
		No gender elements	
7. Targeting Classification:		8. Location Impact:	
	Targeted Intervention		
	Geographic dimensions of inclusive growth	Millennium development goals	Income poverty at household level
General Intervention			
X			
		Rural	Medium
		Urban	Medium
		National	High
10. Safeguard Categorization:			
	Environment	FI	
	Involuntary resettlement	FI	
	Indigenous peoples	FI	
11. ADB Financing:			
	Sovereign/Nonsovereign	Modality	Source
	Nonsovereign	Loan	Ordinary capital resources
			Amount
			Up to \$40 million
12. Cofinancing: Not applicable			
13. Counterpart Financing: Not applicable			
14. Aid Effectiveness: Not applicable			

I. THE PROPOSAL

1. I submit for your approval the following report and recommendation on a proposed senior loan of up to \$40,000,000 to Khan Bank for Supporting Micro, Small, and Medium-Sized Enterprises (MSMEs) in Mongolia.¹

II. THE FINANCIAL INTERMEDIARY

A. Investment Identification and Description

2. In most developing countries, MSMEs are important engines of economic growth and key contributors to poverty reduction by increasing individual incomes and creating employment. In Mongolia, MSMEs comprise 98% of all enterprises, three-quarters of which are microenterprises. Access to finance is the foremost constraint for Mongolian MSMEs—30% of small and medium-sized enterprises (SMEs) in Mongolia perceive access to finance as the largest issue for their operations.² It is estimated that only 10% of about 37,000 Mongolian SMEs regularly access finance through banks.³ A World Bank study notes that when finance is available to SMEs, loan terms and conditions are characterized by high interest rates, shorter maturities, and smaller amounts that do not meet the full financial needs of these companies and primarily require immovable collateral (footnote 2). Overall, bank lending has continued to increase since the global financial crisis of 2008–2009. However, a marked gap remains in terms of funding needs for the numerous MSMEs, as many banks continue to focus on top-tier, larger companies, which are perceived to be of less risk.⁴

3. Given the access to finance issues in Mongolia for MSMEs, the Asian Development Bank (ADB) met with several banks in 2013 to identify suitable candidates with the interest and ability to serve the SME segment, and to reach the microenterprise segment. Additionally, ADB sought banks that could effectively address the needs of MSMEs, with outreach to rural areas outside Ulaanbaatar. Rural areas tend to have higher incidences of poverty in Mongolia.⁵ The bank has a sound credit profile, strategic focus on MSMEs, and the largest branch network in rural areas. Khan Bank has a developed and growing MSME platform, and has received technical advisory services from the European Bank for Reconstruction and Development for the creation of institutional structures, and training and education programs designed for local staff. The proposed assistance builds on an ADB nonsovereign loan amounting to \$10 million provided to Khan Bank in 2007, which was general in nature.⁶ As the bank has matured and

¹ The design and monitoring framework is in Appendix 1.

² World Bank. 2012. *Financial Sector Assessment: Mongolia*. Washington, DC.

³ The World Bank Enterprise Surveys. <http://www.enterprisesurveys.org/>. Other constraints noted were the tax rate, inadequately educated workforce, informal sector practices, political instability, and licensing and permitting problems. Asian Development Bank (ADB). 2012. *Improving Access to Finance in Mongolia*. Manila; ADB. 2012. *Promoting Private Sector Development in Mongolia*. Manila.

⁴ The International Finance Corporation (IFC) and McKinsey & Company estimate that 20%–39% of SMEs in Central Asia and Eastern Europe have a need for access to finance but have neither a loan nor an overdraft. IFC. 2010. *Scaling-Up SME Access to Financial Services in the Developing World*. http://www.gpfi.org/sites/default/files/documents/G20_Stocktaking_Report_0.pdf

⁵ World Bank. 2012. Poverty Level Estimated at 29.8 Percent in Mongolia. Press Release. 17 April. <http://www.worldbank.org/en/news/press-release/2012/04/17/poverty-level-estimated-at-nearly-30-percent-in-mongolia>

⁶ ADB. 2007. *Report and Recommendation of the President to the Board of Directors: Proposed Loan to Khan Bank in Mongolia*. Manila.

financing needs of MSMEs have emerged, the assistance will target this important customer segment. Fitch Ratings has rated Khan Bank's long-term issuer default ratings B (stable).⁷

