

# Project Administration Manual

Project Number: 48015-002  
Loan Number: LXXXX  
October 2015

Proposed Loan and Technical Assistance Grant  
Mongolia: Supporting the Credit Guarantee System  
for Economic Diversification and Employment  
Project

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## **Project Administration Manual Purpose and Process**

The project administration manual (PAM) describes the essential administrative and management requirements to implement the project on time, within budget, and in accordance with Government and Asian Development Bank (ADB) policies and procedures. The PAM should include references to all available templates and instructions either through linkages to relevant URLs or directly incorporated in the PAM.

The Ministry of Finance and the Credit Guarantee Fund of Mongolia are wholly responsible for the implementation of ADB financed project, as agreed jointly between the borrower and ADB, and in accordance with Government and ADB's policies and procedures. ADB staff is responsible to support implementation including compliance by Ministry of Finance and the Credit Guarantee Fund of Mongolia of their obligations and responsibilities for project implementation in accordance with ADB's policies and procedures.

At Loan Negotiations the borrower and ADB shall agree to the PAM and ensure consistency with the Loan and Project agreement. Such agreement shall be reflected in the minutes of the Loan Negotiations. In the event of any discrepancy or contradiction between the PAM and the Loan Agreement, the provisions of the Loan Agreement shall prevail.

After ADB Board approval of the project's report and recommendations of the President (RRP) changes in implementation arrangements are subject to agreement and approval pursuant to relevant Government and ADB administrative procedures (including the Project Administration Instructions) and upon such approval they will be subsequently incorporated in the PAM.

## Abbreviations

ADB	=	Asian Development Bank
AFS	=	audited financial statements
BOM	=	Bank of Mongolia
CDTA	=	capacity development technical assistance
CGFM	=	Credit Guarantee Fund of Mongolia
DMF	=	design and monitoring framework
EIA	=	environmental impact assessment
EMP	=	environmental management plan
ESMS	=	environmental and social management system
GACAP	=	governance and anticorruption action plan
GDP	=	gross domestic product
GOM	=	Government of Mongolia
GRM	=	grievance redress mechanism
ICB	=	international competitive bidding
IEE	=	initial environmental examination
LIBOR	=	London interbank offered rate
MOF	=	Ministry of Finance
MOI	=	Ministry of Industry
NGOs	=	nongovernment organizations
NPL	=	non-performing loan
OCR	=	ordinary capital resources
PAI	=	project administration instructions
PAM	=	project administration manual
PCU	=	public complaints unit
PFI	=	participating financial institution
PIU	=	Credit Guarantee Fund project implementation unit
PSC	=	Project Steering Committee
REA	=	rapid environmental assessment
RRP	=	report and recommendation of the President to the Board
SME	=	small to medium sized enterprise
SOE	=	statement of expenditure
SPS	=	ADB Safeguard Policy Statement (2009)
SPRSS	=	summary poverty reduction and social strategy
TASF	=	Technical Assistance Special Fund
TOR	=	terms of reference

## I. PROJECT DESCRIPTION

### A. Rationale, Location and Beneficiaries

1. The Government of Mongolia (GOM) has requested the Asian Development Bank (ADB) to provide lending support to small and medium-sized enterprises (SMEs) by backing the credit guarantee system operated by the Credit Guarantee Fund of Mongolia (CGFM).<sup>1</sup> The proposed Supporting the Credit Guarantee System for Economic Diversification and Employment Project will expand access to finance by SMEs to diversify the economy through job creation in non-mining related sectors. The objective of the proposed loan is to improve SME access to finance and business sustainability thereby fostering growth, economic diversification, and employment creation. The TA will improve the quality of the CGFM and the credit guarantee system.

2. **Development problems and opportunities.** The Mongolian economy is heavily reliant on the mining sector contributing about 25% of gross domestic product and placing the country at risk from commodity price fluctuations. Micro, small and medium-sized enterprises are an important job source accounting for 90% of registered businesses and approximately 50% of employment. Yet, up to 90% of the 36,800 SMEs do not have regular access to finance through banks. Limited access to finance impairs the ability of SME's to contribute more fully to economic diversification, employment creation and growth. Access to finance for SMEs is impaired by their lack of pledgeable collateral, a lack of longer-term loans offered by banks at reasonable rates, and the liquidity constraints faced by banks in funding longer-term lending. Further impairments result from an inadequate credit information base,<sup>2</sup> burdensome requirements when applying for credit, SMEs lack financial management knowledge, and underdeveloped loan underwriting capabilities of banks. The value of total outstanding SME and small business purpose loans stood at MNT1,270 billion at year-end 2014 comprising approximately 10.2% of total loans in the financial system down from 16.8% in 2013.

3. SMEs often rely on borrowed collateral for use in pledging when seeking loans or face no financing for investment needs and growth. The lack of collateral is even more problematic for SMEs run by women. While an ownership and liens' register on immovable property exists,<sup>3</sup> a system to enforce security interests of moveable assets does not. This impairs development of alternative sources of collateral apart from real estate. Standards for asset appraisals are also weak impairing collateral value credibility. Tight liquidity conditions of banks, partially due to an underdeveloped longer-term deposit market, pose obstacles to their offering of longer-term loans appropriate for capital investments. Yet, banks tend to emphasize only short-term loans to SMEs to better match their shorter funding sources regardless of SME needs. Additionally, with bank loan rates in MNT normally over 16% per annum and generally found in the 22-26% range for SMEs, due to lower foreign currency interest rates and to help balance foreign currency open positions, banks often stress issuance of US dollar loans to SMEs. This

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<sup>1</sup> A 100% state owned enterprise established under the Law on the Credit Guarantee Fund of Mongolia of 2012. Members include the Ministry of Finance, Ministry of Labour, Ministry of Industry, Financial Regulatory Commission, National Chamber of Commerce and Industry, and Mongolian Employers Federation. Capital has only been injected by the government of Mongolia.

<sup>2</sup> Bank of Mongolia operates a credit registry. Credit Information Bureau LLC was established in 2009 by the Mongolian Bankers Association under the support of United States Agency for International Development. However, it has yet to operationalize.

<sup>3</sup> On 25 March 2014 the International Finance Corporation signed a cooperation agreement with the Ministry of Justice to reform the secured transaction system by collaborating to establish a proper legal framework for secured transactions by a new law on pledging, an online registry for moveable property, and to raise awareness and train industry professionals.

is despite their lack of repayment capacity in foreign currency. The Mongolian National Chamber of Commerce and Industry reported a rising number of SME bankruptcies due to increased debt service requirements from loans made in US dollar.

4. In response to SMEs' impediments with collateral, the GOM established the CGFM in November 2012. Operations began in April 2013. CGFM currently cooperates with 10 banks and 6 non-bank financial institutions. While its overall impact on the economy has been limited, results are positive with jobs created with each guarantee issued. CGFM's impact none-the-less remains constrained by having only one basic guarantee product, a lack of operational capacity, and limited expertise. SME use of credit guarantees is also impaired by low awareness of credit guarantee availability by potential borrowers, weak marketing of program offerings, and a lack of financial management knowledge by SMEs when seeking loans. Further, no law exists that specifically defines operation of a private guarantee system.

5. Commercial banks in Mongolia dominate the financial sector, accounting for 96% of total financial assets. The financial sector is underdeveloped with a narrow range of products and service offerings, and weaknesses in risk assessment capabilities when underwriting new loans. Ensuring local financial markets are capable of providing additional long-term funding is an essential part of facilitating Mongolia's growth.

6. The proposed loan will back previous and ongoing ADB lending programs supporting the development of a sound and broad-based financial sector that effectively channels resources to productive investment. These efforts include supporting financial regulation and governance seeking to reduce the cost of borrowing and expand access to credit by improving the framework for secured transactions and enhancing the role of the non-bank financial sector in savings mobilization for investment capital.<sup>4</sup> Additional effort focused on supporting rural finance to increase the availability of and access to savings and credit services in rural areas and among the poor.<sup>5</sup>

7. **Government plans and linkage with country partnership strategy.** The project is consistent with the Millennium Development Goal-based Comprehensive National Development Strategy of Mongolia.<sup>6</sup> The government also has approved the "SME development program 2014-2016".<sup>7</sup> The project is consistent with the Interim Country Partnership Strategy for Mongolia, 2014–2016, which seeks to promote the financial sector as a new priority area.<sup>8</sup> The project pursues financial sector development, one of ADB's core areas of operation under Mid-term Review Strategy 2020.<sup>9</sup> The project will build on previous and ongoing ADB lending programs<sup>10</sup> that included supporting financial regulation and governance, expanding access to credit, and enhancing the role of the non-bank financial sector. Additionally, rural finance was supported to increase the availability of savings and credit services in rural areas and among

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<sup>4</sup> ADB. 2005. *Report and Recommendation of the President to the Board of Directors: Proposed Loan on Financial Regulation and Governance Program*. Manila (Loan 2218).

<sup>5</sup> ADB. 2001. *Report and Recommendation of the President to the Board of Directors: Proposed Loan on Rural Finance*. Manila (Loan 1848).

<sup>6</sup> Government of Mongolia. 2008. *Millennium Development Goal-based Comprehensive National Development Strategy of Mongolia* (State Great Hural, Resolution No.12, 2008). Ulaanbaatar.

<sup>7</sup> Government of Mongolia. Ministry of Labour. 2013. *SME Development Program*. Ulaanbaatar.

<sup>8</sup> ADB. 2014. *Interim Country Partnership Strategy for Mongolia, 2014–2016*. Manila.

<sup>9</sup> ADB. 2014. *Midterm Review Strategy 2020: Meeting the Challenges of a Transforming Asia and Pacific*. Manila.

<sup>10</sup> ADB. 2005. *Report and Recommendation of the President to the Board of Directors: Proposed Loan on Financial Regulation and Governance Program*. Manila (Loan 2218) and ADB. 2001. *Report and Recommendation of the President to the Board of Directors: Proposed Loan on Rural Finance*. Manila (Loan 1848).

the poor.<sup>11</sup> The project is an extension of ADB's SME on-lending programs,<sup>12</sup> and TA work in microfinance, mobile and branchless banking, and regulatory and supervisory frameworks.<sup>13</sup>

**8. Development partners and lessons.** Nearly no assistance has been provided to the CGFM by development partners. Only Japan International Cooperation Agency (JICA) has provided CGFM with limited periodic training and has proposed placement of a volunteer credit guarantee expert. Development partner assistance has primarily focused on supporting SME development and by providing financing for private enterprises with no or limited access to finance. Much of such assistance was aimed at addressing the high cost of loans by offering concessional rates, but not addressing the unavailability of collateral to obtain loans or the lack of availability of long-term funding in banks. Although an increasing number of development partners are working in SME development and financing, limited access to affordable longer-term finance continues to constrain SMEs. Key lessons from these programs reflect the need to overcome collateral unavailability by SMEs and to support the financial system's development of a longer-term funding base.

## **B. Impact, Outcome and Outputs**

9. The impact will be increased job creation in non-mining related sectors. The outcome will be SMEs' access to finance expanded.

**10. Output 1: Longer-term financing for SMEs increased.** Up to \$60.0 million of funding will be made available under the proposed financial intermediation loan enabling participating financial institutions (PFI) to make long-term loans denominated in local currency<sup>14</sup> to SMEs for eligible sub-projects.<sup>15</sup> In addition, the project will back introduction of new guarantee products to support up to \$432.0 million of SME sub-projects creating up to 13,200 jobs over the life of the ADB loan.<sup>16,17</sup> Output 1 will be accomplished by: (i) helping PFIs mitigate maturity mismatches by placing time deposits into PFIs to fund a portion of their eligible SME sub-loans; and (ii) CGFM guaranteeing a portion of the credit risk of these sub-loans. Possibilities will be identified for enhanced inclusion of low-income groups outside the capital and women entrepreneurs into the credit guarantee system through creation of new targeted credit guarantee products.

<sup>11</sup> ADB. 2001. *Report and Recommendation of the President to the Board of Directors: Proposed Loan on Rural Finance*. Manila (Loan 1848).

<sup>12</sup> ADB. 2014. *Report and Recommendation of the President to the Board of Directors: Proposed Loan to Khan Bank Supporting Micro, Small, and Medium-Sized Enterprises*. Manila (Loan 7410); ADB. 2013. *Report and Recommendation of the President to the Board of Directors: Proposed Senior Loans XacBank and TenGer Financial Group Supporting Micro, Small, Medium-Sized Enterprises and Leasing Finance*. Manila (Loan 7401).

<sup>13</sup> ADB. 2000. *Technical Assistance to Mongolia for Rural Finance*. Manila (TA 3397); ADB. 2009. *Technical Assistance to Mongolia for Transformational Mobile Banking Services*. Manila (TA 7479); and, ADB. 2009. *Technical Assistance to Mongolia for Policy and Institutional Support for Banking Sector Systemic Risk Management*. Manila (TA 7397).

<sup>14</sup> Ministry of Finance will convert ADB loan funds to MNT for on-lending to CGFM. CGFM will then place funds on time deposit in qualified PFIs up to the level of the guarantee percentage issued and for the maturity of eligible SME sub-loans.

<sup>15</sup> Eligible SME sub-loans must be for at least 5 year maturity consistent with lending for capital investments. An exception is allowed in that at any time, only up to 15% of the gross amount of the Subsidiary Loan Agreement shall be used for SME loans with repayment period of or tenor less than five years.

<sup>16</sup> The maximum regulatory leverage of 10x the \$9.0 million gross current and projected capital base of CGFM or \$90.0 million of issued guarantees. Assuming PFIs will lend only 75% of SMEs' total project cost, \$90.0 million of guarantees can support \$120.0 million of SME sub-projects at one time without considering recycling. Economic analysis shows that 13,200 jobs may be created and loan funds may be recycled 3.6 times over the project resulting in \$432 million of SME sub-projects' supported.

<sup>17</sup> As of 30 June 2015, CGFM has issued 364 guarantees for MNT 24.4 billion supporting MNT 59.7 billion of gross loans with an average 43 month tenor and creating 1,210 new jobs or an average of 3.3 jobs per guarantee.

Awareness raising and outreach programs by the CGFM will take place to make women and the rural poor aware of the credit guarantee system.

11. **Output 2: A longer-term bank deposit market developed.** Funding will be placed as MNT time deposits by the CGFM in PFIs establishing a market for 5-year deposits, building confidence in the MNT deposit market and encouraging private sector savings mobilization into longer-term funding. Market-based rates for time deposits will be utilized consistent with existing funding from government, unilateral and multinational organizations. Placement of time deposits in PFIs will require CGFM issuance of new guarantee products in support of eligible SME sub-loans. Funds will be recycled through the term of the ADB loan to support new SME sub-loans.



