SMEs and Women-owned SMEs in Mongolia

MARKET RESEARCH STUDY

IN PARTNERSHIP WITH

International Finance Corporation

Foreign Affairs, Trade and Development Canada

Affaires étrangères, Commerce et Développement Canada
SMEs and Women-owned SMEs in Mongolia

MARKET RESEARCH STUDY
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<th>Description</th>
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<tbody>
<tr>
<td>ADB</td>
<td>Asian Development Bank</td>
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<td>ATM</td>
<td>Automatic Teller Machine</td>
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<td>EAP</td>
<td>East Asian and Pacific</td>
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<td>BOM</td>
<td>Bank of Mongolia</td>
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<td>BPI</td>
<td>Business Plus Initiative</td>
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<td>BPN</td>
<td>Business Professionals Network</td>
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<td>CEO</td>
<td>Chief Executive Officer</td>
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<td>DBM</td>
<td>Development Bank of Mongolia</td>
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<td>EBRD</td>
<td>European Bank for Reconstruction and Development</td>
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<td>EU</td>
<td>European Union</td>
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<td>FDI</td>
<td>Foreign Direct Investment</td>
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<td>FI</td>
<td>Finance Institution</td>
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<td>FRC</td>
<td>Financial Regulatory Commission</td>
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<td>FS</td>
<td>Frankfurt School of Finance &amp; Management</td>
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<td>FX</td>
<td>Foreign Exchange</td>
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<td>GDP</td>
<td>Gross Domestic Product</td>
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<td>HO</td>
<td>Head Office</td>
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<td>IFC</td>
<td>International Finance Corporation</td>
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<td>IFI</td>
<td>International Finance Institution</td>
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<td>IMF</td>
<td>International Monetary Fund</td>
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<td>IRIM</td>
<td>Independent Research Institute of Mongolia</td>
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<td>IT</td>
<td>Information Technology</td>
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<td>JICA</td>
<td>Japan International Cooperation Agency</td>
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<td>MBA</td>
<td>Mongolian Bankers Association</td>
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<td>MCA</td>
<td>Millennium Challenge Account</td>
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<td>MFI</td>
<td>Micro Finance Institution</td>
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<td>MIS</td>
<td>Management Information System</td>
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<td>MNCCI</td>
<td>Mongolian National Chamber of Commerce and Industry</td>
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<td>MNT</td>
<td>Mongolian Tugrik</td>
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<td>MOL</td>
<td>Ministry of Labor</td>
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<td>MONES</td>
<td>Mongolian Women’s Fund</td>
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<td>MSME</td>
<td>Micro, Small and Medium Enterprises</td>
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<td>NCAV</td>
<td>National Center Against Violence</td>
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<td>NBFI</td>
<td>Non-Bank Financial Institution</td>
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<td>NCGE</td>
<td>National Committee on Gender Equality</td>
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<td>NGO</td>
<td>Non-Governmental Organization</td>
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<td>NPL</td>
<td>Non-Performing Loans</td>
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<td>NSO</td>
<td>National Statistical Office of Mongolia</td>
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<td>OT</td>
<td>Oyu Tolgoi copper mine</td>
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<td>PPP</td>
<td>Purchasing Power Parity</td>
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<td>SCC</td>
<td>Savings and Credit Cooperative</td>
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<td>SME</td>
<td>Small- and Medium-Sized Enterprise</td>
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<td>STCR</td>
<td>Secured Transactions and Collateral Registry Program</td>
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<tr>
<td>TA</td>
<td>Technical Assistance</td>
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<tr>
<td>UB</td>
<td>Ulaanbaatar</td>
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<tr>
<td>UNDP</td>
<td>United Nations Development Program</td>
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<tr>
<td>US</td>
<td>United States</td>
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<tr>
<td>USAID</td>
<td>United States Agency for International Development</td>
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<tr>
<td>USD</td>
<td>United States Dollars (1 USD=1,800 MNT conversion rate is used in this paper for ease of calculations)</td>
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<tr>
<td>VAT</td>
<td>Value Added Tax</td>
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<tr>
<td>WE</td>
<td>Women Entrepreneur</td>
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<td>WIN</td>
<td>Women in Business Program</td>
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Executive Summary

The World Bank Group has been active in Mongolia since 1991 and has invested in many projects across a variety of sectors. International Finance Corporation (IFC) is a member of the World Bank Group and is the largest global development institution focusing exclusively on the private sector. IFC has been active in Mongolia for more than two decades and has provided equity, loans and trade financing, as well as advisory services to companies, financial institutions and regulatory authorities. Supporting growth and competitiveness of small and medium enterprises (SMEs) is central to IFC’s strategy in Mongolia. The future IFC programs in Mongolia will also prioritize women-owned SMEs in order to address some of the obstacles that women entrepreneurs face accessing finance.

IFC wishes to compile data on both male- and female-owned enterprises in Mongolia in order to better understand the business characteristics of SMEs, the profile of the entrepreneurs, their relations with financial institutions, the challenges they face, and their expectations for the future. For this purpose, IFC has commissioned the Frankfurt School of Finance & Management (FS) and the Independent Research Institute of Mongolia (IRIM) to conduct market research focusing on the enabling environment, and supply and demand prospects for SMEs, with particular focus on women-owned businesses. The study is expected to provide guidance to IFC in the design and implementation of their SME Banking and Women in Business Programs for Mongolia.

The market research was carried out by a team of international and local consultants in May-July 2014. It started with the desk review of the literature related to the topic. Two sets of questionnaires were developed for the assessment of the supply and demand regarding financial products as well as services for SMEs and women-owned SMEs. To assess the environment that SMEs operate in and the availability and scope of financial and non-financial services provided to them, interviews were conducted with various stakeholders engaged in SME finance and gender-related and regulatory issues (Annex A). Additionally, a survey among men- and women-owned SMEs was conducted with the representative sample of 240 interviews in three cities (Ulaanbaatar, Erdenet, Darkhan). Through this survey, more information on the entrepreneurs and their businesses could be obtained and challenges, constraints and opportunities could be explored, in particular regarding access to financial and non-financial services.