B. Business Overview and Strategy

4. **Overview.** Khan Bank, established in 1991, is Mongolia's largest bank in terms of total assets, loans, and deposits—with market shares of 23% (assets), 23% (loans), and 26% (deposits) in 2013. The bank, previously known as the Agriculture Bank of Mongolia, was owned by agricultural cooperatives, herdsman, and farmers. It was privatized in 2003 and renamed Khan Bank in a post-Soviet effort to privatize the banking sector. Although privatized, it continues to maintain a focus on reaching the underserved in rural areas with inclusive finance as a priority in strategy and planning. Khan Bank has 335 ATMs, accounting for 34% of all ATMs in Mongolia, and a branch network of 528 (100 in Ulaanbaatar and 428 in rural areas), providing banking services to at least 62% of households in Mongolia (1.8 million customers out of a population of 2.9 million).⁸ The bank is also the largest single employer in the financial sector with 5,000 employees. Female staff represented 63% of total employees in 2013.

Khan Bank's principal activities are corporate and MSME lending, as well as retail and institutional lending.⁹ Product lines include a range of loan and deposit products, foreign exchange, trade finance, cash management, and international payment services.

5. Khan Bank's current MSME portfolio is well diversified in terms of sectors, comprising mainly trade and commerce, construction, agriculture, and transportation loans. Khan Bank began officially segregating its lending to MSMEs in 2000. A separate SME center was established in 2010, which enabled a more focused approach to MSME lending.¹⁰ Through its expanded branch network, Khan Bank plans to offer new products, such as working capital, trade finance, and capital expenditure financing through electronic and mobile banking to promote cost efficiencies. As part of its strategy, Khan Bank intends to implement a structured customer acquisition process, maximize cross-sale opportunities, and position Khan Bank as a total solutions provider to the MSME segment.

6. Khan Bank tailors its relationship management approach and product offering to each subsegment. In addition, Khan Bank has established a business incubator center in 2006, which provides practical assistance to improve business management skills, connects MSMEs to desired partners, provides updated information to enable them to make business decisions, and helps to maintain long and stable relations with these businesses.

C. Ownership, Management, and Governance

7. **Ownership.** The largest shareholder of Khan Bank is Sawada Holdings (Japan), which owns 41.3% of the bank's capital. Sawada Holdings is engaged in securities, banking, commodities, real estate, and venture capital. Sawada Holdings is listed on the Osaka Stock

⁷ Reuters. 2013. RPT-Fitch Affirms Mongolia's Khan Bank and XacBank at 'B'; Outlook Stable. 14 November. <http://www.reuters.com/article/2013/11/14/fitch-affirms-mongolias-khan-bank-and-xa-idUSFit67648420131114>

⁸ Khan Bank November 2013 due diligence.

⁹ MSME lending is classified into four categories: (i) small business loans (short-term working capital financing loans), (ii) term loans (3- to 5-year investment loans), (iii) express micro loans (up to 1-year working capital financing loans), and (iv) agricultural loans (working capital financing and investment loans). The current average loan size is MNT36 million.

¹⁰ Seven SME centers—five in Ulaanbaatar and two in the largest rural areas (Darkhan and Erdenet)—specialize in providing banking services to MSMEs, with higher authorization levels and more specialized staff.

Exchange and has total assets of \$3.0 billion as of December 2013. Tavan Bogd owns 23.0% of Khan Bank. The Tavan Bogd Group is one of the largest private conglomerates in Mongolia, with 12 affiliated companies engaged in retail and wholesale, travel and tourism, manufacturing, and food production. HS International (Asia) Limited (HSIA) owns 13.1% of Khan Bank. HSIA is a 100% subsidiary company of Sawada Holdings in Hong Kong, China. HSIA conducts business activities within the People's Republic of China, including market research on various regions in Asia. D. Hulan¹¹ has a shareholding in Khan Bank of 13.3% and the International Finance Corporation (IFC) owns the remaining 9.3%.

8. **Management.** The senior management team is composed of a team of experienced banking executives with prior work at multiple banks throughout Asia. The four key senior positions are (i) chief executive officer (CEO); (ii) deputy CEO; (iii) chief financial officer; and (iv) chief risk officer. Additional information on the bank's management and an organizational diagram is provided in Ownership, Management, and Governance.¹²

9. **Governance structure.** The board of directors comprises seven members who bring extensive international banking and other professional experience to Khan Bank. The board has two independent non-executive directors and five non-executive directors. The board is chaired by H. Sawada, who is the President and CEO of Sawada Holdings, the bank's largest shareholder; he is also a founder and chairman of HSIA.