## II. IMPLEMENTATION PLANS

### A. Project Readiness Activities

12. Overall Project Readiness Activities are presented below.

Indicative Activities	2015					2016		Agency Responsible
	08	09	10	11	12	01	03	
Establish project implementation arrangements	■							CGFM, MOF, ADB
Staff Review Meeting		■						ADB
Loan Negotiations		■						ADB, CGFM, MOF
ADB Board consideration				■				ADB
Loan signing					■			ADB, CGFM, MOF
Government legal opinion provided						■		MOF, MOJ
Government budget inclusion							■	MOF
Loan effectiveness							■	MOF

ADB = Asian Development Bank, MOI = Ministry of Industry, MOF = Ministry of Finance, MOJ = Ministry of Justice, CGFM = Credit Guarantee Fund of Mongolia

### B. Overall Project Implementation Plan

13. Based on the implementation plan below, the project implementation will be completed by 31 March 2021 and the loan account will close by 31 October 2021. The subaccount will close within 6 months of when ADB loan funds are fully drawn-down and utilized. The overall project implementation plan is shown in Figure 1.

14. The overall implementation plan will be updated at the annual and mid-term reviews, as and when required by the CGFM and MOF. The updated implementation plan will be submitted to ADB for no objection. Further updating will take place as required during loan review, with contract and disbursement projections for the following year.



CGFM = Credit Guarantee Fund of Mongolia, EOI = expression of interest, ESMS = Environmental and Social Management System, PFI = participating financial institution, PIU = Project Implementation Unit, PSC = Project Steering Committee, SME = small and medium-sized enterprise.

### III. PROJECT MANAGEMENT ARRANGEMENTS

#### A. Project Implementation Organizations – Roles and Responsibilities

Project implementation organizations	Management Roles and Responsibilities
<b>Executing Agency:</b> • <b>Ministry of Finance (MOF)</b>	<ul style="list-style-type: none"> <li>➤ Enter into a subsidiary loan agreement with CGFM</li> <li>➤ Fulfill requests from the CGFM for drawdowns from the ADB loan and pass on proceeds to the CGFM promptly</li> <li>➤ Convert and reconvert ADB loan funds between US dollar and MNT</li> <li>➤ Participate in the monitoring and effective implementation of the project.</li> <li>➤ Submit audit reports to ADB</li> <li>➤ Assume responsibility for:               <ul style="list-style-type: none"> <li>○ repayment of the loan;</li> <li>○ conversion of US dollar loan proceeds into local currency and reconversions during repayment; and on-lending to the CGFM.</li> </ul> </li> <li>➤ Chair the PSC</li> <li>➤ Enter into tri-party time deposit and guarantee agreements among MOF, CGFM and PFIs</li> </ul>
<b>Implementing Agency:</b> • <b>Credit Guarantee Fund of Mongolia (CGFM)</b>	<ul style="list-style-type: none"> <li>➤ Assume direct accountability and responsibility for all Outputs</li> <li>➤ Assume overall accountability and responsibility for project planning, management and implementation</li> <li>➤ Enter into time deposit agreements with PFIs</li> <li>➤ Issue credit guarantees to PFIs for eligible SME sub-loans</li> <li>➤ Establish a monitoring program to ensure that implementation of subprojects will achieve the desired objectives</li> <li>➤ Participate in the effective implementation of the project</li> <li>➤ Support revision to the Law on the Credit Guarantee Fund of Mongolia</li> <li>➤ Oversee effective implementation of the project</li> <li>➤ Effectively manage the enhancement of the credit guarantee program by issuing new products, properly managing risks and supporting SME financing needs.</li> <li>➤ Enter into a subsidiary loan agreement with MOF</li> <li>➤ Place time deposits in PFIs that have received guarantees from CGFM for eligible SME loans</li> <li>➤ Serve as member of the PSCConduct environmental due diligence as specified in the ESMS</li> <li>➤ Monitor and guide the inclusion of social and gender safeguards within the project</li> <li>➤ Screen for indigenous peoples and involuntary resettlement impacts</li> </ul>
<b>Oversight body:</b> • <b>Project Steering</b>	<ul style="list-style-type: none"> <li>➤ Chaired by MOF</li> <li>➤ Comprises at least three members of relevant ministries,</li> </ul>

<b>Committee (PSC)</b>	<p>agencies and entities, including CGFM and the Ministry of Industry</p> <ul style="list-style-type: none"> <li>➤ Meets at least quarterly until 2019 and then bi-annually for the remainder of the project</li> <li>➤ Monitor project status under the project implementation plan and the appropriateness of sub-projects funded against project objectives and restrictions</li> <li>➤ Support coordination among stakeholders</li> <li>➤ Review and assess project implementation progress</li> <li>➤ Endorse the annual project budget for ADB approval</li> </ul> <p>Provide advice on policy matters relating to the project</p>
<b>Implementing Unit:</b> • <b>CGFM Project Implementation Unit</b>	<ul style="list-style-type: none"> <li>➤ Review and report on progress in project implementation</li> <li>➤ Guide and support implementation</li> <li>➤ Assist CGFM with project planning and implementation, including consultant recruitment for the CDTA and financial management</li> <li>➤ Prepare project progress reports</li> <li>➤ Prepare and obtain required project and financial audits</li> <li>➤ Prepare annual environmental progress reports</li> <li>➤ Prepare annual social and gender progress reports</li> <li>➤ Appoint a gender focal-point</li> <li>➤ Appoint an environmental safeguards focal-point</li> </ul> <p>Monitor Eligibility Criteria of PFIs and submit status reports to ADB</p>
<b>Participating Financial Institutions (PFIs):</b>	<ul style="list-style-type: none"> <li>➤ Conduct financial due diligence for proposed SME sub-loans in consultation with CGFM</li> <li>➤ Conduct environmental due diligence as specified in the ESMS</li> <li>➤ Monitor consultation and public disclosure. Ensure that borrowers conduct consultations with affected people and other concerned stakeholders, as specified in the ESMS</li> <li>➤ Propose SME sub-loans for guarantee issuance to CGFM</li> <li>➤ Issue new market-based, floating or fixed-rate local currency loans, leases and other forms of finance to eligible SMEs for eligible sub-projects, according to government and ADB policies and requirements</li> <li>➤ Monitor and track gender disaggregated data</li> </ul> <p>Monitor compliance with social and gender safeguards</p>
<b>Asian Development Bank (ADB)</b>	<ul style="list-style-type: none"> <li>➤ Assume responsibility for project administration ensuring timely execution of the loan and project agreements by the executing agency and implementing agency</li> <li>➤ Disburse loan proceeds</li> <li>➤ Review and approve consultant recruitment for the CDTA; safeguard compliance; and audit reports</li> </ul> <p>Conduct project implementation monitoring through review missions</p>

CDTA = capacity development technical assistance, MOI = Ministry of Industry, SME = small and medium-sized enterprises.

**B. Key Persons Involved in Implementation**

<b>Executing Agency</b> <b>MOF</b>	Badamkhatan Gantulga Director General Development Financing and Debt Management Department, MOF E-mail: <a href="mailto:gantulga.b@mof.gov.mn">gantulga.b@mof.gov.mn</a> Nyamaa Buyantogtokh Director General of Financial Policy Department, MOF E-mail: <a href="mailto:nyamaa_b@mof.gov.mn">nyamaa_b@mof.gov.mn</a> Manduul Nyamandele Director of Financial Market and Insurance Division, Financial Policy Department, MOF E-mail: <a href="mailto:manduul_n@mof.gov.mn">manduul_n@mof.gov.mn</a> Narangerel Nyamsambu Director of Debt Management Division, Development Financing and Debt Management Department, MOF E-mail: <a href="mailto:Narangerel_n@mof.gov.mn">Narangerel_n@mof.gov.mn</a> Telephone: +976 51 262 272 Fax No.: +976 51 267 468 Address: Government Building 2, Danzan Street- 5/1, Chingeltei District, Ulaanbaatar-15160, Mongolia
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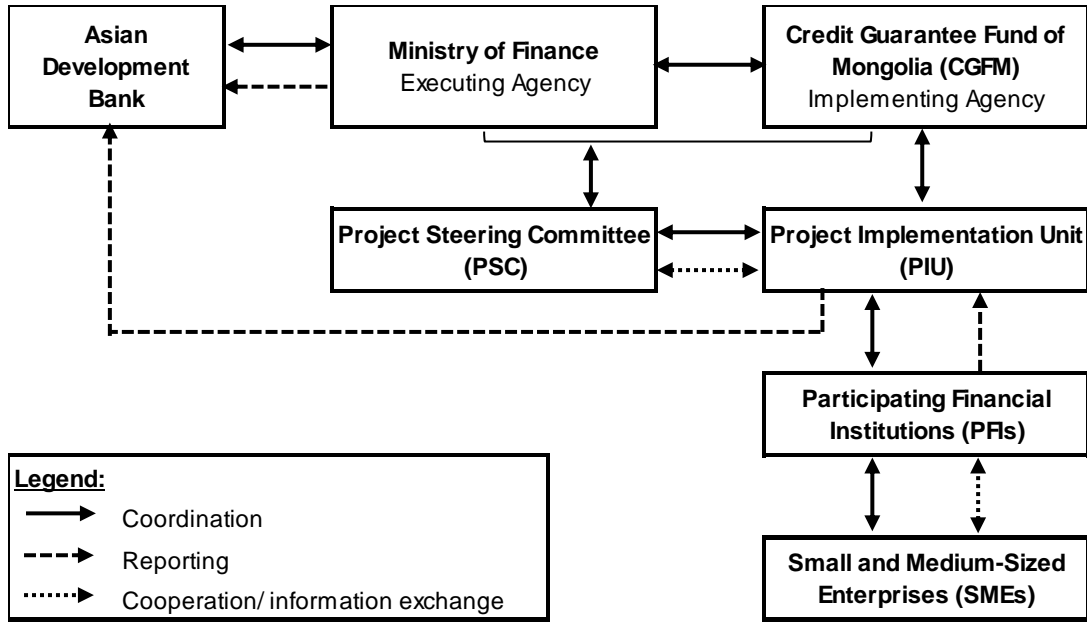
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**C. Project Organization Structure**





#### IV. COSTS AND FINANCING

15. The project is estimated to cost \$90 million (Table 1). The government has requested a loan of \$60.0 million from ADB's ordinary capital resources to help finance the project. The loan will have an 18-year term, including a grace period of 12 years, an annual interest rate determined in accordance with ADB's London interbank offered rate (LIBOR)-based lending facility, a commitment charge of 0.15% per year (the interest and other charges during implementation to be capitalized in the loan), and such other terms and conditions set forth in the draft loan and project agreements. The loan will have principal repayments in semi-annual instalments over the last 6 years of the loan to allow for the recycling of funds and to support long-term maturities of SME sub-loans and interest will be repaid semi-annually and interest will be repaid semi-annually with interest and commitment fees capitalized up to the allocation amount in Table 1 to support the build-up of capital and reserves in CGFM allowing for future leverage capacity.

16. Ministry of Finance (MOF) will re-lend ADB loan funds to CGFM<sup>18</sup> which will place deposits in PFIs that meet selection criteria agreed with ADB and that have received guarantees from CGFM for SME loans for eligible sub-projects. Each PFI will use the deposits and guarantees received to issue new market-based, floating or fixed-rate MNT loans, leases and other forms of finance to eligible SMEs for eligible sub-loans. CGFM may recycle ADB loan proceeds to make new deposits throughout the tenor of the ADB loan potentially allowing for up to \$432 million of SME sub-projects to be supported. All payment and repayment obligations of Mongolia under the ADB loan are independent of the timely and due performance by CGFM under the relevant subsidiary loan agreement, SME borrowers under the relevant SME loan agreements and any conversion or hedging risk borne by Mongolia in the conversions of the ADB loan into MNT or reconversion to USD.

17. CGFM will charge a market-based rate on the deposits placed in eligible PFIs consistent with existing funding available from government, unilateral and multinational organizations for SME lending support. CGFM will receive a market-based fee to cover the risk assumed for issuance of credit guarantees. Each PFI will use the deposits and guarantees received to issue new market-based, floating or fixed-rate local currency loans, leases and other forms of finance to eligible SMEs for eligible sub-loans. ADB loan funds may be used to support SME eligible sub-loans, through deposits placed by the CGFM, if their maturity is at least 5 years.<sup>19</sup> A small

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<sup>18</sup> A subsidiary loan agreement will be completed between MOF and CGFM in MNT. The terms for relending the proceeds of the Loan in MNT to CGFM shall include: (i) for the first three years of the Loan, an interest rate only up to of 1% on the balance of the Loan funds disbursed to CGFM in MNT, and after the first three years of the Loan, the Borrower may charge CGFM on the disbursed Loan balance a maximum of the pass-through rate of interest charged by ADB, plus only up to 0.5% and may additionally charge only up to 0.15% on the undisbursed balance of the Loan; and (ii) a repayment tenor consistent with the Loan.

<sup>19</sup> The volume of time deposits placed in a PFI will be linked to the level of guarantee issued for eligible SME sub-loans. Only eligible sub-loans that use new guarantee products will be eligible to receive partial ADB loan funding. Time deposits will be placed in PFIs at maturities equal to the principal amortization schedule of the underlying portfolio of SME sub-loans in annual maturity increments to the maximum of the level of guarantee percentage issued. Time deposits will be placed up to 5-year maturity and if the principal amortization schedule for the portfolio of SME Loans reflects tenors longer than five years, then all remaining amortizations beyond five years shall be cumulated into a five-year time deposit and then at the five-year maturity, the time deposits shall be rolled over into new time deposits, using the same method described herein, to cover the remaining portfolio amortization schedule through the final maturity of the portfolio of SME Loans. Co-funding from CGFM will be placed in PFIs at the same terms and conditions as deposits using ADB loan funds. Time deposits placed by CGFM into PFIs will pay a market-based rate in line with the government and other development agencies' loan financing programs as determined by ADB from time to time. The initial rate will be set by ADB and after three years, it shall be reset by ADB in line with the government and other development agencies' loan financing programs. The interest rate on

portion of ADB loan funds may be used to fund SME eligible sub-loans with a maturity of less than 5 years if they support the outputs and objectives of this project and utilize new guarantee products issued by CGFM.<sup>20</sup> CGFM may recycle ADB loan proceeds to make new deposits on new guarantees issued throughout the tenor of the requested ADB loan.

18. A 12 year grace period is necessary to allow CGFM to recycle ADB loan proceeds approximately 3.6 times throughout the tenor of the ADB loan by supporting placement of new, recurring time deposits linked to guarantees issued for new SME sub-loans. The grace period also allows supporting the issuance of long-term maturities of SME sub-loans that can provide for capital investment lending. With recycling, up to \$432 million of SME sub-projects potentially may be supported. In order to support the build-up of capital in CGFM, allowing for additional guarantee issuance capacity through leverage, interest and commitment fees will be capitalized up to the allocation amount.