Definition of SMEs and Women-owned SMEs

Despite the introduction of a national SME definition in 2007, this definition is not widely used by industry stakeholders. The National Statistical Office of Mongolia (NSO) uses a different employee-number categorization in collecting its annual business register data. Commercial banks either do not segment their clients or use their own segmentation criteria in terms of employee number and annual turnover.
A revision of the SME definition seems to be necessary. Industry stakeholders are of the opinion that the current national definition is far too broad regarding the employment size and outdated in terms of annual turnover because of an about 55% depreciation of the Mongolian Tugrik (MNT) since the enactment of the SME Law.

There is currently no definition for women-owned enterprises generally accepted by governmental or financial institutions. Gender-disaggregated data on SME clients at commercial banks is currently not available either. However, according to the managers of several commercial banks and non-bank financial institutions, the share of female-owned businesses in the sector is significant, approaching nearly 60% of micro-scale, family, and sole-entrepreneur-owned businesses. This observation of industry stakeholders differs significantly from the findings of the Mongolia Enterprise Survey 2013 recently completed by the World Bank, which shows the percentage of firms with female ownership at 38.9%.1

**Enabling Environment**

The stability of the macroeconomic environment is important for businesses of all segments, including SMEs. After posting high growth rates in the last decade, Mongolia entered a more volatile economic period that was immediately reflected in the deterioration in the business sentiment. The government’s action plan to stabilize the environment produced satisfactory results in the last two years and also boosted entrepreneurship, as illustrated by the roughly 35% increase in the number of registered and active enterprises from 2010 to 2013. Nevertheless, poor corporate governance, gaps and inconsistencies in the regulatory framework, and lack of adequate support mechanisms in Mongolia, remain key restraining factors that hamper the development of both male- and female-owned SMEs. The pressure is especially strong at the smallest end of SMEs with a considerable portion of micro-enterprises ceasing activities shortly after being established.

The country suffers from harsh geographical conditions exacerbated by poor infrastructure and limited transportation, causing economic activities and most businesses to be based in Ulaanbaatar. This works against an equal distribution of the national income. In addition, poorly designed regulations, bureaucratic burdens, and lack of incentive schemes for business registry encourage informality in Mongolia, making quantitative analysis difficult.

**Supply Perspective**

The strengthening of SMEs is crucial to achieve broad-based and sustainable growth in Mongolia. Nevertheless, SMEs are constrained by a number of problems, among which access to finance is identified as one of the most difficult barriers to growth and development. As far as the banking sector is concerned, loans provided by commercial banks tend to be short-term, expensive and require very high collateral.

Collateral requirements are particularly constraining for SMEs since commercial banks usually ask for immovable property due to the non-existence of a central registry of movable assets. Weaknesses in the legal framework for enforcement mechanisms also force banks to avoid accepting the pledge of movable property. Securing repayment in a case of competing claims can be very difficult, especially when real-time information on priority pledges is not available. As a result, the market for providing bank finance against movable collateral is almost non-existent in Mongolia.

Secured transactions reform has been on agenda of the Mongolian government since 2006. IFC also provided support in the finalization of the draft bill as part of its Secured Transactions and Collateral Registries (STCR) Program, which covers Mongolia as well as 27 other countries worldwide as of November 2013. IFC has offered additional help to the government with the establishment of the pledge registry and is waiting for an official invitation by the government as well as for its decision on strategy before taking further steps.2

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1 Enterprise Survey (2013).
2 IFC has vast experience in the establishment of online collateral registries for movable assets worldwide (China, Ghana, Mexico, Vietnam, Afghanistan, etc.).
Although bank lending has posted high growth rates in recent years, this growth stemmed from increased exposure in construction companies and real estate developers, as well as individuals. Household lending in particular picked up in 2013 with the introduction of the housing development program by the government through commercial banks. As a result, while corporate and individual loans reached 47% and 37% of the total loan book respectively, SME loans remained at 16% revealing a low level of commercial-bank penetration in this segment.

Lending to SMEs is perceived as risky by commercial banks because of this segment’s low capitalization and lack of immovable assets. This is also partly due to the lack of capacity at commercial banks in implementing cash-flow-based lending mechanisms. The situation is exacerbated by the ineffectiveness of the existing credit-information system, which covers less than 15% of all enterprises in Mongolia.3

Lending to women is generally perceived by the banks as more risky than lending to men, as women more often lack assets that can be provided as collateral. At the same time, both commercial banks and NBFI’s say that loan repayment rates by women are higher than those of men. Financial institutions are either not aware of or not convinced that women-owned SMEs are a distinct business segment or at least a significant market opportunity. One of the reasons for this lack of awareness can be the reluctance of financial institutions to collect gender-disaggregated data on SMEs. This makes it difficult to estimate the share and analyze the profitability of women-owned SMEs in the total SME portfolio. Collecting and analyzing gender-disaggregated data, however, could be the first step to recognizing women-owned SMEs as an underserved yet profitable client segment.

Nevertheless, in some lending programs, such as the one implemented jointly by selected banks, the Development Bank of Mongolia, the Ministry of Economic Development, and the Ministry of Food and Agriculture entitled “Wool, Cashmere, Sewing Lines, Greenhouse and Intensive Farming Projects”, the share of women-owned businesses has been estimated at 60%.

In the absence of bank financing that reaches out to all client segments, SMEs in Mongolia seek funding outside of the banking sector. Non-bank financial institutions (NBFI’s) and savings and credit cooperatives (SCCs) are alternative sources that SMEs often pursue, especially when in need of short-term or start-up financing. NBFI’s, however, cannot fully meet the SMEs’ demand for finance due to their limited funding capacities.