10. The board approves Khan Bank's strategic plan and key policies and monitors their implementation through the board committees and key management personnel appointed by the board. The three board committees—audit committee, risk management committee, and governance and remuneration committee—are chaired by board directors.

D. Financial Performance

11. Khan Bank has had healthy growth from 2010 to 2013. Total assets grew from \$1,125 million in 2010 to \$2,904 million in 2013, representing a compound annual growth rate of 37.18%. Gross customer loans grew from \$568 million in 2010 to \$1,502 million in 2013. Total customer deposits grew at a robust pace of 22.7% (3-year compound annual growth rate) from \$955 million in 2010 to \$1,763 million in 2013. Financial highlights of Khan Bank are provided in the financial analysis.¹³

12. **Earnings.** In 2013, net income was MNT96.7 billion, which represented a growth rate of 35% from MNT71.4 billion in 2012. The increase can be attributed to the increase in net interest income (29.4% in 2013 and 19.2% in 2012) as a result of the growth in the loan portfolio resulting from effective marketing and sales efforts and Khan Bank's reputation. Despite the falling interest rate environment, the net interest margin was still healthy (6.8% in 2013 and 8.0% in 2012) across all business segments. Operating efficiency improved despite branch expansion, training, and adaptation to new information software (cost-to-income ratio was 46.3% in 2013 and 52.7% in 2012). In 2013, return on average assets (ROAA) was 2.5% and return on average equity (ROAE) was 34.0%. This was above the banking sector average (2.17% ROAA and 28% ROAE) and is the highest among its peers. Khan Bank has managed to

¹¹ D. Hulan is a citizen of Mongolia and is a founder and shareholder of Tavan Bogd Group. Since 2003, she has been the executive vice-president of Tavan Bogd Group.

¹² Ownership, Management, and Governance (accessible from the list of linked documents in Appendix 2).

¹³ Financial Analysis (accessible from the list of linked documents in Appendix 2).

maintain a stable ROAA of above 2.5% and an ROAE of at least 30% in 2011–2013 because of its leading position in the market as well as its well diversified deposit and loan portfolio.

13. **Capitalization.** Khan Bank had a tier 1 capital adequacy ratio (CAR) of 11.1% and a total CAR of 16.6% in 2013 (2012: tier 1 CAR, 10.8%, total CAR, 16.6%). The bank's capitalization was above that of its peers, which had an average CAR of 15.5% in 2013 resulting from an increase in subordinated debt obtained from IFC. The total CAR year-end results were similar to 2012 and the bank met the new regulatory requirements of tier 1 CAR of 9.0% and total CAR of 14.0%, which came into effect on 30 June 2013. Total growth in capital was supported by retained earnings and new subordinated debt provided by FMO and DEG amounting to \$32 million in 2012 and most recently \$40 million from IFC, which were fully disbursed in March 2014.

14. **Funding and liquidity structure.** In 2013, Khan Bank's funding structure comprised the following: customer deposits (64.7%), short-term borrowings (16.3%), long-term borrowings (11.4%), equity and retained earnings (7.0%), and others (0.6%). Customer deposits grew by 34% in 2013 (14.4% in 2012), which was slightly above the sector average growth rate of 32% in 2013.¹⁴ It also receives specialized funding, as do the other large banks, from the government to provide subsidized funding to SMEs active in specific industries (e.g., meat and flour), as well as for home loans. This funding comprised 19% of total liabilities as of December 2013. Khan Bank has existing credit lines with the European Bank for Reconstruction and Development, FMO, and IFC, and trade finance facilities with ADB; and will continue to maintain and develop relationships with local and international commercial banks. In 2013, Khan Bank's cash reserve ratio was 15.8% (14.7% in 2012) and its liquidity ratio (liquid assets as a percentage of total assets) was 46% (34.6% in 2012). Both were compliant with the Bank of Mongolia (BOM) minimum requirement of 12% (cash reserve ratio)¹⁵ and 25% (liquidity ratio).