19. On an ongoing basis, a PFI will make sub-loans and obtain guarantees from CGFM at various coverage ratios, for various maturities, and according to various principal amortization schedules of the sub-loans. Each PFI’s guarantee portfolio will be cumulated at the end of each month into a representative portfolio amortization pool to calculate each portfolio’s cumulative amortization schedule by annual increments. Time deposits will then be placed by CGFM in the PFI at maturities equal to the portfolio’s principal amortization schedule in minimum yearly increments, but to no more than a 5 years tenor. If the principal amortization schedule for the portfolio of SME Loans reflects tenors longer than five years, then all remaining amortizations beyond five years shall be cumulated into a five-year time deposit and then at the five-year maturity, the time deposits shall be rolled over into new time deposits, using the same method described herein, to cover the remaining portfolio amortization schedule through the final maturity of the portfolio of SME Loans. Through assistance from the TA, the specific methodology and formulae will be refined to support this methodology.

**A. Summary Financing Plan**

**Table 1: Project Investment Plan**  
(\$ million)

<b>Item</b>	<b>Total</b>
<b>A. Cost<sup>a</sup></b>	
Funding for eligible SME sub-loans	88.63
<b>Subtotal (A)</b>	<b>88.63</b>
<b>B. Financing Charges During Implementation<sup>b</sup></b>	<b>1.37</b>
<b>Total (A+B)</b>	<b>90.00</b>

ADB = Asian Development Bank, SME = small and medium-sized enterprises.  
<sup>a</sup> Refers to time deposits funded from ADB loan and CGFM co-funding plus PFIs’ funding contribution  
<sup>b</sup> Includes interest and commitment charges estimated for a 3-year period computed for ADB’s ordinary capital resources loan at the 3-year US dollar (USD) fixed swap rate plus an effective contractual spread of 0.5% and maturity premium of 0.1%. Commitment charges for an OCR loan are 0.15% per year to be charged on the undisbursed loan amount.  
Source: Asian Development Bank

escrow account balances will be at market rates at maturity of no more than 1 month. Time deposit and escrow agreements will be confirmed by ADB and cannot be changed without ADB clearance.  
<sup>20</sup> Ibid 15

**Table 2: Financing Plan**

Source	Amount (\$ million)	Share of Total (%)
Asian Development Bank		
Ordinary capital resources (loan)	60.0	66.7
Private sector <sup>a</sup>	21.9	24.3
Government <sup>b,c</sup>	8.1	9.0
<b>Total</b>	<b>90.0</b>	<b>100.0</b>

<sup>a</sup> Difference between ordinary capital resources loan funds and available Credit Guarantee Fund of Mongolia funding and reflects sources contributed by participating financial institutions to partially fund small and medium-sized enterprise guaranteed loans.

<sup>b</sup> Comprises \$8.1 million of current capital and additional proposed capital to be sourced by either proposed Government of Mongolia additional capital injection or through retained earnings available at the Credit Guarantee Fund of Mongolia net of required hold-back of 10% according to supervisor regulations.

<sup>c</sup> The Government will finance and local taxes and duties that may be due under the project.

Source: Asian Development Bank

## B. Allocation of Loan Proceeds

**Table 3: Allocation Plan**

Allocation and Withdrawal of Loan Proceeds			
Number	Item	Total Amount Allocated for ADB Financing (\$) Category	Basis for Withdrawal from the Loan Account
1	Time Deposits for eligible SME sub-loans <sup>a</sup>	58,630,000.00	90.0% of total expenditure
2	Interest and Commitment Charges	1,370,000.00	100.0% of amount due
	<b>Total</b>	<b>60,000,000.00</b>	

<sup>a</sup> Linked to issuance of new guarantees on eligible SME sub-loans. Subject to condition for withdrawals in the Loan Agreement and described in the PAM.

## C. Summary Cost Estimates

**Table 4: Summary Cost Estimates**  
(\$ million)

Item	Current Amount	Total
<b>A. Base Cost<sup>c</sup></b>		
1. Time Deposits for eligible SME sub-loans	88.63	88.63
<b>Subtotal (A)</b>	<b>88.63</b>	<b>88.63</b>
<b>B. Financing Charges During Implementation<sup>a</sup></b>	<b>1.37</b>	<b>1.37</b>
<b>Total (A+B)</b>	<b>90.00</b>	<b>90.00</b>

<sup>a</sup> Interest and commitment charges during the first 3 years of the loan

#### D. Detailed Cost Estimates by Financier

**Table 5: Detailed Cost Estimates by Financier  
(\$ million)**

Item	ADB		CGFM		PFIs		Total Cost {D}
	Amount	% of Cost Category	Amount	% of Cost Category	Amount	% of Cost Category	
	{A}	{A/D}	{B}	{B/D}	{C}	{C/D}	
<b>A. Investment Costs</b>							
1 Time Deposits for eligible SME sub-loans	58.63	66.2	8.10	9.1	21.90	24.7	88.63
Interest and	1.37	100.0	0.00	0.0	0.00	0.0	1.37
2 Commitment Charges							
<b>Total Cost</b>	<b>60.00</b>	66.7	<b>8.10</b>	9.0	<b>21.90</b>	24.3	<b>90.00</b>
<b>Total Project Cost</b>	<b>0.00</b>	0.0	<b>0.00</b>	0.0	<b>0.00</b>	<b>0.0</b>	<b>0.00</b>
<b>% Total Project Cost</b>		<b>66.7</b>		<b>9.0</b>		<b>24.3</b>	<b>100</b>

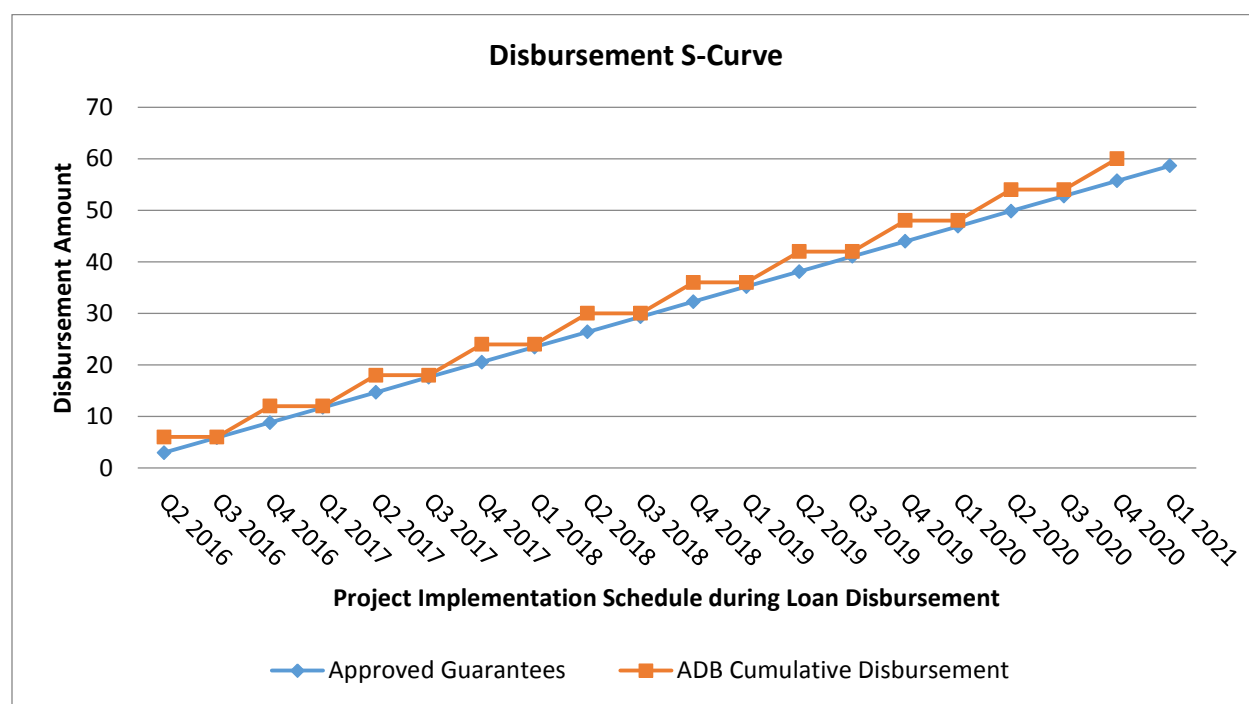
## E. Disbursement S-curve

20. Figure 1 shows the estimated disbursement progress over the implementation period of the Project. The Disbursement S-Curve will help to assess disbursement performance at any time during the project implementation. In case of delays and poor disbursements, this will help as an early warning system for taking timely remedial measures.

**Table 6: Schedule of Disbursement**

Years	New Guarantee Issuance (\$ Million)					Disbursement (\$ Million)				
	Q1	Q2	Q3	Q4	Total	Q1	Q2	Q3	Q4	Total
2016	0.00	2.96	2.93	2.93	8.82	0.00	6.00	0.00	6.00	12.00
2017	2.93	2.93	2.93	2.93	11.72	0.00	6.00	0.00	6.00	12.00
2018	2.93	2.93	2.93	2.93	11.72	0.00	6.00	0.00	6.00	12.00
2019	2.93	2.93	2.93	2.93	11.72	0.00	6.00	0.00	6.00	12.00
2020	2.93	2.93	2.93	2.93	11.72	0.00	6.00	0.00	6.00	12.00
2021	2.93	0.00	0.00	0.00	2.93	0.00	0.00	0.00	0.00	0.00
<b>Total</b>					<b>58.63</b>					<b>60.00</b>

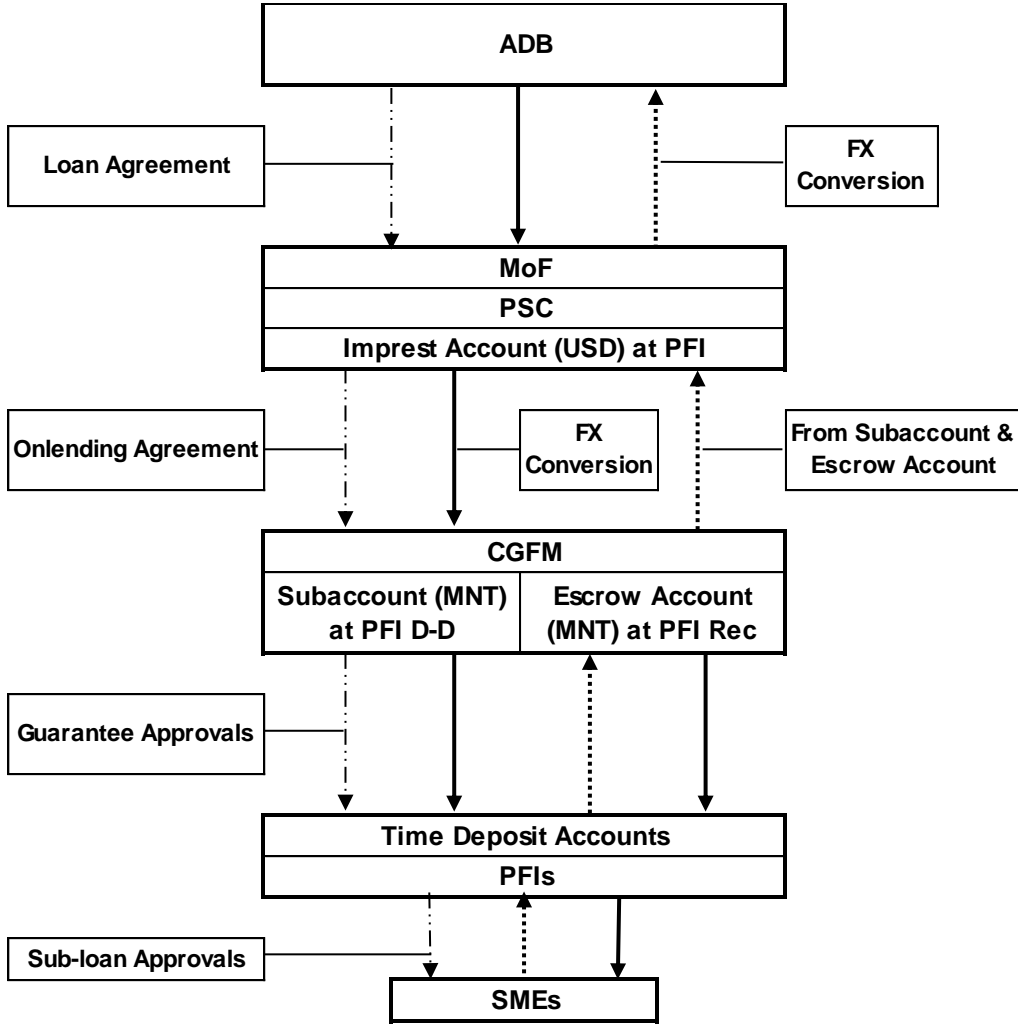
**Figure 1: S-Curve**



21. ADB loan proceeds will initially be drawn-down to the imprest account based on the estimated time deposits to be placed for the forthcoming 6 months. Loan proceeds are expected to be fully drawn-down over the first 5 years or sooner depending on the speed of issuance of new guarantees. A simple straight-line estimate of drawdowns of equal amounts semi-annually is assumed through year 5 equal to the estimated volume of new guarantees issued and time deposits placed by CGFM. More specific drawdown estimates cannot be made

as demand for new guarantee products yet to be created, the need to enhance capacity of CGFM, and the need for PFIs to become more comfortable with issuing longer-term loans must be upgraded over the first few years of the project. While financial and economic analysis indicates that substantial SME loan demand exists, specific utilization can only be estimated at this time.

**F. Fund Flow Diagram**



**Legend:**

- > ADB Loan Advance and Deposit
- .....> Repayment
- . . -> Financing Agreement
- D-D** Draw-Downs
- Rec** Recycling of Funds
- PSC** Project Steering Committee

ADB = Asian Development Bank, BOM = Bank of Mongolia, CGFM = Credit Guarantee Fund of Mongolia, FX = foreign exchange, MNT = Mongolian Tugrik, PFI = participating financial institution, SME = small and medium-sized enterprise, USD = US Dollar.

## V. FINANCIAL MANAGEMENT

### A. Financial Management Assessment

22. **CGFM.** A Financial management assessment (FMA) of CGFM was conducted in May 2015 in accordance with ADB's Guidelines for the Financial Management and Analysis of Projects and the Financial Due Diligence: a Methodology Note. The FMA confirmed that CGFM has adequate capacity for financial management of the project. Staff with a suitable range of skills and familiar with government and ADB requirements on disbursement, procurement, and social and environmental safeguards will be selected by CGFM to form a CGFM PIU that will manage project implementation. The selection will be approved by ADB. A wide diagnostic assessment of the CGFM was completed during due diligence. While the assessment identified strengths and progression by the CGFM since its founding it also identified areas that must be strengthened so as to more effectively deliver its mandate and meet financial management needs more fully through the project. Recommendations include development of a strategic plan, improving policies to address credit risk, establishing a full formal risk management unit, enhancing human resource policies, and improving Management Information Systems.<sup>21</sup> Prior to steps being taken to augment CGFM financial management practices supported by the TA, financial management pre-mitigation risk of CGFM is moderate.