In this situation, the government of Mongolia often intervenes in the sector through a number of SME support programs that provide lending at below-market rates through commercial banks as well as business advisory trainings through public bodies. Nevertheless, apart from the recently established Credit Guarantee Fund, the programs launched so far by the government do not tackle the issue of collateral, which is of utmost importance to SMEs in accessing finance. Additionally, in the long term, such programs with subsidized lending rates may lead to the distortion of market mechanisms in the banking sector.

**Demand Perspective**

The information concerning the size of the SME sector in Mongolia is difficult to obtain from official sources. The statistics on SMEs are limited and unreliable. The NSO does not produce data exclusively on SMEs. The statistics declared by the NSO cover all business entities in Mongolia, including large companies and are not in alignment with the official definition of SME Law.

The Mongolia Enterprise Survey 2013 recently completed by the World Bank represents one of the latest sources of information on characteristics of and obstacles experienced by private-sector enterprises in Mongolia. For

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This survey, business owners and top managers of 360 firms were interviewed from December 2012 through July 2013.

Most of the SMEs and women-owned SMEs surveyed for the present study indicated high-level use of banking services and familiarity with most of available financial and non-financial services offered by various financial institutions. The level of loan penetration is high as more than 60% of all businesses in the survey had a loan for business purposes. Most of the businesses, irrespective of the gender of their owner, had the successful experience of applying for and obtaining a loan for business purposes (of 84% who applied for a loan, 88% were successful).

The majority of the SMEs (95%) are interested in obtaining a loan in the future, mostly for the purchase of equipment and machinery as well as to cover working capital needs, preferably on conditions of a grace period (three to six months) and for a longer period of time than is currently available.

Banking is still very dependent on branch visits with a high share of entrepreneurs visiting a branch at least weekly. Still, modern banking technologies like internet banking and especially mobile banking (with a weekly usage rate of 57%) are also becoming ever more popular.

**Gender-specific Differences**

Social and cultural aspects should be considered when analyzing the business profile of SMEs through a gender lens. Mongolian culture exhibits collectivistic cultural characteristics: it is family-oriented with a strong cultural identity and cohesiveness. It has been largely influenced by the nomadic way of life: breeding livestock, living in “Gers” and moving form pasture to pasture. Women have been participating in all activities related to this way of life as well as in taking decisions about family businesses.

Today, family ties still play a significant role. Many of the businesses are established as family businesses or with the support of family members. Even if a woman is not an owner, she nevertheless takes an active part in key business decisions.

Another factor that has played a role in the high social status of women in Mongolia is the equality in education and social rights granted to women during the communist era from 1924 to 1990. The communist culture, however, promoted the clear separation of responsibilities, assigning women the role of mother and housewife rather than entrepreneur. After the collapse of the communist system, Mongolia witnessed a rise in women’s social status as many of women started their own businesses and now perform the same jobs men do.

This study revealed that the issues confronting women entrepreneurs do not differ considerably from those confronting male entrepreneurs in terms of doing business and access to finance. Certain gender differences however come to the fore when the social role of women is considered.

Women are perceived to be the primary caretaker of household chores and the children. The men surveyed generally recognized this additional burden; female survey respondents specifically referred to family and household responsibilities as their most important challenge, which limits their time for networking or participating in training, etc.

The legal framework provides women equal rights in inheritance, land use and ownership of the property. However, industry stakeholders are of the opinion that women entrepreneurs usually possess less movable and immovable assets. Therefore, there is a pervasive belief that women face greater difficulties fulfilling collateral requirements than men do. The findings of this study, however, show that this does not hold true, although both men and women perceive collateral requirements as the greatest challenge in applying for a loan.

These and potentially other factors, our study finds, are responsible for the fact that women’s businesses are typically smaller, demonstrate
lower turnover rates and have fewer employees. In general, women are more likely to employ women.

**Prevalence of Family-owned Businesses**

As mentioned above, Mongolian culture is a family-oriented, collectivistic culture, heavily influenced by the nomadic way of life. As our observations during the interviews have shown, a significant number of businesses operate as family businesses, revealing that more than 45% of the businesses in the sample are family-owned.

In Mongolia, the decision about the potential owner of a property is usually made jointly within the family and the decision is not necessarily based on the gender of the owner. Other issues such as employment status of the potential owner are also considered. The possibility of taking a bank loan is higher for the employed, therefore they are preferred by the family to be the owner of the property and to pledge collateral to the bank.

As usually more women work informally compared to men, women might also be sacrificing their property ownership right in favor of their husbands in order to access finance as a family. Hence, despite the existence of an equal treatment of men and women by law with regards to property ownership, incentives for business registry should be promoted to encourage women to take ownership of family property.

Furthermore, introduction of family-friendly workplace and government policies could help women to balance work and family life and would benefit all business development, family stability, community and society. Tax breaks and subsidies can be used to encourage businesses and other entities to adopt family-friendly policies (maintaining an on-site child care center, for instance, or for subsidizing employees’ child care costs). Public funding can be provided for family-friendly interventions and services such as family literacy programs, women programs and long-term elder-care services as well as for maintaining family-oriented public facilities. These are just a few ways for the government to encourage family-friendly policies in business and public life in general.

**Recommendations**

The present study reveals important features of SMEs in Mongolia and provides insights into gender implications for SME banking. It also suggests some recommendations for International Finance Institutions (IFIs), governmental/regulatory authorities, financial Institutions and SME development/support institutions.

Thus, against the backdrop of an environment where assessing the credibility of SMEs is a challenge for banks, regulatory authorities are advised to enhance the existing credit information system by which SMEs are currently not widely covered. Providing tax incentives in the leasing law would facilitate the development of the leasing industry. Adequate legal framework for pledging receivables would encourage the development of factoring. Both can be important instruments of financing for SMEs.

The high penetration of technology in people’s daily lives creates a suitable environment for the introduction of contract financing and on-line factoring as complementary financing mechanisms. Chambers of commerce and banks are, for instance, advised to cooperate in the establishment of supply-chain finance mechanisms.