15. **Loan portfolio.** Khan Bank's total loan portfolio of MNT2,484.8 billion as of December 2013 is segmented as follows: corporate banking (20%), MSME (26%), and retail (54%). In 2013, gross loans were concentrated in (i) consumption loans—including salary, pension, leasing, mortgage, and employee loans (49%); (ii) trade and finance (16%); (iii) construction (10%); (iv) agriculture (3%); (v) industrial (8%); (vi) mining (4%); and (vii) others (10%). Geographically, the portfolio is in Ulaanbaatar (55%) and rural areas (45%). As more branches open in rural areas, demand for banking services is expected to increase.¹⁶

16. Exposure to the top 20 group obligors is moderate, at 17.3% (18.2% in 2012) of gross loans in 2013. The largest single borrower accounted for 12% of the total exposure to top 20 borrowers; and is a large Mongolian conglomerate whose operations are mainly in retail, wholesale trade, manufacturing, and construction. Exposure to the largest individual and/or group accounted for 12.5% of the bank's total capital, which is below the 20% regulatory limit. Loans to related parties amounted to MNT17.9 billion and accounted for 3.8% of total capital in 2013 (6.4% in 2012). Related party loans are to Tavan Bogd and its affiliates as well as key management personnel.

¹⁴ ADB's Mongolia Resident Mission; Bank of Mongolia. *Bank Statistics*. <http://www.mongolbank.mn/eng/default.aspx> (accessed 28 April 2014); Moody's. 2014. *Moody's changes ratings outlooks of Mongolia banks to negative and affirms ratings*. 8 January.

¹⁵ The reserve requirement (or cash reserve ratio) is a central bank regulation that sets the minimum fraction of customer deposits and notes that each commercial bank must hold as reserves and not lend out.

¹⁶ 2013 figures. Source: Khan Bank.

17. **Asset quality.** The bank's asset quality is sound. Nonperforming loans (NPLs) were reported at 1.5% of gross loans in 2013 (0.9% in 2012), which is below the sector average of 5.3% (4.2% in 2012).¹⁷ NPLs of MSMEs amounted to 1% in 2013 (0.9% in 2012). Khan Bank plans to maintain its total gross NPL ratio below 5% at all times. Khan Bank uses the BOM standard loan classification specification.¹⁸ Since 2012, Khan Bank's loan loss coverage ratio has been above 100%.¹⁹

III. THE PROPOSED ADB ASSISTANCE

A. The Assistance

18. ADB proposes to provide a senior unsecured \$40 million loan for a tenor of 5 years to Khan Bank for the exclusive purpose of funding MSMEs in Mongolia. The borrower shall use the proceeds to extend new loans to eligible MSME sub-borrowers.²⁰

B. Implementation Arrangements

19. Khan Bank will provide ADB with development effectiveness, safeguards, financial reports, and MSME loan portfolio information at predetermined regular intervals and as requested. ADB will review these reports on an ongoing basis and monitor the facility accordingly. Monitoring reports will be prepared and submitted to ADB's Office of Risk Management on a regular basis, but at least annually.²¹ The first such report will be submitted no later than 12 months after Board approval.

C. Value Added by ADB Assistance

20. ADB's value addition is expected to be the following:

- (i) The financial sector in Mongolia is underdeveloped. The country's capital markets are nascent and commercial bank funding is not readily available in large amounts. Moreover, loans with longer tenors are particularly in short supply. As a result, domestic credit provided by the banking sector was 36.8% and, as such, the country lags behind its peers.²² Mongolia has also been impacted by the banking sector crisis in Europe, as European commercial banks and investors have curtailed their lending. This has resulted in a shortage of funding. Hence, international financial institutions are needed to fill this funding gap. ADB's longer tenor loan will address a funding gap estimated to total \$223 million by 2016, and help the bank to reduce asset–liability mismatches as it will, in turn, provide longer-tenor funding to MSMEs.
- (ii) Access to credit remains one of the most critical obstacles to the development of the MSME sector. ADB assistance will help to address this gap and support a bank that is active in MSME lending through (i) the provision of long-term financing, which will result in more private businesses serving the local economy,

¹⁷ Average NPLs were 4.6% in 2009–2013.