**Table 7: Summary of the Financial Management Assessment**

<b>Particulars</b>	<b>Conclusions</b>
<b>A. Funds Flow Arrangements</b>	Funds denominated in US dollars will be provided to MOF. CGFM may draw-down funds through a subsidiary loan agreement as guarantees are issued to PFIs that have made eligible SME sub-loans. Once funds are fully mobilized, and some SME loans begin to repay sub-loans, the linked time deposit funds will be recycled back to the CGFM to use for new time deposits supporting new guarantees issued on new eligible SME sub-loans. This recycling is important to ensure that the project has broad impact and can leverage-up the funds. MOF will complete a foreign currency conversion into MNT for on-lending to CGFM. As the CGFM issues guarantees to PFIs for SME sub-loans, the CGFM will place time deposits equal to the level of the guarantee issued for the same tenor as the sub-loans in PFIs. Funds flow arrangements are appropriate and acceptable.
<b>B. Staffing</b>	Loan officers working in CGFM usually have four years or more of experience in Mongolian commercial banks. Accordingly, CGFM is staffed with experienced financial specialists who are experts in managing internal finance. CGFM has sufficient staff to support loan processing at project start-up. Staff will need further training and development on reporting and monitoring on use of loan funds and placement of time deposits in PFIs.
<b>C. Accounting Policies &amp; Procedures</b>	The chart of accounts based on the national government standard format has been in use since the founding of CGFM. Segregation of duties is specified for budgeting, payments, policies and procedures, cash and bank transactions, and safeguards over assets. A separate financial management manual within the CGFM PIU is planned to be established for the Project in accordance with ADB requirements. Longer-term budgeting linked to strategic objectives is needed to improve performance over a longer period. Financial management policies and procedures could be refined to allocate clearer responsibilities.
<b>D. Internal &amp; External Audits</b>	A limited internal audit function is currently available. Internal audit functions need to be upgraded to include certain tasks that are now assigned the

<sup>21</sup> A detailed diagnostic report and recommendations is contained in supplementary document 2 (available upon request).

	<p>supervisory board, yet are more appropriate for internal audit. CGFM needs to establish a separate risk management unit along with associated policies and procedures. Independent external audits of CGFM have been completed for 2012, 2013 and 2014 with satisfactory results. The 2014 audit was completed by the Mongolian National Audit Office that will also prepare the 2015 results. Audits were completed in line with international financial standards.</p>
<b>E. Reporting &amp; Monitoring Mechanisms</b>	<p>Financial statements are prepared on monthly, quarterly and annual basis. As per Articles of Association of CGFM the Board of Directors has to approve annual projected budget and to monitor and to control the performance of the approved budget. Management reporting tools and reports are in need of upgrade to more effectively support financial management. Related to this, the Financial Regulatory Commission does not believe that the control and decision making power of the Governing Board regarding budget planning and other budget matters are sufficient. Nevertheless, the existing reporting system can still be linked with the financial information needs of actual project progress.</p>
<b>F. Information Systems</b>	<p>Financial management system is computerized and produces the necessary financial reports of the ongoing progress reports. Staff is adequately trained to maintain the system and the management organization and processing system safeguard the confidentiality, integrity, and availability of the data. Improvements to the management information system will need to enhance the effectiveness of analytical capabilities and harmonization of data with PFIs, in developing enhanced capability and functionality, and to develop a suite of new portfolio and oversight reports. The systems will need strengthening in line with anticipated growth of the CGFM portfolio and linked management activities.</p>

23. With consideration given to the FMA, in order to support the CGFM's enhancement of capacity and to fully address any weaknesses identified in due diligence, a piggy-back capacity development technical assistance (TA)<sup>22</sup> program is being processed concurrently with the loan. Under the TA it is planned that financial management, operational, governance, and risk management capacity of the CGFM will be enhanced as well as its product set. The legal framework supporting CGFM will be reviewed and relevant amendments will be proposed to strengthen collection and foreclosure, enforceability of guarantees, improved governance, and increased transparency. The roadmap developed during project preparatory TA will be used as a guide to required improvements to the CGFM. The roadmap provides for sequenced improvements.

24. Key actions to be taken by CGFM over the first 2 years of the loan to enhance capacity in financial management will follow the roadmap developed during project preparatory TA as part of due diligence. Specifically, the following tasks will be completed for governance, operations, and financial management through support of the TA:

- (i) Corporate governance practices will be improved to include: (a) Preparation of new corporate governance policies; (b) transfer of relevant supervisory board functions to an internal audit unit; (b) corporate governance training for shareholders, board directors and senior and mid-level managers of the CGFM; and (d) enhancing the strategic plan, marketing plan, human resources plan and a training plan.
- (ii) Risk management, capacity and operational practices will be enhanced to include: (a) expanding credit assessment documentation formats for new products; (b)

<sup>22</sup> Capacity development technical assistance (accessible from the list of linked documents in Appendix 2 of the report and recommendation of the President to the Board of Directors).



developing a statistical credit data base; (c) improving existing credit scoring model; (d) designing a credit committee approval authority system; (e) designing a new credit guarantee manual; (f) developing new credit guarantee policies covering the full credit guarantee cycle; (g) developing sector appetite statements; (h) designing environmental and gender guidelines and screening processes; (i) establishing a work-out unit; (j) producing new job descriptions and work flow charts; (k) developing updated operational risk policies; (l) developing regulatory risk policies; (m) developing an internal CGFM risk grading system; (n) putting in place a program for staff development needs, and (o) enhancing the subrogation procedure.

- (iii) Management information systems and reporting will be improved: (a) harmonizing management information between CGFM and PFIs; (b) expansion of management information system capability and functionality; (c) expanding portfolio and oversight reports; (d) introducing key performance indicators to measure Fund performance; and (e) seeking expressions of interest for information technology and risk management system replacement or enhancement.
- (iv) Financial management practices will be enhanced: (a) developing a new chart of accounts and recommend enhancements, in accordance with international accounting standards, as needed to accommodate the introduction of new products and services; (b) developing reports to extract all needed information to monitor and analyze credit guarantee portfolio and CGFM operational; (c) develop an enhanced annual budgeting process to link to a 5 year strategic plan, including monthly variance analysis; (d) upgrading external reporting for Financial Regulatory Commission regulations, ADB loan covenants and needs of other relevant parties; (e) developing new policies for finance, accounting, balance sheet management; (f) developing a set of key performance indicators; (g) developing profit and cost centers within CGFM; and (h) preparing a capital management plan.

25. Following support from the piggy-back TA, it is anticipated that pre-mitigation risks will be reduced as issues are addressed.

26. **MOF.** MOF currently is and previously has been executing agency on a number of ADB projects and programs. FMAs for ADB funded projects<sup>23</sup> have confirmed MOF as a suitable candidate for executing agency. Due diligence during this project confirms that MOF has adequate capacity for financial management. MOF is familiar with GOM and ADB requirements on disbursement, and social and environmental safeguards. ADB's Anticorruption Policy (1998, as amended to date) was explained to and discussed with MOF.

27. **PFIs.** Due diligence was performed on PFIs<sup>24</sup> according to the due diligence selection criteria.<sup>25</sup> The assessment covered all PFIs that submitted expressions of interest. ADB reviewed the PFIs' credit, operational, and counterparty risks and the measures that they have implemented for monitoring and mitigating these risks.

<sup>23</sup> See also ADB. 2015. *Report and Recommendation of the President to the Board of Directors: Proposed Loan for Additional Financing and Administration of Technical Assistance Grant for Additional Financing Mongolia: Agriculture and Rural Development Project*. Manila (Project 39229-033 forthcoming).

<sup>24</sup> PFIs submitted EOs which were evaluated according to predetermined selection criteria. All PFIs were deemed suitable for further consideration and review through due diligence.

<sup>25</sup> Details are found in supplementary document 3 (available upon request).

28. A final selection of PFIs will be made jointly with CGFM and MOF at project implementation.

29. Measures taken to address gaps in PFIs for social, gender and environmental safeguards will be supported through TA and training provided to CGFM that will back knowledge transfer to PFIs.

30. Time deposit and guarantee agreements between CGFM and PFIs will also be confirmed by ADB. Improvements recommended to PFIs to ensure the sustainability of the project will be addressed indirectly by the piggy-back TA. Through the TA, training will be provided to CGFM that will then support knowledge transfer to PFIs through ongoing outreach.

31. PFIs will conduct financial due diligence for each sub-loan before submitting to CGFM to seek a potential credit guarantee and partial funding. The CGFM will also continue its own financial due diligence for cross-checking and conduct economic due diligence for selected sub-loan projects before making a decision on issuance of a guarantee. Each PFI selected will be required to sign a master guarantee agreement approved by ADB with the CGFM prior to receiving any funds from CGFM for time deposits.

32. CGFM will monitor PFIs to ensure that SME sub-loans will finance activities consistent with ADB's Safeguard Policy Statement (2009 SPS) and other loan qualification criteria, including the extended Prohibited Investment Activities List. Auditing procedures will meet ADB requirements. ADB's Anticorruption Policy (1998, as amended to date) was explained to and discussed with CGFM and the PFIs.

33. **Risk Analysis.** CGFM might face some risks that can generally be divided into three main categories: (i) country level, (ii) entity level, and (iii) project level. The following table summarizes these risks and suggested mitigation measures. Financial management risks shall be updated primarily during the first 2 years of the project through support of the TA. Risk mitigation measures shall also be updated accordingly.

**Table 8: Financial Management Risk Assessment and Mitigation Measures**

<b>Risk</b>	<b>Risk Assessment</b>	<b>Risk Mitigation Measures</b>
<b><i>Inherent Risk</i></b>		
1. <b>Country Specific Risks</b>	M	MOF shall ensure the timely re-lending release of funds to CGFM.
2. <b>Entity-specific Risks</b>	L	MOF is familiar with ADB procurement guidelines and disbursement procedures. ADB will be involved in the recruitment of consultants and training on ADB procedures as needed.
3. <b>Project-specific Risks</b>	M	Close interaction and coordination will occur between ADB the PSC, CGFM and MOF to track project status and address any issues as they occur. This is performed through mid-term and annual reviews on review of regular reporting from the CGFM PIU.
<b>Overall Inherent Risk</b>	M	
<b><i>Control Risk</i></b>		
1. <b>Implementing</b>	M	Organizational capacity building of the CGFM PIU will support the existing organizational structure. The TA will

<b>Entity</b>		also support improvements to risk management and creation of a risk management unit and loan work-out department.
2. <b>Funds Flow</b>	L	Timely availability of funds will be ensured by implementing the proposed funds flow arrangements.
3. <b>Staffing</b>	M	CGFM PIU shall design and implement a program for ADB financial reporting requirements. CGFM PIU staff will be approved by ADB. CGFM has sufficient skilled staff in place and they will be provided with further capacity development through the TA in order to more fully meet requirements.
4. <b>Accounting Policies and Procedures</b>	M	Accounting policy reflects the national accounting standards and the requirements of ADB. Requirements to augment accounting policies and practices to better keep pace with the growth of new products and volume under the project will be addressed through assistance under the TA.
5. <b>Internal Audit</b>	M	Internal auditor skill-sets will be improved by training under the TA. Audit-like functions of the supervisory board will be transferred to an internal audit function.
6. <b>External Audit</b>	L	Audit of project accounts shall be done in accordance with the International Standards on Auditing, by an auditor acceptable to ADB.
7. <b>Reporting and Monitoring</b>	M	MOF and CGFM PIU shall regularly report in accordance with ADB requirements on inherent adequate control mechanisms. Reporting and monitoring mechanisms will be upgraded more fully with the help of consultants specializing in financial management under the TA.
8. <b>Information Systems</b>	M	The efficiency of the existing information system and reporting is adequate for initial needs. The TA will specifically support information system requirements further by assisting CGFM to compile needs and implement solutions in-house or through outside assistance.
<b>Overall Control Risk</b>	M	

H = High, S = Substantial, M = Moderate, N = Negligible or Low.

ADB = Asian Development Bank, CGFM = Credit Guarantee Fund of Mongolia, MOF = Ministry of Finance, PIU = project implementation unit.

## B. Disbursement

34. **Disbursement.** The loan proceeds will be disbursed in accordance with ADB's *Loan Disbursement Handbook* (2015, as amended from time to time).<sup>26</sup> To facilitate project implementation an imprest account in USD will be established at a PFI acceptable to ADB following loan effectiveness by MOF where draw-downs on the ADB loan will be placed. MOF will administer the imprest account. The subaccount and escrow account will be established at PFIs acceptable to ADB by the CGFM to manage re-lending funds received from MOF and for recycling of funds. These accounts will be administered by the CGFM PIU. The CGFM PIU will

<sup>26</sup> An electronic copy was provided to the MOF and CGFM. Available at: <http://www.adb.org/documents/loan-disbursement-handbook>

cause to have audited the subaccount and escrow account and MOF will cause to have audited the imprest account following a method and at a frequency acceptable to ADB. A statement of expenditures procedure will be used by CGFM and MOF to request draw-downs.

35. **Statement of Expenditure.** The statement of expenditure submitted will follow *ADB's Loan Disbursement Handbook* (2015, as amended from time to time). On the statement of expenditure found in appendix 9C sub-loan references will be separated by each PFI reflecting the volume of time deposits placed. Sub-project cost will reflect the gross volume of SME sub-loans that have received guarantees. Sub-loan amount approved will reflect the cumulative guarantee volume to which time deposits will be linked. ADB's disbursement ratio will reflect ADB's co-funding percentage and the sub-loan amount to be financed by ADB will indicate the US dollar volume of the claim to be paid by ADB.

36. **Local currency deposits and co-funding mix.** The MOF will receive the US dollar loan proceeds from ADB and convert to local currency. The total volume of time deposits placed in each PFI will be linked to the level of guarantee issued for eligible SME sub-loans. Only eligible sub-loans that have been issued new guarantee products created by the CGFM and approved by ADB will receive partial funding in the form of time deposits. The time deposits will be funded by a mix of 90% ADB loan proceeds in local currency and 10% funds from the CGFM. Time deposits will be placed in PFIs at maturities equal to the principal amortization schedule of the underlying SME sub-loans in annual maturity increments, either individually or in a pool, that have been issued guarantees by the CGFM to the maximum of the level of guarantee percentage issued. Time deposits will be placed up to 5-year maturity and if the principal amortization schedule for the portfolio of SME Loans reflects tenors longer than five years, then all remaining amortizations beyond five years shall be cumulated into a five-year time deposit and then at the five-year maturity, the time deposits shall be rolled over into new time deposits, using the same method described herein, to cover the remaining portfolio amortization schedule through the final maturity of the portfolio of SME Loans. Co-funding from CGFM for the time deposits will be placed in PFIs at the same terms, rates and conditions as deposits using ADB loan funds. Time deposit agreements will be drafted by CGFM with the assistance of the TA and will ensure that the deposits cannot be pledged, retained or claimed by the PFI should the PFI have a claim for a credit guarantee issued. The content of the time deposit agreements will be confirmed by ADB and cannot be changed without ADB consent.

37. The CGFM PIU will establish a process and documentation, along with the TA consultants, to calculate the appropriate level of deposits to be placed in PFIs and the tenor of those deposits that is acceptable to ADB. The methodology used will generally confirm to the following requirements.