Enactment of the draft bill on the pledge of movable properties and the introduction of a registration procedure setting out the full process should be given priority. It would increase banks’ lending to the SME segment. Above all, regulatory authorities are recommended to coordinate the efforts of all the institutions and NGOs involved in capacity building for SMEs and women entrepreneurs.

To address the issue of SMEs being perceived as risky by commercial banks, IFIs can consider incorporating risk-sharing mechanisms into their
investment programs for Mongolia. This would alleviate the banks’ discomfort in lending to SMEs. On the other hand, designing financing programs exclusively for Women Entrepreneurs (WEs) would increase the banks’ awareness about women-owned SMEs as a distinct segment. Financial institutions are advised to develop internal capacity to move from collateral-based to cash-flow-based lending.

In collaboration with SME support institutions, they are also encouraged to organize SME networking and information-sharing events as well as trainings to address the key challenges that both male and female-owned SMEs face in terms of their internal capacity, especially at the start-up phase. Considering the geographical conditions and poor infrastructure in rural Mongolia, seminars and capacity-building activities should be offered in a format suitable for remote learning. Thus the content of those can be transferred to e-learning platforms and proposed to SMEs in online modules.

International financial institutions should further support capacity building at banks in the field of SME finance as well as through programs targeting exclusively women entrepreneurs. The latter should promote women entrepreneurs to the banks as an attractive market segment in particular though gender awareness raising events (invite women entrepreneurs, promote collecting gender-disaggregated data) and/or loan-dedicated programs (design of women-entrepreneur product packages, etc.). Capacity building should be further provided to banks and SME support centers in terms of development of high-quality training courses on most requested topics like financial management, marketing and sales, etc., as well as business advisory services (legal issues, taxation, loan application).

SME support institutions are advised to cooperate more strongly with banks in training and business advisory services, to expand trainings to rural areas and to improve their quality, as well as to organize information campaigns about land registry and property rights that reach out to women entrepreneurs.
1. Introduction

Mongolia has posted impressive growth over the past decade, driven primarily by extensive investment in mining and large infrastructure projects. The recent growth has been boosted in particular by fiscal and monetary programs led by the government. To realize its full economic potential, the country still needs to make the growth sustainable in order to develop its economy, to become less vulnerable to external shocks, and to decrease income disparity. This can only be achieved if growth is broad-based across various sectors and business segments, ranging from large corporations to micro, small and medium enterprises (SMEs).4

Although SMEs make up nearly 98% of all enterprises in Mongolia (about 80% of which are microenterprises), their contribution to GDP remains low at 25%.5 This raises the question of what measures can be taken to address the specific needs of Mongolian SMEs in order to improve their performance and accordingly their contribution to economic development.

Undertaking efforts to support SMEs in general and women-owned enterprises in particular in realizing their growth potential is crucial, especially in developing and transition countries. Prior to the boom of the last decades, the Mongolian economy was centered on agriculture (mainly herding and livestock breeding), which traditionally enabled women to contribute to the household income and participate in economic life. Influenced by the Mongolian nomadic way of life, on the one hand, and communist educational policies and the post-communist era of freedom, on the other hand, Mongolian culture and history has influenced women’s entrepreneurial motivations and social status.6

Given the social and historical context in Mongolia, many women are today engaged in business life, a fact also shown by the World Bank’s estimate on women’s participation in the workforce: 57% as of 2013.7 In rural areas, women are actively involved in day-to-day family business issues and in making key decisions about, for example, buying equipment, selling or buying livestock, or moving to a different location. Furthermore, in urban areas, many women have become active entrepreneurs engaged in manufacturing, tourism, and trade, etc.

Recognizing the importance of SMEs’ and women-owned SMEs’ contribution to the economy, international organizations and regulatory authorities are keen on improving the regulatory and operating environment for SMEs, as well as access to funding and non-financial services, which can pose major impediments to

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4 According to the official definition (see Table 3), SMEs include micro entrepreneurs (small companies are companies with less than 19 employees). To be in alignment with this definition, the abbreviation “SME” and not “MSME” is used in this paper.
7 World Bank (2013).
their development. To be able to design tailored support, a comprehensive view across the SME market from several perspectives – enabling environment, the supply and demand sides of financial services – is crucial. This highlights the need to capture the quantitative and qualitative data on both male- and female-owned SMEs to be able to better understand the financial and non-financial constraints that can be addressed at policy, financial sector, and market levels.

The rationale for this research is thus to collect and analyze the data from public (government, available literature) and private (business women’s organizations, local and international research institutions, financial institutions) sources, incorporating the findings from a survey conducted with a representative sample of men- and women-owned enterprises. Based on the information collected through desk and field research, this study highlights the key trends, challenges and opportunities for SME development across the three perspectives outlined above: enabling environment, supply provided to SMEs, and demand for and ability to access finance. The study further explores specific constraints faced by women-owned businesses. The knowledge obtained from analysis of the research target groups by gender will help to better cater to their needs in the future.

The market research on SMEs and women-owned SMEs in Mongolia was conducted by Frankfurt School of Finance & Management (FS) and Independent Research Institute of Mongolia (IRIM) from May to July 2014.

The research was commissioned by the International Finance Corporation (IFC), a member of the World Bank Group. The IFC intends to implement a SME Banking Program in Mongolia, supported by specific advisory services to increase SMEs’ access to finance. The future IFC program in Mongolia will also focus on women-owned SMEs and will leverage IFC’s investment and advisory services. It will also cooperate with women organizations and other stakeholders (business women associations, business development service providers, etc.) to address some of the demand-side obstacles to achieve greater access to financial services for women entrepreneurs.

Road Map of the Study

Chapter 1 summarizes the scope of the study and outlines its key objectives. It explains the rationale for collecting data on SMEs in Mongolia in general and women-owned SMEs in particular. It also provides recommendations for integrating the insights form the study into the on-the-ground practice of SME banking, as well as potential interventions on the regulatory and policy level.