¹⁸ Joint Resolution of the Governor of the Bank of Mongolia and the Minister of Finance. 2010. *Regulation on Assets, Clasifying, Provisioning and its Allocations*. http://www.mongolbank.mn/documents/regulation/bankactive_eng.pdf

¹⁹ Khan Bank. 2011. *Annual Report 2011*. Ulaanbaatar; Khan Bank. 2012. *Annual Report 2012*. Ulaanbaatar.

²⁰ MSMEs will be defined as those obtaining a maximum loan size of MNT5 billion and operating in trade or services, manufacturing or processing, agriculture, and wholesale and retail trade. The average loan size under the MSME loan facility will not exceed MNT55 million.

²¹ ADB. 2013. *Nonsovereign Operations. Operations Manual*. OM D10. Manila.

²² World Bank. 2013. *The Little Data Book on Financial Development 2013*. Washington, DC.

- the underserved rural, and the poor; and (ii) the strengthening of the non-resources sector, which helps diversify exports.
- (iii) Through on-site monitoring and communication with Khan Bank management over the life of the loan, ADB will support adherence to high corporate governance, social, environmental, and risk management standards. Development effectiveness indicators will also be monitored regularly.

D. Risks

21. **Challenging operational environment.** Mongolia's economy is largely reliant on the agricultural and mining sectors. It is also exposed to the slowing growth in the People's Republic of China. Recent high inflation and the depreciating currency have further exposed the banking sector to economic and policy risks. Solid economic growth prospects, together with progress in economic stabilization and an open, market-led economy, partly mitigate these weaknesses. The banking industry is viewed as having an underdeveloped regulatory framework—lacking strict enforcement of regulatory requirements. Transparency and disclosure are considered weak by international standards. However, authorities have taken measures to tighten prudential regulations on capital requirements, asset classification, and loss provisions. To help mitigate the risks imposed by the operating environment, Khan Bank carefully manages its capital position, keeps a significant liquidity buffer, and maintains a diversified and highly granular loan portfolio with prudent sector and borrower concentration limits.

22. **Asset quality.** As Khan Bank's portfolio expands and the economy continues to grow more slowly, asset quality may deteriorate. However, Khan Bank has a comprehensive risk management system that defines, assesses, and monitors risks.

IV. DEVELOPMENT IMPACT AND STRATEGIC ALIGNMENT

A. Development Impact, Outcome, and Outputs

23. **Impacts.** ADB assistance will lead to (i) increased contribution of MSMEs to gross domestic product; and (ii) increased access to credit by MSMEs in Mongolia. Growth of MSMEs in non-mineral-based resource sectors will help diversify and strengthen the resilience of the economy.

24. **Outcome.** The outcome will be the growth and sustainability of Khan Bank's financial services to MSMEs. Khan Bank's MSME loan portfolio is expected to grow beyond the level of ADB's funding. Providing financing to MSMEs through loans for working capital and investment will contribute to job creation, capital formation, and asset creation, including through loans for agriculture.

25. **Outputs.** The outputs will be the (i) increased availability of MSME financing from Khan Bank; and (ii) increased tenor of MSME loans.

B. Alignment with ADB Strategy and Operations

26. **Consistency with Strategy 2020 and country strategy.** Under Strategy 2020, ADB will promote inclusive growth at the regional and national levels by helping to develop financial

infrastructure, institutions, and products and services.²³ Through such initiatives, ADB will continue to assist in channeling the region's savings into the most productive investments, as well as build the capacity of financial institutions by introducing international best practices. ADB assistance supports institutional and financial sector development through the deepening of the financial sector by increasing the ability of Khan Bank to expand lending to MSMEs and by strengthening the bank's capital base.

27. The country partnership strategy for Mongolia highlights private sector development as a driver of change, and states that ADB will help strengthen financial markets to support long-term investment, innovation, and access to finance.²⁴ The strategy also notes that access of SMEs and the rural population to formal sources of credit is limited. ADB's financial sector assessment for Mongolia concludes that broader and deeper financial intermediation is necessary to achieve sustainable, long-term growth.²⁵ The finance sector assessment recommends the continued development of the finance sector and improvements in access to finance. The proposed loan is also consistent with the government's SME development program targeting SME capacity development and job creation.