38. On an ongoing basis, PFIs will make eligible SME sub-loans and obtain guarantees from CGFM at various coverage ratios, for various maturities and with various principal amortization schedules. On at least a quarterly basis, a PFI will calculate the sub-loan guarantee portfolio's cumulative principal amortization schedule according to projected monthly maturities. The PFI will then request time deposit funding from the CGFM according to the projected monthly principal amortization schedule for the portfolio of sub-loans made during that set reporting time period. CGFM will place time deposits in the PFI at maturities equal to the portfolio's principal amortization schedule, in yearly increments, but to no more than 5 years tenor. If the principal amortization schedule for the portfolio of SME Loans reflects tenors longer than five years, then all remaining amortizations beyond five years shall be cumulated into a five-year time deposit and then at the five-year maturity, the time deposits shall be rolled over into new time deposits, using the same method described herein, to cover the remaining portfolio amortization schedule

through the final maturity of the portfolio of SME Loans. Time deposits made will combine ADB loan funds and CGFM co-financing according to the funding mix ratio agreed. At the end of each year, as the guaranteed sub-loan portfolio matures or is paid down, the CGFM will rollover or adjust time deposit volumes as required through the remaining life of the guaranteed sub-loan portfolio according to the remaining principal amortization. The cumulative total of time deposits placed should be no more than the cumulative level of guarantees issued to the PFI.

39. **Escrow account and recycling.** ADB loan proceeds will initially be drawn-down to the imprest account based on the estimated time deposits to be placed for the forthcoming 6 months. Loan proceeds are expected to be fully drawn-down over the first 5 years or sooner depending on the speed of issuance of new guarantees. Funds may only be used to place deposits in PFIs by CGFM. ADB funds initially drawn-down by MOF will be converted to MNT and immediately deposit –the funds into a subaccount set up at a PFI approved by ADB in the name of CGFM. The subaccount will be established for the use of CGFM to place time deposits into PFIs. Upon the maturity of time deposits, funds will be repaid to an escrow account held by CGFM at a PFI approved by ADB to hold recycled funds available for new time deposits. Interest earned from the time deposits and from the escrow accounts will be paid directly to the operating bank account used by CGFM. Any interest earned on the Subaccount shall be retained by CGFM.

40. **Conditions for Withdrawal from Loan Account.** No withdrawals shall be made from the Loan Account under Category 1 (Time Deposits for eligible SME Loans) until the following are met:

- (a) an ESMS is established by CGFM acceptable to ADB and CGFM has appointed relevant qualified officers to implement the ESMS;
- (b) the Subsidiary Loan Agreement shall have been duly executed and delivered on behalf of, and shall have become legally binding upon, the Borrower and CGFM; and
- (c) a template Time Deposit Agreement is in place, acceptable to ADB.

41. The minimum value per withdrawal application is \$100,000 equivalent. Individual payment below this amount should be paid by (i) MOF and subsequently claimed to ADB through reimbursement or (ii) through imprest account fund procedure, unless otherwise accepted by ADB.

### **C. Accounting**

42. The MOF will maintain an imprest account at a nominated PFI, and record all disbursement to CGFM on the Project. CGFM will maintain one subaccount for draw-downs from MOF and one escrow account for recycling funds from PFIs. Project accounts will follow international accounting principles and practices.

### **D. Auditing and Disclosure**

43. MOF shall and shall cause CGFM to: (i) maintain separate accounts and records for the Project; (ii) prepare an annual Statement of Utilization of Funds for the Project in accordance with accounting principles acceptable to ADB; (iii) have such consolidated Statement of Utilization of Funds audited annually by independent auditors whose qualifications, experience

and terms of reference are acceptable to ADB, in accordance with international standards for auditing or the national equivalent acceptable to ADB; (iv) as part of each such audit, have the auditors prepare a report (which includes the auditors' opinion on the Statement of Utilization of Funds, use of the Loan proceeds and compliance with the financial covenants of the Loan Agreement as well as on the use of the imprest fund and subaccount, and statement of expenditures) and a management letter (which sets out the deficiencies in the internal control of the Project that were identified in the course of the audit, if any); and (v) furnish to ADB, no later than six months of the end of the fiscal year, copies of such audited Statement of Utilization of Funds, audit report and management letter, all in the English language, and such other information concerning these documents and the audit thereof as ADB shall from time to time reasonably request.

44. CGFM shall: (i) provide its annual consolidated financial statements prepared in accordance with international financial reporting standards which shall be supported by a statement of Time Deposits to be reconciled and confirmed by auditors against the audited Statement Utilization of Funds of the PFIs; (ii) have its consolidated financial statements audited annually by independent auditors whose qualifications, experience and terms of reference are acceptable to ADB, in accordance with international standards for auditing or the national equivalent acceptable to ADB; and (iii) furnish to ADB, through the Borrower, no later than 1 month after approval by the relevant authority, copies of such audited financial statements in English language and such other information concerning these documents and the audit thereof as ADB shall from time to time reasonably request.

45. PFIs shall: (i) have annual financial statements prepared in accordance with International Financial Reporting Standard; (ii) have financial statements audited annually by independent auditors whose qualifications, experience and terms of reference are acceptable to ADB, in accordance with international standards for auditing or the national equivalent acceptable to ADB; and (iii) furnish to ADB, through the Borrower, no later than 1 month of confirmation of their acceptability of the fiscal year to which they relate, copies of such audited financial statements, all in the English language, and such other information concerning these documents and the audit thereof as ADB shall from time to time reasonably request.

46. CGFM and PFIs shall enable ADB's representatives to discuss their financial statements and their financial affairs where they relate to the Project with the auditors appointed by the CGFM and each PFI respectively and each shall authorize and require any representatives of such auditors to participate in any such discussion requested by ADB. Such discussions shall be conducted in the presence of an authorized officer of CGFM and each PFI respectively, unless CGFM or the PFI respectively shall otherwise agree. CGFM and PFIs shall enable ADB's representatives to inspect any qualified SME sub-loan; any qualified SME sub-project, the Goods and Works, and any relevant records and documents.

47. **Other Reporting Requirements.** The MOF will provide ADB with annual reports on project: (i) progress achieved by output as measured through the indicator's performance targets, (ii) key implementation issues and solutions; (iii) updated implementation plan for each next 12 months, and (iv) a project completion report within 6 months of physical completion of the project.

48. The Borrower shall provide or cause CGFM to provide to ADB, on a quarterly basis, Statement of Utilization of Funds provided by the relevant PFIs to show that the Loan is used for the purposes of the Project, including a detailed list of SME Loans issued by each PFI with

breakdown by Loan funds used and CGFM funds used and amount of guarantees received by each PFI for eligible sub-loans.

49. Throughout implementation of the Project, the Borrower shall ensure or cause CGFM to ensure that each PFI provides clear, timely and sufficient information on the performance of the SME Loans as requested by CGFM or ADB.

50. **Disclosure.** Public disclosure of the audited project financial statements, including the auditor's opinion on the project financial statements, will be guided by ADB's Public Communications Policy (2011).<sup>27</sup> After review, ADB will disclose the audited financial statements for the project and the opinion of the auditors on the financial statements no later than 14 days of ADB's confirmation of their acceptability by posting them on the ADB's website. The management letter, additional auditor's opinions, and audited entity financial statements will not be disclosed.<sup>28</sup>

## E. Other Arrangements

51. The Borrower shall ensure or cause CGFM to ensure that the following conditions are met at all times during the Project:

- (a) satisfactory annual results from an independent external audit of the financial condition of CGFM, as determined by ADB;
- (b) the ratio of the outstanding balance of sub-loans to which any guarantees have been issued by CGFM that are 90 days or more past due in proportion to the total outstanding balance of the sub-loans to which any guarantees have been issued shall not exceed 8%;
- (c) CGFM maintains appropriate financial soundness at all times as evidenced by adequate capital, asset quality, liquidity and profitability, and maintenance of financial ratios at levels acceptable to ADB including a current assets to current liabilities ratio of 1.2 times;
- (d) CGFM maintains adequate credit guarantee and risk management policies, operating systems and procedures;
- (e) CGFM maintains compliance with prudential regulations, including exposure limits, maximum leverage of credit guarantees issuance of no more than 20 times and an adequate credit risk loss covering 100% of expected claims;
- (f) CGFM maintains acceptable corporate and financial governance and management practices including, among other things, transparent financial and operational disclosure policies and practices;
- (g) CGFM maintains sound business objectives and strategy and/or plans;

<sup>27</sup> Available at: <http://www.adb.org/documents/pcp-2011?ref=site/disclosure/publications>

<sup>28</sup> This type of information would generally fall under public communications policy exceptions to disclosure. ADB. 2011. *Public Communications Policy*. paras. 97(iv) and/or 97(v).

- (h) CGFM maintains autonomy in guarantee issuance and pricing decisions and assesses guarantee requested by PFIs individually;
- (i) CGFM maintains composition of the board and credit guarantee committee consistent with best practice international standards;
- (j) CGFM shall only accept new capital if its use is unrestricted and shall only acquire external credit guarantee portfolios if the new net composite risk shall not materially impact the financial soundness of CGFM or impair its capacity to meet its financial covenants and conditions of the Subsidiary Loan Agreement; and
- (k) CGFM maintains adequate policies, systems and procedures to assess and monitor the economic, social, and environmental impact of subprojects in accordance with parameters established by ADB for the purposes of the Project.

52. **Re-lending arrangement between MOF and CGFM.** For re-lending the proceeds of the ADB loan to CGFM by MOF, except as ADB may otherwise agree, the terms for relending the proceeds of the Loan in MNT shall include: (i) for the first three years of the Loan, an interest rate only up to of 1% on the balance of the Loan funds disbursed to CGFM in MNT, and after the first three years of the Loan, the Borrower may charge CGFM on the disbursed Loan balance a maximum of the pass-through rate of interest charged by ADB, plus only up to 0.5% and may additionally charge only up to 0.15% on the undisbursed balance of the Loan; and (ii) a repayment tenor consistent with the Loan. The Subsidiary Loan Agreement between MOF and CGFM shall be in form and on terms and conditions acceptable to ADB.

53. **Time deposit and placement rates.** Time deposits placed by CGFM into PFIs will be completed in MNT at rates consistent with the market and in line with government and other development agencies' loan financing programs. The initial rate per annum for maturities up to 5 years will be agreed to by ADB. At year 3 of the ADB loan, the interest rate on the time deposits placed by CGFM will be reassessed based on market conditions, demand and loan utilization and may be adjusted subject to ADB approval. The interest rate on escrow account balances will be at market rates negotiated directly between the CGFM and the PFIs holding the escrow accounts with funds placed on call or at maturity of no more than 1 month. Time deposit and escrow account agreements will be reviewed and confirmed by ADB. The rate that each PFI may mark-up the time deposits received to determine the final cost on the SME sub-loan will be confirmed by ADB with each PFI. No rights or obligations under a Time Deposit Agreement shall be assigned, amended, abrogated or waived nor any modifications or changes to a Time Deposit Agreement shall be made or otherwise agreed to by CGFM without prior consent of ADB and MOF.

54. **New guarantee products.** CGFM, with assistance of the piggy-back TA, will create new guarantee products. Only eligible SME sub-loans that have been issued one of these newly created guarantee products will be eligible to receive partial funding from the ADB loan. Products will be issued using risk-based pricing. New guarantee products will be designed to support the outputs of this project and to ensure compliance with safeguards and poverty, social and gender objectives. New products that will utilize ADB loan funds, and all related agreements and documentation will be confirmed by ADB to ensure they are consistent with the objectives of this project.

55. **Proposed changes to law.** The MOF and CGFM with support of the PSC will propose and support the drafting of amendments to the law on the CGFM and support an enabling



environment for a private credit guarantee system through drafting and proposal of a law and supporting regulations.

56. **PFI Selection.** The PFI selection criteria and process is provided in supplementary document 3, which is available upon request, and includes the English version of the request for EOI letter sent by CGFM to all banks in Mongolia. Attached to the EOI letter are (i) the indicative features of the proposed sub-loans, (ii) PFI selection criteria and process, and (iii) the EOI form which asks potential PFIs various questions.

57. ADB reviewed PFIs' credit, operational, and counterparty risks, and risk mitigation processes. Seven of 10 PFIs reviewed under due diligence meet all eligibility criteria. A final selection of PFIs will be made jointly with CGFM and MOF at project implementation and each selected PFI will be required to sign a master credit guarantee agreement with CGFM acceptable to ADB. PFIs that do not meet all eligibility criteria may still participate if they agree to implement measures to meet criteria in a reasonable time as agreed by ADB. Integrity due diligence on the short-listed potential PFIs will pay careful attention to dealings with related parties and politically exposed persons consistent with the recommendations of the Financial Action Task Force and ADB's Anticorruption Policy. Measures taken to address gaps in PFIs for social, gender and environmental safeguards will be supported through TA and training provided to CGFM that will back knowledge transfer to PFIs. CGFM will monitor PFIs to ensure that SME sub-loans will finance activities consistent with the ESMS selection criteria, ADB's Safeguard Policy Statement (2009 SPS), and other loan qualification criteria, including the extended Prohibited Investment Activities List. Auditing procedures will meet ADB requirements. ADB's Anticorruption Policy (1998, as amended to date) was explained to and discussed with CGFM and the PFIs.

58. **Eligibility Criteria for PFIs at selection.** Each PFI shall comply with the following eligibility criteria at selection: (i) be in satisfactory operation for at least the last 5 years as determined by ADB; (ii) have at least 5 years of experience in SME or microcredit lending as determined by documentation submitted by the PFI; (iii) demonstrate a track record of running a successful SME program as determined by ADB; (iv) have corporate, financial and governance practices acceptable to ADB; (v) have adequate credit and risk management policies and operating systems acceptable to ADB; (vi) have a satisfactory and transparent accounting, management information system and internal audit system as determined by ADB; (vii) have satisfied ADB's integrity, anti-money laundering and counter-financing of terrorism due diligence requirements and put in place anti-money laundering and counter-financing of terrorism controls and measures to implement such controls, in each case acceptable to ADB; (viii) have established ESMS acceptable to ADB and appointed a qualified staff to implement the ESMS for screening prospective Qualified SME Subprojects in accordance with the SPS and the requirements set forth in the PAM to the satisfaction of ADB; and (ix) have obtained relevant approvals for newly created guarantee products from CGFM for SME Loans to be provided to Qualified SME Borrowers for Qualified SME Subprojects and signed the relevant master guarantee agreement, approved by ADB.