Chapter 2 begins with the analysis of the general macroeconomic context and provides an overview of the SME sector in Mongolia. The chapter analyzes the latest trends in development of the business environment and the legal framework relevant for SMEs and women-owned SMEs.

Chapter 3 examines the aspect of supply in financial and non-financial products and services currently offered to SMEs by commercial banks and non-bank financial institutions. It also reviews the support provided to SMEs by international financial institutions.

Chapter 4 provides detailed overview of the findings of the demand study, explores the features of SMEs, their relationships with banks and NBFI as well as aspects of current use of bank loans. The chapter further analyzes the usage and demand for other banking products and services by SMEs.

Chapter 5 summarizes the key constraints faced by the SMEs and female-owned SMEs revealed in the interviews with stakeholders and the face-to-face interviews with business owners.

Chapter 6 uses the findings to draw conclusions and recommendations on possible measures to address the challenges of SMEs and women-owned SMEs specifically at different stakeholder levels: governmental and regulatory authorities, international finance institutions, financial institutions and SME development organizations.
2. Enabling Environment

2.1 Country Profile, Demographics and Administration

Mongolia is a land-locked country between China and Russia in Central Asia and covers a vast area of 1.56 million square kilometers. As of 2014, its population of 2.9 million (48.7% males, 51.3% females) makes Mongolia one of the world’s least densely populated countries. Mongolia has 794,100 households, of which 64% are urban and 36% rural. About 81,700 households, or 10% of all households in the country, are headed by females.

Mongolia is administratively divided into 21 aimags and the capital city of Ulaanbaatar. Ulaanbaatar is an independent municipality and is not part of a province. The aimags are sub-divided into soums; and soums into baghs. The capital city is divided into districts; and districts are divided into khooros. Ulaanbaatar is the political and economic hub of Mongolia hosting 46% of the population. Rural areas are considerably less developed and dominated by agriculture, in particular livestock.

The prime minister is the head of the government. All legislative power is granted to the State Great Khural, Mongolia’s unicameral parliament, which has 76 members elected by public vote for a term of four years.

The revised election law, passed in 2012, contains many new regulations, including the introduction of proportional representation for 28 of the 76 seats. It also specifies that a minimum of 20% of the candidates nominated and approved would have to be women. However, no quota on the number of female parliamentarians has been introduced so far. As of 2012, 17% of all parliament members are women, quadruple the women’s share in 2008 (Table 1).

2.2 Macroeconomic Overview and Recent Developments

In recent years, Mongolia has been one of the most rapidly expanding economies in the world. The main drivers of this economic growth have been development of the mining industry and investments in large infrastructure projects.

| TABLE 1: MEMBERS OF THE STATE GREAT KHURAL BY GENDER |
|-----------------|-----|-----|-----|
|                 | 2004 | 2008 | 2012 |
| Female          | 5    | 3    | 11   |
| Male            | 71   | 73   | 65   |
| Female Members as a % in Total | 7%   | 4%   | 17%   |

---

8 National Statistical Office (NSO), 2013.
9 The NSO describes urban population as people residing in Ulaanbaatar city, aimag centers and towns. The rural population includes population reside in soum centers and further rural areas.
10 A mother headed household refers to a single mother who with legitimated children (biological or adopted in/out of a marriage) whereas other parent is not determined legally, or was died, or missed, or has no legal capacity, or whose parental rights have been limited with a court decision.
The country’s rich mineral deposits, as well as growing foreign and local investments to the mining sector, have transformed Mongolia’s economy from one traditionally dependent on herding and agriculture into a booming industrial economy. Mongolia is richly endowed with natural resources such as coal, copper, fluorite, gold, iron ore, and lead, etc. The share of the mining sector in Gross Domestic Product (GDP) has been increasing with the commodity prices in the world market for the past 15 years, reaching 18% as of 2013 (Figure 1). Mineral GDP registered 20.7% growth in 2013 and 27.3% in the first quarter of 2014.

Another driver of growth has been real estate development and construction due to the increase in housing demand and infrastructure spending. Agriculture and trade also accounted for a major share in GDP in 2013, with 14% and 11% respectively.

In 2013, global money fled emerging economies. Mineral prices declined and Mongolia’s mining industry slumped. The second phase development of the Oyu Tolgoi (OT) copper mine was halted due to disagreement between the stakeholders. As a result of these developments, foreign direct investment (FDI) to Mongolia decreased to half of the previous year (from USD 4.4 billion in 2012 to USD 2.3 billion in 2013, see Table 2). The trade deficit fell due to subdued domestic demand, foreign reserves decreased. The Mongolian Tugrik (MNT) depreciated by 20% against the USD. In addition, the slowdown in growth in China curbed demand for coal, Mongolia’s biggest export product.

The Mongolian government reacted by increasing fiscal spending, in particular of large investment projects. Most of the funding was raised through the issuance of Chinggis Bonds in November 2012, which was off-budget spending for the government that not only increased government debt but also pushed up the fiscal deficit ratio to 10.9% of GDP in 2012, 6% higher than in 2011.

Other measures were taken by the Central Bank of Mongolia (BOM), introducing a Price Stabilization Program to combat the slowing economy. The program, which primarily consisted of monetary easing measures and increased liquidity in the financial sector by MNT 3 trillion (close to 20% of GDP), has been carried out through the following actions:

- Provision of subsidized financing of MNT 718 billion for selected industries through commercial banks in order to address supply side constraints.

* The operations of OT mine have been re launched in the second half of 2013.
• Liquidity injection of MNT 900 billion to commercial banks in the form of one-year deposits to support the economy.

• Introduction of a construction and housing development program including a MNT 1,200 billion subsidized mortgage loan (with 8% p.a.) for households and MNT 430 billion for construction companies to be disbursed via commercial banks.