28. **Consistency with sector strategy and relevant ADB operations.** An independent evaluation of ADB's assistance to the financial sector was conducted in 2008.²⁶ Based on the analysis conducted and future challenges and opportunities in the financial sector, recommendations were put forward for future operations. These included (i) considering equity investments and loans to strengthen the operational capacity of Mongolian banks; (ii) using banks to channel credit to address the gap in the supply of rural finance; (iii) providing longer-term loans to meet the needs of MSMEs; and (iv) supporting the development of nonbank and capital market sectors. The proposed assistance to Khan Bank is therefore consistent with the recommendations put forward in this evaluation.

V. POLICY COMPLIANCE

A. Safeguards and Social Dimensions

29. The investment is classified category FI for impacts on the environment, involuntary resettlement and indigenous peoples. The investment's potential environment and social impacts, its risks associated with Khan Bank's existing and/or likely future portfolio, and its commitment and capacity for environmental and social management, have been assessed. Khan Bank will apply ADB's prohibited investment activities list, ensure that investments using ADB funds abide by applicable national laws and regulations, comply with ADB Safeguard Policy Statement (2009), and establish and maintain an appropriate environmental and social management system satisfactory to ADB before disbursement for the financing of investments. ADB funds will exclude financing of subprojects classified category A for environment, and category A and B for involuntary resettlement and indigenous peoples safeguards.²⁷

²³ ADB. 2008. *Strategy 2020: The Long-Term Strategic Framework of the Asian Development Bank, 2008–2020*. Manila.

²⁴ ADB. 2012. *Country Partnership Strategy: Mongolia, 2012–2016*. Manila.

²⁵ ADB. 2010. *Mongolia: A Financial Sector Assessment*. Manila.

²⁶ ADB. 2008. *Evaluation Study: Financial Sector in Mongolia—Transition to a Market Economy Built on Successful Financial Reforms*. Manila.

²⁷ Summary Poverty Reduction and Social Strategy; Safeguards and Social Dimensions Summary; Environmental and Social Management System Arrangement (accessible from the list of linked documents in Appendix 2).

30. Khan Bank's environmental and social management system will include arrangements to comply with national labor laws and ADB's Social Protection Strategy²⁸ to ensure adherence to internationally recognized core labor standards, including provisions prohibiting any discrimination against women in hiring and providing equal pay for equal work for men and women. The investment is classified under operations with some gender elements.²⁹

B. Anticorruption Policy

31. Khan Bank was advised of ADB's policy of implementing best international practices relating to combating corruption, money laundering, and the financing of terrorism. ADB will ensure that the investment documentation includes appropriate provisions prohibiting corruption, money laundering, and the financing of terrorism, and remedies for ADB in the event of noncompliance.

C. Investment Limitations

32. The proposed loans are within the medium-term country, industry, group, and single investment exposure limits for nonsovereign investments.

D. Assurances

33. Consistent with the Agreement Establishing the Asian Development Bank,³⁰ the Government of Mongolia will be requested to confirm that it has no objection to the proposed assistance to Khan Bank. ADB will enter into suitable finance documentation, in form and substance satisfactory to ADB, following approval of the proposed assistance by the Board of Directors.

VI. RECOMMENDATION

34. I am satisfied that the proposed senior loan would comply with the Articles of Agreement of the Asian Development Bank (ADB) and recommend that the Board approve the loan of up to \$40,000,000 to Khan Bank for Supporting Micro, Small, and Medium-Sized Enterprises in Mongolia, from ADB's ordinary capital resources, with such terms and conditions as are substantially in accordance with those set forth in this report, and as may be reported to the Board.

Takehiko Nakao
President

6 June 2014

²⁸ ADB. 2001. *Social Protection Strategy*. Manila.

²⁹ Khan Bank commits to implement the following gender measures: (i) prioritize hiring of women for at least 60% of jobs created; (ii) provide training to Khan Bank staff on servicing MSMEs and borrowers; (iii) provide assistance including training to individual borrowers and MSMEs through Khan Bank's Business Incubator Centre; and (iv) include gender-disaggregated information in the annual report.

³⁰ ADB. 1966. *Agreement Establishing the Asian Development Bank*. Manila.

LIST OF LINKED DOCUMENTS

<http://adb.org/Documents/RRPs/?id=47934-001-3>

1. Sector Overview
2. Ownership, Management, and Governance
3. Details of Implementation Arrangements
4. Contribution to the ADB Results Framework
5. Financial Analysis
6. Country Economic Indicators
7. Summary Poverty Reduction and Social Strategy
8. Safeguards and Social Dimensions Summary