59. **Eligibility Criteria for PFIs at selection and at all times.** PFIs shall comply with the following eligibility criteria at all times (including at selection): (i) comply fully with capital adequacy ratios and all other prudential requirements mandated by the agency responsible for banking and financial supervision in Mongolia (currently the Bank of Mongolia), as evidenced by the most recent annual audited financial statements or interim financial statements, public reports or reports issued by the banking and financial supervision in Mongolia, provided that if the requirements set forth here imposes more stringent requirements, such more stringent

requirements shall apply; (ii) have a ratio of non-performing loans (NPLs) less than 8% of the total loan portfolio (for the purposes of the foregoing, NPLs means loans overdue by 90 days or more), as evidenced by its most recent annual audited financial statement or interim financial statements, in which case, a certification must also be provided by a PFI to CGFM certifying compliance with this eligibility criteria; (iii) be profitable for its most recently completed fiscal year (for the purposes of the foregoing, profitability refers to operating profit after tax), as evidenced by the most recent annual audited financial statements; and (iv) have its financial accounts audited by an external auditor annually and the results are satisfactory as determined by ADB, as evidenced by the most recent annual audited financial statements.

60. PFIs that do not meet all eligibility criteria, whether quantitative or qualitative, may still participate if they agree to implement measures to meet criteria in a reasonable time as agreed by ADB. PFIs may achieve full compliance within 12 months of selection regarding the following criteria: (i) complying with capital adequacy ratios and all other prudential requirements of the banking supervisor in Mongolia as evidenced by the most recent annual or interim audited financial statement, public reports or reports issued by the banking supervisor; (ii) having a ratio of non-performing loans less than 8% of the total loan portfolio; (iii) being in satisfactory operation for at least the last 5 years as determined by ADB; (iv) having at least 5 years' experience in SME or microcredit lending as determined by PFI documentation submitted; (v) being profitable for the most recent completed fiscal year; (vi) demonstrating capacity to run a successful SME program and reach appropriate scale acceptable to ADB within 12 months; (vii) having financial accounts audited annually by an external auditor with results satisfactory to ADB; (viii) having corporate, financial and governance practices acceptable to ADB; (ix) having adequate credit and risk management policies and systems acceptable to ADB; (x) maintaining satisfactory and transparent accounting, management information system and internal audit as determined by ADB; and (xi) providing clear, timely and sufficient information of SME sub-loan performance throughout the project.

61. If a PFI does not come into full compliance with all of the PFI eligibility criteria provided here above within 12 months of signing the relevant master guarantee agreement with CGFM, it shall not be permitted to continue to participate under the Project and the Borrower shall cause CGFM to promptly notify ADB and exercise its rights under the relevant agreements in consultation with ADB.

62. **Monitoring of Eligibility Criteria of PFIs.** The Borrower shall cause CGFM to monitor each PFI's compliance with the eligibility criteria set out in paragraph 60 of the PAM. For eligibility criteria provided in paragraph 60 (i) and (ii), submit quarterly reports to ADB on the status of compliance and for eligibility criteria provided in paragraph 60 (iii) and (iv), submit annual reports to ADB on the status of compliance. Upon becoming aware of any non-compliance by any PFI of any of the eligibility criteria set out here above, the Borrower shall cause CGFM to promptly notify ADB and exercise its rights under the relevant agreements in consultation with ADB.

63. **SME Sub-loans.** CGFM will cause each PFI to: (i) bear the unguaranteed credit risk associated with each SME Loan made by it to a Qualified SME Borrower; (ii) independently determine the creditworthiness of each qualified SME borrower and the terms and conditions of the related SME loans, in accordance with international best practices for lending to SMEs (including determination of margins and associated fees, security taken and proper legal documentation); (iii) ensure that qualified SME subprojects will not be used for activities that are

included in the extended prohibited investment activities list;<sup>29</sup> (iv) ensure that qualified SME subprojects will screen out category A projects for environment and category B and A projects for resettlement and indigenous peoples according to SPS (2009) criteria. ADB's Safeguard Policy Statement (2009); (vi) ensure that qualified SME subprojects will not be used for activities that are not in compliance with the applicable laws and regulation of Mongolia; (vii) ensure that each PFI has appointed designated staff for project implementation particularly for financial management and reporting and monitoring and evaluation; (viii) ensure that each PFI has environmental and social assessment processes to screen and categorize the significance of potential environmental, indigenous peoples or involuntary resettlement impacts associated with subprojects; and ensure each SME sub-loan is denominated in MNT. Sub-loan agreements for SME loans will be confirmed as acceptable to ADB.

**64. Eligibility Criteria for Qualified SME Borrowers.** A qualified SME borrower will: (i) be an SME according to the definition stipulated in the Law on SMEs of 2007; (ii) not be engaged in any prohibited investment activities; (iii) utilize CGFM's newly created guarantee products; and (iv) be in compliance with applicable laws and regulations of Mongolia; and (v) meets appropriate credit and other risk related criteria as determined and applied by the PFI and CGFM. Qualified SME sub-loans and sub-projects will: (i) utilize CGFM's newly created guarantee products; (ii) not be used for activities included in the prohibited investment activities list; (iii) not be used for activities that have any involuntary resettlement and indigenous peoples impact and any significant environmental impacts in accordance with ADB's SPS; and (iv) be used only for activities that comply with applicable laws and regulation of Mongolia.

**65. Qualified SME Subprojects (Screening, Categorization and Environmental and Social Assessment and Planning).** Before any proposed subproject is approved as a Qualified SME Subproject for financing, the Borrower shall cause CGFM to ensure that: (i) each PFI has appointed adequate number of qualified staff for the Project implementation particularly for financial management, reporting and evaluation; (ii) the ESMS is used to screen and categorize the significance of potential environmental, indigenous peoples or involuntary settlement impacts associated with such subproject; and (iii) an EMP is prepared for the proposed subprojects as required pursuant to the ESMS.

**66. CGFM agreements with PFIs.** Agreements covering credit guarantee processes, requirements for and collection of additional collateral, and claim procedures will be amended to conform to international best practices with assistance of the TA. These agreements and processes will be confirmed by ADB for use with new credit guarantee products.

**67. Restrictions on Distribution of Excess Funds by CGFM.** The Borrower shall ensure or cause CGFM to ensure that that no distribution of excess operating revenues net of expenses or equity shall be made to any founder or member of CGFM unless:

- (a) the co-funding ratio between ADB and CGFM can be met for the remaining life of the Loan (which requires that the total Time Deposits shall be funded at an agreed ratio of 90% funded by the Loan and 10% funded by CGFM funds);
- (b) the level of non-performing loans ("NPLs") remains below 3% of the total loan guarantee portfolio (for the purposes of the foregoing, NPLs means loans overdue by 90 days or more);

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<sup>29</sup> Supplementary document 1 (available upon request).

- (c) the maximum leverage of credit guarantee issued by CGFM does not exceed 10x;
- (d) expected claims on credit guarantee issuance remains covered at 100%;
- (e) CGFM has surplus during the prior fiscal year and is anticipated to have surplus in the next fiscal year (surplus refers to operating revenue minus expenses and any tax); and
- (f) CGFM will remain in sound financial condition capable to meet the terms and conditions of the Subsidiary Loan Agreement.

## VI. PROCUREMENT AND CONSULTING SERVICES

68. There will be no procurement under the ADB loan and no procurement will be undertaken by CGFM or PFIs. A piggy-backed capacity development TA of \$0.8 million<sup>30</sup> will provide assistance to CGFM and will involve consulting services.

69. **Procurement of Works and Goods under the Subprojects.** Qualified SME Borrowers undertakes procurement of Goods and Works with due attention to economy and efficiency and in accordance with established private sector or commercial practices within the framework of Mongolian laws and regulations. SME procurement of works and goods for the SME subprojects will meet ADB member country procurement eligibility. This requirement shall be deemed to be met so long as a Qualified SME Borrower will have acquired Goods and Works from ADB member countries, in an amount equal to or larger than the SME Loan for a Qualified SME Subproject given that funds are fungible.

70. The project will not require advance contracting or retroactive financing.

### A. Procurement of Consulting Services under the TA

71. The proposed TA is being processed at the request of GOM in support of the Project. The MOF is the executing agency and the CGFM is the implementing agency for the proposed ADB loan and for the TA. The TA will accompany the loan and support the implementation of the project. It will be implemented over 2 years, from loan effectiveness.

72. A firm will be recruited to support Output 3 under the TA according to ADB's *Guidelines on the Use of Consultants* (2013, as amended from time to time). The terms of reference for all consultants are detailed in Section B.

73. **Quality of CGFM and the credit guarantee system improved.** The quality of CGFM and the credit guarantee system will be improved under the TA during the initial 2 years of the loan. The operational, governance, and risk management capacity of CGFM will be enhanced as will its product set. The credit guarantee system legal and regulatory framework will be enriched to support an enabling environment for a private credit guarantee system by drafting law and regulations. CGFM's legal framework will be reviewed to strengthen collection and foreclosure, enforceability of guarantees, governance, operations, risk management, and transparency. Project arrangements will consider the current and planned activities of other donor agencies.<sup>31</sup> This program will utilize the roadmap created by the project preparatory TA.<sup>32</sup>

### B. Consultant's Terms of Reference

74. **Credit Guarantee Specialist (International, 7.5 person-months).** The consultant will have at least 10 years' experience in credit guarantee systems and experience dealing with small and medium-sized enterprise (SME) finance in advanced and also developing countries. The consultant will hold a minimum of a bachelor's degree in finance, economics or a related field applicable to this position. The consultant will be the team leader and lead the TA and be

<sup>30</sup> ADB grant funding (TASF-V) under P48015-003.

<sup>31</sup> Since 2012, the Japan International Cooperation Agency (JICA) has implemented a Two-Step Loan Project providing lending and capacity development to PFIs supporting SMEs. JICA also supports CGFM through regular training sessions and the proposed placement of a volunteer credit guarantee expert in July 2016.

<sup>32</sup> The Asian Development Bank provided project preparatory technical assistance for Mongolia: Supporting the Credit Guarantee System for Economic Diversification and Employment Project (48015-001).

responsible to assist the CGFM to improve operating procedures, risk management, portfolio management, transparency practices, governance structure, marketing, development of new products, and staff development. The consultant should be prepared to implement methods to support gender and social safeguards within new products and processes of the CGFM. The consultant will help to ensure that new product development and outreach will be structured to support achieving the outcomes and outputs of the project including meeting gender, regional distribution, and economic diversification and employment goals through outreach, marketing and product development. The consultant will also prepare draft text and documentation to include operating procedures, marketing programs, training material, and new product material and other documents as needed to assist the CGFM.

**75. Credit Risk Management Specialist (International, 6.5 person-months).** The consultant will have at least 10 years' experience in credit risk management, measurement, underwriting, collection, and collateral resolution processes working in advanced and also developing countries. The consultant will have practical knowledge of best practices in credit guarantee systems globally. The consultant will hold a minimum of a bachelor's degree in finance, economics, or a related field applicable to this position. The consultant will be responsible to assist the CGFM to improve credit guarantee underwriting, portfolio risk management, non-performing loan control, collateral management, and collection practices. The consultant will prepare other text to include operating procedures, training material, underwriting procedures and other documentation as needed.

**76. Financial Management & Accounting Specialist (International, 3 person-months).** The consultant will have at least 10 years' experience in financial management and expertise internationally in credit guarantee systems' asset liability management and accounting processes. The consultant will have practical knowledge of best practices in credit guarantee systems globally and experience in developing countries. The consultant will hold a minimum of a bachelor's degree in finance, accounting, or a related field applicable to this position. The consultant should also hold a relevant professional certification in accountancy or finance qualification such as a CPA, CA, or CFA. The consultant will assess financial management processes and recommend policy including asset liability management policy, investment policy, and accounting policy and principles. The consultant will also prepare other draft text, documents, and training material as needed to assist the CGFM.

**77. Credit Guarantee Specialist (National, 8.5 person-months).** The consultant will have at least 5 years' experience in dealing with SME finance and credit guarantee systems. Experience internationally would be an advantage. The consultant will hold a minimum of a bachelor's degree in finance, economics or a related field applicable to this position. The consultant will be responsible to assist the CGFM to improve operating procedures, financial management, risk management, portfolio management, transparency practices, governance structure, marketing, development of new products, and staff development. The consultant will lead in managing workshops and training. The consultant will also prepare other draft text, documents, and training material as needed. The consultant will support translation and interpretation for the international consultant.

**78. Environmental Safeguards Specialist (National, 5 person-months).** The consultant will have at least 5 years' experience in environmental safeguards and have familiarity with ADB Safeguard Policy for Environment (2009). The consultant will hold a minimum of a bachelor's degree in an applied environmental science or have applicable work experience. Experience internationally would be an advantage. The consultant will work with the CGFM, the Mongolian Banker's Association and selected participating financial institutions to provide training, outreach

and guidance to ensure that the Environmental and Social Management System Arrangement can be properly implemented. The consultant will lead in managing workshops and training. The consultant will help CGFM establish a monitoring mechanism for environmental safeguards and establish loan safeguard and ESMS performance indicators to be used by CGFM and PFIs during loan implementation. The consultant will also prepare other draft text, documents, and training material as needed.

**79. Financial Management & Accounting Specialist (National, 4 person-months).** The consultant will have at least 5 years' experience in financial management or accounting. The consultant will hold a minimum of a bachelor's degree in finance, accounting, or a related field applicable to this position. The consultant will work with the international consultant on financial management to implement improvements at CGFM according to the due diligence performed during loan processing and as outlined in the roadmap of the CGFM. The consultant will assess financial management processes and recommend policy including asset liability management policy, investment policy, and accounting policy and principles. The consultant will also prepare other draft text, documents, and training material as needed. The consultant will support translation and interpretation for the international consultant.

**80. IT System Specialist for Financial Risk Management (National, 4 person-months).** The consultant will have at least 5 years' experience in IT systems for risk management and portfolio management within financial institutions and have knowledge about the management information system needs of credit guarantee funds internationally. Experience internationally would also be an advantage. The consultant will hold a minimum of a bachelor's degree in computer science, programming or a related field applicable to this position. The consultant will assist the CGFM in identifying their risk management system needs and limitations, including needs for gender disaggregated data, drafting terms of reference to solicit offers for systems' upgrade or replacement, and assisting in offer evaluations. The consultant will also prepare other draft text, including request for expressions of interest, and training material as needed.

**81. Legal Specialist for Credit Guarantee and SME Finance (International, 2.5 person-months).** The consultant will have at least 10 years' experience internationally in legal issues related to SME financing, credit guarantees and credit collection processes. The consultant will hold a minimum of a bachelor's degree in law or hold sufficient work experience applicable to the topic. The consultant will be responsible to assist the CGFM to review and draft new guarantee issuance documentation, time deposit agreements, association agreements with PFIs and other related documents. Along with the national specialist, the consultant will also be responsible to provide written input into amendments to the Law on the CGFM, and propose new text for law and regulation to support a private credit guarantee system in Mongolia. The consultant will produce an inception report within 1 week of start-up, interim report within 10 weeks of start-up, draft final report 2 months of project end, and a final report within 1 month of project end.