These actions hold GDP growth in double digits, but nevertheless growth dropped from 12.4% in 2012 to 11.7% in 2013 (Table 2). The Chinggis Bonds are due in 2017 and 2022 and will have to be repaid by the central government, which is a source of concern for some investors. Considering the huge direct spending by the government, the fiscal deficit is likely to stay above 10% of GDP as is the case with the inflation rate.12

2.3 The SME Sector

SMEs make up 98% of all enterprises in Mongolia (about 80% of which are microenterprises). They contribute 25% to GDP and employ 52% of the workforce.13 The SME Law adopted in July 2007 was aimed at improving the consistency and effectiveness of government support programs; it provided a definition for SMEs in Mongolia for the first time.

According to the law, SMEs are defined as legally registered business entities with 199 or fewer employees and with an annual turnover of up to MNT 1.5 billion (USD 833,000). The SME Law also differentiates between sectors in terms of number of employees and annual turnover for a company to be considered as small or medium enterprise (Table 3).

### Table 2: Selected Macroeconomic Indicators

<table>
<thead>
<tr>
<th></th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014 (F)</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP, current prices (USD mln)*</td>
<td>6,197</td>
<td>8,761</td>
<td>10,322</td>
<td>11,516</td>
<td>12,057</td>
</tr>
<tr>
<td>Real GDP Growth (y.o.y.)*</td>
<td>6.4%</td>
<td>17.5%</td>
<td>12.4%</td>
<td>11.7%</td>
<td>12.9%</td>
</tr>
<tr>
<td>GDP per capita, by PPP (USD)°</td>
<td>3,985</td>
<td>4,721</td>
<td>5,298</td>
<td>5,885</td>
<td>6,631</td>
</tr>
<tr>
<td>GDP per capita, Atlas method (USD)°</td>
<td>1,900</td>
<td>2,340</td>
<td>3,160</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Poverty headcount, national poverty line**</td>
<td>38.7%</td>
<td>33.7%</td>
<td>27.4%</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Unemployment rate (% of total labor force)*</td>
<td>9.9%</td>
<td>7.7%</td>
<td>8.2%</td>
<td>10.4%</td>
<td>8.7%</td>
</tr>
<tr>
<td>Inflation rate, end of period*</td>
<td>14.3%</td>
<td>9.4%</td>
<td>14.2%</td>
<td>12.3%</td>
<td>13.3%</td>
</tr>
<tr>
<td>Net government lending/borrowing (% of GDP)*</td>
<td>0.5%</td>
<td>-4.8%</td>
<td>-10.8%</td>
<td>-10.1%</td>
<td>-7.6%</td>
</tr>
<tr>
<td>Current Account Balance (% of GDP)*</td>
<td>-15.0%</td>
<td>-31.5%</td>
<td>-32.6%</td>
<td>-27.9%</td>
<td>-22.1%</td>
</tr>
<tr>
<td>FDI Inflow (% of GDP)*</td>
<td>25.2%</td>
<td>53.1%</td>
<td>43.0%</td>
<td>18.5%</td>
<td>10.5%</td>
</tr>
<tr>
<td>Exchange rate, end of period (MNT/USD)***</td>
<td>1,257</td>
<td>1,396</td>
<td>1,392</td>
<td>1,659</td>
<td>1,824</td>
</tr>
</tbody>
</table>

Note: f=forecast. Sum may not add up to 100% due to rounding. Source:*IMF, **World Bank, ***IFC’s Economic Outlook Report

### Table 3: SME Definition in Mongolia as per SME Law in 2007

<table>
<thead>
<tr>
<th>ENTERPRISE CATEGORY</th>
<th>SECTOR</th>
<th>NUMBER OF EMPLOYEES</th>
<th>ANNUAL TURNOVER IN MNT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Small</td>
<td>All sectors</td>
<td>≤ 19 employees</td>
<td>≤ MNT 250 mln</td>
</tr>
<tr>
<td></td>
<td>Services</td>
<td>≤ 49 employees</td>
<td>≤ MNT 1.0 bln</td>
</tr>
<tr>
<td>Medium</td>
<td>Wholesale</td>
<td>≤ 149 employees</td>
<td>≤ MNT 1.5 bln</td>
</tr>
<tr>
<td></td>
<td>Retail / Manufacturing</td>
<td>≤ 199 employees</td>
<td>≤ MNT 1.5 bln</td>
</tr>
</tbody>
</table>

**World Bank (2012).
Nevertheless, it is observed that the SME definition introduced in 2007 is not widely used by industry stakeholders. For instance, commercial banks widely use their own segmentation criteria based on annual turnover and/or loan size. Even the National Statistical Office of Mongolia (NSO) uses a different employee number categorization in collecting its yearly business register data.\textsuperscript{14} The NSO does not produce data exclusively on SMEs. The statistics declared by the NSO cover all business entities in Mongolia, including large companies. In addition, NSO does not provide a breakdown for companies employing more than 50 employees. Therefore, this category includes not only SMEs, but also large corporations with a higher number of staff.

As of 2013, there were 99,603 registered establishments of which 54,929 were active (Table 4). Of all enterprises, 63\% are located in Ulaanbaatar. It is worth noting that although the number of registered enterprises increased by nearly 35\% from 2010 to 2013, the percentage of active ones remained the same at 55\%. It is also observed that the share of active enterprises out of the registered ones increased for all categories, except for the smallest segment with up to nine employees constituting 90\% of total registered businesses. This fact might indicate that enterprises with less than ten employees face severe challenges for growth.