**82. Legal Specialist for Credit Guarantee and SME Finance (National, 3.5 person-months).** The consultant will have at least 7 years' experience in legal issues related to SME financing, credit guarantees and credit collection processes. Experience internationally would be an advantage. The consultant will hold a minimum of a bachelor's degree in law or hold sufficient work experience applicable to the topic. The consultant will be responsible to work with the international specialist and assist the CGFM to review and draft new guarantee issuance documentation, time deposit agreements, association agreements with PFIs and other related documents. The consultant will advise on legal aspects of non-performing loan control, collateral management, and collection practices. The consultant will also be responsible to

provide written input into amendments to the Law on the CGFM, and propose new text for law and regulation to support a private credit guarantee system in Mongolia. The consultant will also prepare other draft legal text, documents, and procedures as needed. The consultant will support translation and interpretation for the international consultant.

**83. Social and Gender Development Specialist (National, 3 person-months).** The consultant will have at least 5 years' experience in social development and design of programs for financial inclusion. The consultant will hold a minimum of a bachelor's degree in an applied social science or have applicable work experience. Experience internationally would be an advantage. The consultant will work with the CGFM and selected participating financial institutions to provide training, outreach and promotion of the social and gender outputs of the project. The consultant will help CGFM establish a monitoring mechanism for social safeguards and gender impacts. The consultant will lead in managing workshops and training. The progression of tasks will essentially first require proposed actions are reviewed, followed by CGFM PIU and PFI staff training, and then establishing an implementation and reporting system. The consultant will also assess progress, suggest improvements where needed and assist with reporting. A thorough project progress evaluation will also be performed at the end of the TA. The consultant will also prepare other draft text and training material as needed.

**84. Credit Risk Management Specialist (National, 7.5 person-months).** The consultant will have at least 5 years' experience in credit risk management, measurement, underwriting, collection, and collateral resolution processes. Experience internationally would be an advantage. The consultant will hold a minimum of a bachelor's degree in finance, economics, or a related field applicable to this position. The consultant will be responsible to assist the CGFM to improve credit guarantee underwriting, portfolio risk management, non-performing loan control, collateral management, and collection practices. The consultant will work with the international specialist to prepare other text to include operating procedures, training material, underwriting procedures and other documentation as needed. The consultant will support translation and interpretation for the international consultant.

## VII. SAFEGUARDS

**85.** Safeguard due diligence was performed to assess potential environmental and social impacts and risks associated with the PFIs' existing and likely future portfolios as well as their commitment and capacity for environmental and social management as per paragraph 55 of Operations Manual Section F1. The project is in compliance with information disclosure and consultation requirements in line with paragraph 22 of Operations Manual F1. ADB will work closely with CGFM, MOF and PFIs to ensure that the SME sub-loans will comply with ADB's SPS, Mongolia's labor, environmental, health, safety, and social laws and regulations and the prohibited investment activities list attached to loan and project agreement.

**86.** Pursuant to ADB's Safeguard Policy Statement (2009) (SPS),<sup>33</sup> ADB funds may not be applied to the activities described on the ADB Prohibited Investment Activities List set forth in Appendix 5 of the SPS and the prohibited investment list attached to the loan and project agreements and found in supplementary document 1. All financial institutions must ensure that their investments are in compliance with applicable national laws and regulations and will apply the extended prohibited investment activities list<sup>34</sup> to sub-projects financed by ADB.

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<sup>33</sup> Available at: <http://www.adb.org/documents/safeguard-policy-statement>.

<sup>34</sup> Supplementary document 1.



87. **Environment.** The project is classified FI and treated as B. The project confirmed mainly positive environmental benefits as SMEs in non-mining sectors are supported diversifying the economy and reducing mining-related environmental impacts. An ESMS<sup>35</sup> was prepared for PFIs that includes elements of an environmental assessment review framework (EARF) to provide guidance to the PFIs to conduct due diligence on sub-projects as per requirements of Mongolia's laws on environmental protection and EIA, and ADB's. The screening procedures in the ESMS include a brief climate risk assessment that will be applied to every sub-project. Based on the proposed sector loan activities, no significant adverse environmental impacts are expected, and climate risk is considered low. The potential impacts of the Category B projects will be mitigated through implementation and monitoring prescribed by generic environmental management plans agreed upon as part of sub-loan approval.

88. The ESMS developed for the PFIs will also provide guidance to the national consultants who will be outsourced by the PFIs and SMEs to conduct the initial environmental examination (IEE) for the B-level projects. An IEE will include preparation of an environmental management plan (EMP). The ESMS will screen out Category A projects for environment and Category B and A projects for resettlement and indigenous peoples from CGFM support according to SPS (2009) criteria. All Category C projects will be subject to the Mongolia EIA law environmental due diligence requirements of the government as overseen by the Ministry of Environment and Green Development (MOEGD). Sensitive category C subprojects may require a simplified EMP and grievance redress mechanism (GRM). The ADB prohibited investment list<sup>36</sup> will be applied to all project loan applications.

89. With initial input from the International Finance Corporation (IFC) (Environment, Safety, and Health Guidelines 2007), the Mongolian Banker's Association (MBA) in 2014 initiated their Sustainable Finance Program (SFP) with the financial institutions which together have begun developing a simple generic financial institution-wide environmental and social management framework which the individual financial institutions apply according to their own organizational structures and imperatives. The MOEGD has also been directly involved with the MBA's SFP. Some financial institutions such as the Xac Bank, Khaan Bank, and National Investment Bank of Mongolia reported comparatively advanced ESMSs already in place as a result of early support from other donor assistance such as the Millennium Challenge Account -USA, The Netherlands Development Finance Company, JICA Two Step Loan Project, and IFC, as well support from international auditing firms such as Price Waterhouse Coopers. Notable is that these financial institutions have guiding policies and principles for environmental safeguards. However, the CGFM currently does not have any form of ESMS in place.

90. The ESMS for the project is developed to align with the emerging Sustainable Finance Program (SFP) that the MBA initiated for the PFIs which is based on the national environmental and social safeguard requirements of the government (MOEGD). For consistency the ESMS will also reside in the CGFM. The ESMS prescribes standard elements including policy and guiding principle statements, environmental and social safeguards as part of the PFI's risk assessment program and department, staff training to implement their policies and be able to address borrower due diligence, monitoring and reporting for government and periodically ADB, and loan agreements that specify required level of environmental and social impact assessment to meet the loan covenants of the government and the ADB's SPS (2009).

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<sup>35</sup> See linked document 12.

<sup>36</sup> See supplementary document 1 (available upon request).

91. The ESMS initially has been applied by the PFIs at two levels or tiers depending on the current abilities of the PFIs for overseeing the environmental and social due diligence of subprojects that are category B for environment. After initial training on the ESMS from the loan implementation TA the more experienced and skilled PFIs will use the ESMS to oversee the due diligence of category B and C subprojects. Until demonstrating sufficient understanding and hands-on experience the less experienced PFIs will only process category C subprojects for environment with the ESMS.

92. **Social Safeguards.** An SME survey, consultations with stakeholders, and workshops and focus groups held contributed to the results of the social safeguards (including gender) due diligence.

93. The project is classified FI and treated as C for Involuntary Resettlement and for Indigenous Peoples, in line with ADB's SPS. Project activities will not likely result in any direct or indirect impacts on ethnic minority communities and will not require involuntary land acquisition or displacement. An ESMS process will screen out category A and B projects for resettlement and indigenous peoples according to SPS (2009) criteria. ADB's Safeguard Policy Statement (2009); SMEs financed will be representative of all regions in Mongolia.

94. The CGFM and MOF have assured ADB that implementation of the Project shall conform to all applicable ADB policies concerning social safeguards.

95. **Consultation and public disclosure.** In accordance with ADB's SPS (2009), and as specified in the ESMS the PFIs must ensure their borrowers conduct consultations with affected people and other concerned stakeholders, including civil society, women, and facilitate their informed participation. The consultation process shall also be used to introduce and discuss the project GRM. Following ADB's guidelines, at least one public consultation is required for category B projects during IEE preparation. The IEE shall document details of the public consultation by providing details of the environmental issues and concerns raised by stakeholders and by indicating how these will be addressed in the project design and mitigation measures. Proof of consultations such as attendance sheets, minutes of meetings and pictures shall be included in the documentation.

96. The PFIs and the CGFM are responsible for ensuring that all environmental and social assessment documents and environmental and social monitoring reports are properly and systematically kept as part of the record of a loan and project implementation by the borrower. The PFI and CGFM shall make these documents available in a form, language, and at a location in which they can be easily accessed by all stakeholders including affected people. The IEE reports will be prepared and submitted by the CGFM PIU and submitted on an annual basis shall be posted on ADB's website.

97. **Grievance redress mechanism for qualified SME sub-projects.** Prior to the first SME loan guarantee, the CGFM shall establish a GRM to deal with complaints about each Qualified SME Subproject's environmental and social concerns in accordance with the ESMS. Specifically, the CGFM will establish a public complaints unit (PCU) prior to the first sub-loan guarantee being issued to deal with complaints from affected people throughout implementation of the subproject. The PCU must include an offsite representative of each PFI. It is recommended that the environmental and social safeguard officer of CGFM PIU and PFIs represent the PCU/PFI. The PCU should be continued in both organizations after loan implementation TA is completed. The CGFM PIU will be responsible for the initial set-up of PCU and the coordination of the GRM at the local levels and will staff the PCU. The

environmental and social safeguard officer of the PCU and PFIs will be the key contact points for *Soum* representatives who may require information about the subproject or who have an issue they would like to discuss. The GRM will address affected people's concerns and complaints promptly, using an understandable and transparent process that is gender responsive, culturally appropriate, and readily accessible to all segments of the affected people at no costs and without retribution. The GRM will not impede access to Mongolia's judicial or administrative remedies. The GRM will be introduced by the SME borrower and PFI during consultation with community and made publicly available and accessible to the affected people prior and during to sub-project implementation. The GRM will serve category B sub-projects, and category C sub-projects where necessary. CGFM will ensure that each PFI includes in the relevant SME Loan Agreement a requirement that each qualified SME Borrower will refer affected people's concerns, complaints and grievances about each qualified SME Subproject's environmental and social concerns to the PFI or the public complaints unit under the GRM and implement any redress solution as further described in the ESMS.

98. **Institutional arrangements and responsibilities.** The MOF is the executing agency of the project. The CGFM will act as the implementing agency, and will establish a PIU. The PFIs will effectively implement the outputs of the project through the CGFM. The CGFM PIU will oversee all the work, and have the responsibility to ensure the ESMS is applied by the PFIs for compliance with safeguard requirements. The CGFM shall appoint an environment and social safeguard specialist as part of the PIU. The CGFM will also appoint a public complaints unit to oversee the implementation of the GRM. The public complaints unit will have an offsite representative of each PFI. PFIs shall appoint an environment safeguard specialist, if not yet available, per the ESMS; and ahead of the first loan disbursement.

99. Independent national environment specialists or institutes shall be available to the SME loan borrowers to conduct the required environmental and social due diligence on sub-loan applications unless the SME borrower has qualified staff to do the required safeguard work to satisfy government and ADB requirements. The generic terms of reference for the outsourced consultant support is included in the ESMS. The responsibilities of the PFIs and CGFM in conducting the required environmental and social due diligence specified in the ESMS is as follows: (i) classify sub-loan applications by completing a rapid environmental assessment (REA) using ADB REA checklists to determine subproject category (Category B or C). Category A sub-projects and sub-projects on the ADB Prohibited Investment Activities List will be rejected; (ii) if a Category B application is received, conduct environmental assessment and prepare IEE report in compliance with the requirements of National legislation and ADB's SPS (2009); (iii) ensure that SME borrower and consultant holds meaningful consultation with affected people and other stakeholders in accordance with ADB's SPS (2009); (iv) for each IEE ensure SME borrowers develop an SPS-responsive EMP which is submitted to the PFI; (v) ensure SME borrower and consultant implements environmental monitoring in accordance with the approved EMP; (vi) screens for impact on indigenous people or resettlement and categorizes any impacts; and (vii) monitors environmental performance of project with regular reports to the PFI and CGFM. PFIs are responsible for obtaining domestic EIA approvals.

100. CGFM and their consultants will be responsible for development, implementation, monitoring, and reporting of ADB loan project. CGFM shall establish a PIU which includes a person in charge of environmental, safety, and health. The PFI will oversee the successful safeguard work of the SME borrower. If a PFI lacks sufficient expertise and capacity to ensure adequate environmental and social management of their SME loan sub-projects, the MBA should organize institutional strengthening, environmental management, and capacity development of the PFI and CGFM. The CGFM PIU will organize required capacity

development training with the assistance of the MBA for the PFIs. The MOEGD will be responsible to oversee Mongolian EIA safeguard compliance with the Law on Environmental Assessment (2012). The IEEs will be publicly disclosed in Mongolian by the PFIs on their websites, and in English on the ADB website.

101. **Prohibited Investment Activities.** Pursuant to ADB's SPS (2009) ADB funds may not be applied to the activities described on the ADB Prohibited Investment Activities List set forth in Appendix 5 of ADB's SPS (2009) and as in the expanded list of prohibited investment activities list attached to the loan and project agreement. All PFIs will ensure that their investments are in compliance with applicable national laws and regulations, and will exclude any or all ADB prohibited investment activities.

102. A number of other activities and sectors specific to the conditions of the loan for this project have been added to the abovementioned list.

### VIII. GENDER AND SOCIAL DIMENSIONS

103. **Socioeconomic Impact.** While the project will not have a direct impact on income growth and poverty reduction in the country, the indirect impacts on the living standards, well-being of the local population, and job creation will be significant. The expected economic, social and gender impacts of the proposed project will include the following.

104. The impact of the proposed project will be increased contribution of SMEs to economic diversification and creation of new and support existing jobs. There will be indirect impact on the levels of employment in the project area. This impact will be in the form of expanded opportunities for employment and self-employment, as well as SME business development.

105. Implementation of the proposed project in Mongolia will significantly improve access of SMEs to the financial resources and thus will support further development of the businesses both in urban and rural areas. The project will enhance the capacity of private undertakings in production and service provision, and will lead to increases in the volume, quality and competitiveness of their products and services. This will indirectly promote the increase and stabilization of income received by employees of these enterprises.

106. The credit guarantee scheme will broaden opportunities for SMEs that, due to lack of collateral, were not able to access commercial bank loans. This in turn will help SMEs to build up credit history with the banks, which is important for future business activities with the financial institutions. Longer-term loans made available to the SMEs will allow them to secure long-term investments in machinery and equipment, as well as projects on expanding business and increasing the efficiency of production.

107. Provision of trainings and capacity building for men and women entrepreneurs will increase understanding and improve business related skills, as well as improve chances for successful applications for commercial bank loans.

108. During project preparation, an SME survey and consultations with the stakeholders were undertaken to collect impact data and raise awareness about the project. The project design is based on provision of the financial intermediation loan to the CGFM to enable selected PFIs to make new longer-term and investment loans, with no special measures for the poor or vulnerable. The latter will be done through public awareness and capacity building activities.

109. **Gender.** As the project outcome is likely to directly improve men and women's access to commercial bank loans and indirectly improve employment opportunities for women in the SME sector, the proposed gender category for the project is Some Gender Elements.

110. The PSC and CGFM PIU will ensure that the principles of gender equity aimed at increasing Project benefits and impacts on women are consistent with ADB's Policy on Gender and Development (1998) and are followed during implementation of the project. These principles include: (i) equal pay to men and women for work of equal value, (ii) enabling working conditions for women workers and (iii) taking necessary actions to encourage women living in the project area to participate in the design and implementation of project activities.

111. **Gender Impact.** Improved access of male and female led SMEs to commercial banks loans will be secured through the target indicators on the percentage of the loan accounts opened for women (at least 50%) and men businesses during the project implementation. The ultimate goal of the project is not only improve access to the financial resources for SMEs, but to develop a good ground for the increased employment opportunities for women, especially in the rural areas. This will be achieved through the targeting on financing SMEs investment project that anticipate increase in employment.

112. The project will promote gender equality in workplace both in CGFM and PFIs, consistent with national legislation and the Mongolia Gender Equality Law (2011). CGFM will ensure that the principles of gender equity aimed at increasing Project benefits and impacts on women area consistent with ADB's Policy on Gender and Development (1998) are followed during implementation of the Project, including (i) equal pay to men and women for work of equal value; (ii) enabling working conditions for women workers; and (iii) taking necessary actions to encourage women living in the Project area to participate in the design and implementation of project activities.

113. The CGFM PIU will have a social and gender focal point to assist in gender analysis and support outreach and transfer of knowledge to PFIs. The training will be provided to the front-line officers of the PFIs and CGFM on gender sensitivity in working with potential clients. The upgrade of systems and training to gather and analyze gender disaggregated data for decision making will be required of PFIs and CGFM.

## IX. PERFORMANCE MONITORING, EVALUATION, REPORTING AND COMMUNICATION

### A. Project Design and Monitoring Framework

**Impacts the Project is aligned with:**

 Job creation in non-mining related sectors increased (SME Development Program 2014-2016)<sup>a</sup>

Project Results Chain	Performance Indicators with Targets and Baselines	Data Sources and Reporting	Risks
<b>Outcome</b>  SMEs' access to finance expanded	By 2021  a. Mix of rural vs. urban area SME loan accounts opened increases to 20% (Baseline 2011: 17.3%) b. SME loan accounts opened by women SMEs account for half of total SME loan accounts opened. <sup>b</sup> (Baseline 2014: 46%) c. Number of active enterprises with fewer than 50 employees increase at a 10% annual average rate during 2016-2022 (Baseline 2014: 8.8% average annual rate of increase from 2006 to 2014)	a. Global Financial Inclusion Database (World Bank: Annual) b. PFI reports  c. Global Financial Inclusion Database (World Bank: Annual) and Mongolian Year Book (NSO: Annual)	Instability of the economy negatively affects the willingness of financial institutions to make loans to SMEs
<b>Outputs</b>  1. Longer-term financing for SMEs increased	1a. At least three new credit guarantee products are issued by CGFM with at least one supporting women entrepreneurs by end of 2018. (Baseline 2014: 0 new product) 1b. At least \$58.63 million of funding is channeled to PFIs utilizing CGFM guarantees by end of 2026. (Baseline 2015: 0)	1a. Project monitoring reports; CGFM reports  1b. Project monitoring reports; CGFM, PFIs, and MOF reports	Amendments and establishment of relevant laws and regulations delayed.
2. A longer-term bank deposit market developed	2a. At least 4 PFIs participating in the CGFM program regularly offer time deposits of at least 5-years maturity in MNT by 2026. (Baseline 2015: 0)	2a. Project monitoring reports; CGFM, PFIs, and MOF reports	

<p>3. Quality of CGFM and the credit guarantee system improved<sup>c</sup></p>	<p>3a. Two new procedures on risk management and financial management adopted and implemented by CGFM by end of 2017. (Baseline 2015: 2 old procedures)</p> <p>3b. Amendments are adopted for enhancement of the legal framework supporting the credit guarantee system, including support for a private guarantee system by end of 2016. (Baseline 2015: 0)</p> <p>3c. CGFM marketing program and action plan drafted and implemented jointly with regional CGFM representatives and PFIs by end of 2017. (Baseline 2015: none)</p> <p>3d. Management Information system of CGFM allows collecting, reporting and analyzing of gender disaggregated data on the number of guarantees and loans issued, types and sizes of loans, and repayment status of loans by end of 2017. (Baseline 2015: no data)</p>	<p>3a. Project monitoring reports; CGFM, MOF, and MOI reports</p> <p>3b. Project monitoring reports; CGFM, MOF, and MOI reports</p> <p>3c. Project monitoring report CGFM</p> <p>3d. Project monitoring report CGFM</p>	
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### Key Activities with Milestones

#### 1. Longer-term financing for SMEs increased

- 1.1 Prepare new credit guarantee service agreements to be signed between CGFM and PFIs by end of 2016.
- 1.2 Hold training for CGFM and PFIs' staff in financial and safeguard, gender and labor issues by end of 2016.
- 1.3 Establish and implement ESMS for screening sub-projects by end of 2016.
- 1.4 Design new marketing program for CGFM products and services to SMEs with emphasis on areas outside of the capital by end of 2017.
- 1.5 Create new guarantee products tailored to needs of men and women entrepreneurs and SMEs outside the capital by end of 2018.

#### 2. A longer-term bank deposit market developed

- 2.1 Draft new time deposit agreements between CGFM and PFIs for placement of funds into PFIs by end of 2016.
- 2.2 Place first time deposits in PFIs by end of 2016

#### 3. Quality of CGFM and the credit guarantee system improved

- 3.1 Conclude consultations with all stakeholders regarding amendment to the Law on the CGFM and preparing a legal and regulatory framework for the operation of a private credit guarantee system and by end of 2016.
- 3.2 Develop and implement operational, governance, and risk management capacity of CGFM by end of 2016.

<p>3.3 Enhance management information and risk management systems of CGFM by issuing EOIs for new system needs and beginning vendor work by end of 2017.</p> <p>3.4 Begin regular outreach training for CGFM regional representatives and in aimags on guarantee program, products, environmental and social safeguards, labor standards, and gender support by end of 2017.</p>
<p><b>Inputs</b></p> <p><b>Project Loan</b> ADB: \$60.0 million Government and private sector: \$30.0 million</p> <p><b>Technical Assistance</b> ADB: \$800,000 (TASF-V)</p> <p>Note: The government will also finance the equivalent of counterpart costs in kind to include providing adequate counterpart staff, office facilities, office supplies, secretarial assistance, domestic transportation and accommodation for counterpart staff, and communication facilities for consultants.</p>
<p><b>Assumptions for Partner Financing</b> Not applicable</p>

<sup>a</sup> Introduced by the Ministry of Labour 28 November 2013 and subsequently became responsibility of the Ministry of Industry at its founding in 2014.

<sup>b</sup> Women run businesses for this project are identified as businesses that meet at least one of these criteria: (i) at least 50% of ownership controlled by women; (ii) at least 60% of senior managers are women; or, (iii) at least 50% of the registered contractual employees are women. Source: Asian Development Bank Gender Toolkit for Micro, Small, and Medium-Sized Enterprise Finance and Development, 2014.

<sup>c</sup> Supported by the TA.

CGFM = Credit Guarantee Fund of Mongolia, EOI = Expressions of Interest, MOF = Ministry of Finance, MOI = Ministry of Industry, NSO = National Statistical Office of Mongolia, PFI = participating financial institution, SME = small and medium-sized enterprise, TASF = Technical Assistance Special Fund.  
Source: Asian Development Bank.

## B. Monitoring

114. A Project Performance Monitoring System will be established and implemented by the PSC in the first month of project implementation. Throughout project implementation, the Project Performance Monitoring System, through the project performance report, will assess the likelihood that key milestone dates for activities, outputs, outcome, and impact will be achieved—the impact indirectly by monitoring assumptions and risks. The DMF will be reviewed during the project implementation and, when needed, adjusted to reflect changing circumstances and project environments so that the intended project outcome can be achieved. Following project completion, the project is subject to an assessment of the outcome along with recommendations for enhancing and sustaining the outcome. A project completion report will also include a preliminary assessment of the impact.

115. The CGFM PIU will monitor project implementation through preparation of quarterly progress reports from PFIs, regular communications with PFIs, and outreach. The CGFM PIU will gauge progress by tracking the issue of sub-loans to SMEs against the proposed schedule and, as needed, assist the PFIs in taking necessary measures to address any problems arising during the implementation. ADB will continue to monitor project performance in four aspects, e.g., technical, disbursement, financial management, and safeguards, through the executing agency's quarterly project progress reports, day-to-day communication with the CGFM PIU, and ADB review missions.



116. **Compliance monitoring:** The executing agency will monitor compliance with covenants stipulated in the loan agreements. ADB will monitor the compliance status through the executing agency's quarterly project progress reports, day-to-day communication with the MOF, and ADB review missions; and take necessary remedial measures for any noncompliance.

117. **Social monitoring.** There is no foreseen impact on indigenous people or resettlement. Monitoring of social safeguards will therefore not be necessary. There will be some gender benefits that will be enhanced through training for PFIs. A gender focal-point will be appointed by the CGFM PIU. Monitoring of gender benefits will be performed by the CGFM PIU on a quarterly basis and reported to ADB annually with project progress reports.

118. **Environmental Safeguards monitoring.** The PFIs and the CGFM are responsible for ensuring that all environmental assessment documents and environmental monitoring reports are properly and systematically kept as part of the record of a loan and project implementation by the borrower. The CGFM PIU will be responsible for monitoring and reporting and shall appoint a person in charge of environmental issues.

119. The Borrower shall ensure or cause CGFM and PFIs to ensure that the preparation, design, construction, implementation, operation and decommissioning of each qualified SME sub-project will comply with (i) all applicable laws and regulations of Mongolia relating to environment, health and safety; (ii) the ESMS; and (iii) all measures and requirements set forth in the respective EMP, and any corrective or preventative actions set forth in a Safeguards Monitoring Report.

120. **Safeguards Monitoring Report.** The Borrower will cause CGFM and PFIs to do the following: (i) submit semi-annual Safeguards Monitoring Reports to CGFM for compilation and timely submission by CGFM to the Borrower and annually to ADB; (ii) if any unanticipated environmental and or social risks and impacts arise during any qualified SME sub-project implementation, promptly inform the Borrower, CGFM and ADB of the occurrence of such risks or impacts, with detailed description of the event and proposed corrective plan; and (iii) report to the Borrower, CGFM and ADB any actual or potential breach of compliance with the measures and requirements set forth in the EMP, promptly after becoming aware of the breach.

### **C. Evaluation**

121. ADB and the government will jointly undertake reviews of the project at least once a year. The reviews will (i) review overall implementation of the project and update, in consultation with the executing agency, the project implementation schedule; (ii) examine existing and potential implementation problems, and find out measures with the executing agency to resolve them; (iii) review progress in procurement and disbursement; (iv) review the borrower's compliance with particular loan covenants and, where there is any noncompliance or delay, discuss proposed remedial measures with the borrower; and (v) assess the likelihood of attaining the project's outcome.

122. ADB and the government will undertake a midterm review during the 3rd year of implementation to assess disbursement status and take appropriate measures, including modification of scope and implementation arrangements, and rescheduling of loan proceeds, as appropriate to achieve the project's outcomes and impact.

123. Within 6 months of physical completion of the project MOF will submit a project completion report to ADB.<sup>37</sup>

#### **D. Stakeholder Communication Strategy**

124. The project will rely on existing donor coordination mechanism in Mongolia to coordinate project development efforts as well as align and harmonize the contributions of the donors. Public disclosure of project documents as well as project activities will be made available through the project website.

125. The CGFM PIU will work with the executing and implementing agencies to communicate with stakeholders including PFIs and SME associations regarding matters related to the project. Regular dialogue and communication with the PFIs will provide a channel for updating these banks on the overall progress of the project as well as to provide a feedback mechanism for resolving issues regarding sub-loans to SMEs. The CGFM PIU will prepare proposals that include participatory measures and consultations with SMEs nationwide.

### **X. ANTICORRUPTION POLICY**

126. ADB reserves the right to investigate, directly or through its agents, any violations of the Anticorruption Policy relating to the Project.<sup>38</sup> All contracts financed by ADB shall include provisions specifying the right of ADB to audit and examine the records and accounts of the executing agency and all Project contractors, suppliers, consultants and other service providers. Individuals/entities on ADB's anticorruption debarment list are ineligible to participate in ADB-financed activity and may not be awarded any contracts under the Project.<sup>39</sup>

127. CGFM will ensure and will cause each PFI to ensure that it will (a) comply with ADB's Anticorruption Policy (1998, as amended to date) and acknowledge that ADB reserves the right to investigate directly, or through its agents, any alleged corrupt, fraudulent, collusive or coercive practice relating to the Project; and (b) cooperate with any such investigation and extend all necessary assistance for satisfactory completion of such investigation.

128. CGFM will cause each PFI to ensure that anticorruption provisions acceptable to ADB are included in all contracted financed by ADB utilizing the proceeds of the ADB Loan, including provisions specifying the right of ADB to audit and examine the records and accounts of the PFIs and the qualified SME borrowers as they relate to the Project and cooperate fully with any such investigation and to extend all necessary assistance, including providing access to all relevant books and records, for the satisfactory completion of any such investigation.

129. **Anti-money laundering and financing of terrorism.** CGFM will cause each PFI to comply with applicable laws and regulations of Mongolia and relevant international standards, including the recommendations and special recommendations made by the Financial Action Task Force concerning anti-money laundering and combating financing of terrorism. This includes ensuring that each PFI undertakes customer due diligence, report suspicious transactions and maintain internal control and procedures. CGFM will also cause each PFI to acknowledge that ADB may disclose to any competent national or international authority any

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<sup>37</sup> Project completion report format is available at: <http://www.adb.org/Consulting/consultants-toolkits/PCR-Public-Sector-Landscape.rar>

<sup>38</sup> Available at: <http://www.adb.org/Documents/Policies/Anticorruption-Integrity/Policies-Strategies.pdf>

<sup>39</sup> ADB's Integrity Office web site is available at: <http://www.adb.org/integrity/unit.asp>

information obtained by ADB in relation to such PFI's level of compliance with such laws and regulations and international standards.

## **XI. ACCOUNTABILITY MECHANISM**

130. People who are, or may in the future be, adversely affected by the project may submit complaints to ADB's Accountability Mechanism. The Accountability Mechanism provides an independent forum and process whereby people adversely affected by ADB-assisted projects can voice, and seek a resolution of their problems, as well as report alleged violations of ADB's operational policies and procedures. Before submitting a complaint to the Accountability Mechanism, affected people should make a good faith effort to solve their problems by working with the concerned ADB operations department. Only after doing that, and if they are still dissatisfied, should they approach the Accountability Mechanism.<sup>40</sup>

## **XII. RECORD OF PAM CHANGES**

131. All revisions and/or updates during the course of implementation should be retained in this Section to provide a chronological history of changes to implemented arrangements recorded in the PAM.

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<sup>40</sup> For further information see: <http://www.adb.org/Accountability-Mechanism/default.asp>.