According to the NSO, 38\% of active enterprises are engaged in wholesale and retail trade, repair of vehicles and household goods, 17\% in real estate and construction business and 17\% other businesses (Figure 2).

\begin{table}[h]
\begin{center}
\begin{tabular}{|c|c|c|c|c|c|c|}
\hline
 & \textbf{2010} & & \textbf{2013} & & \\
 & Registered & Active & \% & Registered & Active & \% \\
\hline
1-9 employees & 66,062 & 34,844 & 53\% & 90,270 & 46,347 & 51\% \textsuperscript{-2}\% \\
10-19 employees & 3,816 & 2,741 & 72\% & 4,300 & 3,789 & 88\% \textsuperscript{16}\% \\
20-49 employees & 2,568 & 2,186 & 85\% & 3,192 & 2,990 & 94\% \textsuperscript{9}\% \\
>50 employees & 1,349 & 1,180 & 87\% & 1,841 & 1,803 & 98\% \textsuperscript{11}\% \\
\hline
\textbf{TOTAL} & \textbf{73,795} & \textbf{40,951} & \textbf{55\%} & \textbf{99,603} & \textbf{54,929} & \textbf{55\%} \textsuperscript{0}\% \\
\hline
\end{tabular}
\end{center}
\caption{Registered versus active enterprises in Mongolia}

\textit{Source: National Statistical Office (2013), author’s calculations} \\

\begin{figure}[h]
\centering
\includegraphics[width=\textwidth]{figure2.png}
\caption{Active enterprise by economic activity}
\end{figure}

\textit{Note: Sum may not add up to 100\% due to rounding. Source: NSO (2013), authors’ calculations}

\textsuperscript{14} The NSO categorized into four groups per number of employees: 1-9; 10-19; 20-49 and above 50 employees. However, NSO does not link this segmentation to enterprise size (i.e. NSO does not classify them into micro, small, medium-sized and large enterprises).
There is no definition for women-owned enterprises generally accepted by governmental or financial institutions. NSO indicates that when running its yearly survey on enterprises’ registry status, it differentiates between male- and female-owned enterprises. However, no gender-disaggregated data was available upon request. Therefore, it is not possible to identify the share of women-owned SMEs in the total number of registered or active businesses. Still, the Enterprise Survey of 2013 found that 38.9% of firms in Mongolia have a female participation in ownership and that 36.6% employ a female top manager. While these figures are lower than for East Asian countries like China, they are higher than for other former Soviet countries like Russia (28.5%), Kazakhstan (28.3) or Azerbaijan (4.1%).

According to the stakeholder observations, a large number of small businesses and home-based one-person entrepreneurs are working informally. In particular, during the start-up phase (first two years), it is common for the businesses to remain informal in order to avoid tax issues and to get registered at the tax office only if the business is expected to be profitable. Businesses engaged in production and trade of hand-made wooden items (furniture, trinkets, etc.) as well as meat, leather, and cashmere products are more likely to remain informal.

Based on the observations of stakeholders interviewed, nearly 60% of the entrepreneurs engaged in informal activities are women. Hence, the share of women entrepreneurs can be assumed to be higher in the informal sector than in the formal sector. Due to lack of internal capacity, lack of adequate support as well as other constraints analyzed in more detail below, it is more common for women than for men to remain in the informal sector.

2.4 Doing Business in Mongolia

An environment conducive to SME development requires established economic, physical, legal and institutional framework within which SMEs operate. Mongolia ranked 76th among 189 countries in Doing Business 2014 report, an improvement of four ranks compared to the 2013 report. The report recognized three regulatory reforms that contributed to the improvement of the business environment from June 2012 to June 2013: (i) starting a business; (ii) dealing with construction permits; and (iii) getting electricity. Despite improvement, the latter remains one of the most problematic indicators for enterprises in Mongolia, along with trading across borders and issues of resolving insolvency.

According to new regulations, the requirements to have company statutes and charters notarized and to register the new company with the local tax office were eliminated. Furthermore, the requirement for a technical review of the building plans by the state for low- and medium-risk construction projects was removed, which made dealing with construction permits less complex. In addition, Mongolia made obtaining electricity easier by increasing the efficiency of the utility’s internal processes, enforcing time limits at different stages of the connection process, and eliminating the fees for testing the installation.

The country ranks poorly in trading across borders mainly due to its geographical isolation, distance from markets and underdeveloped infrastructure, especially in rural areas. The quality of overall infrastructure is very poor, which makes domestic and international transportation a major challenge. Various sources indicate that only about 10% of approximately 50,000 km of roads in Mongolia are paved, a majority of which are roads leading out of the capital city Ulaanbaatar. Roads are also impacted negatively by extreme weather conditions characterized by high temperature fluctuations in winter and summer, which impairs road quality and shortens the period of operational work on the roads.

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7 Ibid.
8 A typical informal business is “suitcase trading,” characterized with purchasing consumer goods from neighbouring countries and selling them locally.
9 Mongolia has improved its country ranking in “getting electricity” indicator of Doing Business Survey (moved from 171st in 2013 to 162nd in 2014) by increasing the efficiency of the utility’s internal processes, enforcing time limits at different stages of the connection process and eliminating the fees for testing the installation. The country however still underperforms in terms of number of procedures, time required (in days) and connection cost (% of per capita income) an entrepreneur must fulfill to get connected to the electricity.
Restricted access to energy sources, especially in rural Mongolia, is frequently cited as another problematic area for businesses. Although there has been some improvement in recent years, the country’s coal-power heat-supply system remains in poor condition. It is unable to meet the basic supply requirements of industrial and commercial enterprises, as well as that of the urban population. Power-system losses remain high and power cuts are frequent, interrupting manufacturing processes.

Resolving insolvency remains one of the worst among doing business indicators, standing at 133 in the ranking of 189 economies, worse than the regional average (108), China (78) and Russia (55). In the context of supporting viable and efficient businesses, insolvency system reforms are important; however they have not so far contributed to significant change.

Apart from the indicators mentioned above, interviews with key stakeholders and SMEs revealed further constraints. The high level of bureaucracy is one of the most widely cited factors responsible for impeding a more conducive environment for doing business. Interviewed stakeholders also point out a general perception of government officials as lacking adequate skills and up-to-date information required to satisfactorily perform their tasks. Some stakeholders also think that they are not service-minded and helpful to entrepreneurs. This stakeholders’ perception about government officials seems to be shared by SMEs as well, as nearly 37% of all male and 44% all female respondents indicated “government policy” to be the current challenge to their business.

Although business registry is not a major issue as far as the time to register a business is concerned, closing a business can be burdensome as the process requires the inspection of tax authorities, who usually act slowly. Difficulties pertaining to closing a business might be a reason for a relatively low share of active registered small enterprises (51%, up to nine employees as per NSO categorization, see Table 4). Businesses also suffer from poor enforcement mechanisms and lengthy legal proceedings. For instance, in case of a default, the value of property can be an issue of dispute between the debtor and the creditor, leading to court proceedings. Court procedure may take a long time as a consensus between parties is required on the selling value of the property under hypothec, for the property to be sold. Naturally, this is relevant not for SMEs only, but also for banks that face similar problems while dealing with property taken from clients in case of default.

Interviews with different stakeholders and the demand side analysis indicate that a significant portion of SMEs also suffer from shortage of skilled workforce. This is especially surprising for a country with a literacy rate as high as 98%. One reason for this discrepancy is the decreasing enrollment ratios and decreasing quality of education during Mongolia’s transition period between 1991 and 1998, a result of the lack of funding for schools as well as high dropout rates. Gross enrollment ratios dropped to 84% in primary schools and to 65% in secondary schools by 1995 (which were 98% in primary schools, 85% in secondary schools before 1991). High dropouts were especially observed in rural areas where many schools closed and among boys who had to dropout in order to support the families in income-earning activities, such as herding. As a result, between 1991 and 2004, the quality of education declined as the percentage of population reaching tertiary education - exactly at a time when the transition to a market economy called for highly skilled human resources.

The current situation seems to be putting significant constraints not only on SMEs, but also for large corporations operating in Mongolia. Some international institutions have initiated programs to address the issue

21 ADB (2008)
22 Leading to a dropout rate among boys of almost 70%, see Yembuu and Munkh-Erdene (2006).
23 In 2002, the Ministry of Education, Culture and Science mobilized additional funds to rehabilitate schools and dormitories in remote areas. Only after 2004, the dropout rates started to recover gradually after hitting 28%, 15%, and 11% for grade 1, grade 3 and grade 8 respectively. See http://www.unicef.org/mongolia/children_2579.html
of “low quality” experience across different sectors of activity. For instance, the Quality Supplier Development Center and the Quality Management Program launched by USAID are examples of these programs.

2.5 Legal and Regulatory Environment for SMEs

There are a number of laws in Mongolia regulating the operational environment for SMEs. The legal status of business entities was first stipulated in the Civil Code of Mongolia (adopted in January 2002), Article 33, which differentiates between types of legal persons based on establishment purpose. According to it, legal persons can either be “for-profit” or “non-profit” legal entities. While for-profit legal persons can be established in the form of partnership or company (Joint Stock or Limited Liability Company), non-profit legal persons can be established in the form of an association, foundation or cooperative.

Some laws have a direct impact on the business environment for SMEs and some others like the recently introduced Law on Investment (2013) seem to be of greater relevance for large corporate companies and/or foreign investors. Still, SMEs are indirectly impacted by changes in the business environment for large corporations as they are usually important buyers for SMEs. The following provides an overview of legislation directly and indirectly affecting SMEs:

- **Company Law (revised):** On 6 October 2011, the parliament of Mongolia adopted significant revisions to the Company Law of Mongolia. The revised Company Law came into effect on 21 November 2011. The aim of revising the law was to bring the corporate governance standards in Mongolia closer in line with those in more developed jurisdictions. The revised law required all companies to amend their charters before 1 July 2012 in order to reflect the changes. The key features of the revised Company Law are:
  - Broadening of the personal liability of governing persons.
  - Introduction of administrative sanctions for non-compliance.
  - Stricter corporate governance rules.
  - Abolition of minimum capital requirements for companies.

The revised Company Law will be binding for all companies operating within the territory of Mongolia, without regard to their ownership, the size of their property, the amount of their production, or their internal organization.

- **The SME Law:** The SME Law adopted in 2007 authorizes the government to undertake targeted interventions in the SME sector, such as provision of funds at below market rates. However, international experience shows that this measure can lead to weaker financial discipline at the SMEs and is not to the benefit of the SMEs and the national economy in the long run. It is worth noting that the interventions of the government remained unnoticed by the SMEs: around 40% of enterprises surveyed for this study still perceive the lack of adequate government policy as a challenge for their business.

In addition, the SME definition introduced by this law is unfit for the current environment (too broad in terms of employment size and outdated in terms of annual turnover due to 55% depreciation in MNT since the enactment of the SME Law). Many interviewed stakeholders indicated that a revision of the current SME definition is necessary.

- **Law on Investment:** In October 2013, the State Great Khural, Mongolia’s parliament, ratified a new investment law with the aim of altering the investment landscape and economic slowdown in Mongolia. Under the new Investment Law, which replaced the former Law on Foreign Investment, any domestic or foreign investor...
may invest in any industry or sector without any limitation or government approval (exception: requirement of approval by the newly established Invest Mongolia Agency in the case of foreign state-owned enterprises investing in more than 33% of stake in an entity in mining, communication or financial sectors). The law also stipulates that both foreign and domestic investors can take advantage of certain tax and non-tax benefits. Mongolia’s opening up to foreign investment and entry of international companies would make competition stronger and might have an adverse effect on SMEs in the short run. However, in the long run, this is expected to push inefficient/unproductive local firms to improve their methods of production and management, increase their productivity, and adopt innovative technologies.

Law on Credit Guarantee Fund: A law on establishing a Credit Guarantee Fund (CGF), a non-profit legal entity, was adopted by the Mongolian parliament in March 2012. CGF’s mission is to support the development of SMEs and start-ups, especially those facing problems in meeting collateral requirements imposed by commercial banks. Although official establishment of CGF took place in 2012, real activities were started in 2013 with the issuance of first guarantees on 1 June 2013. Operating not longer than a year, CGF still enjoys a 0% NPL rate.

Therefore, there are concerns in the financial sector that the CGF may soon turn into a “bad debt center”, unless revisions explicitly stipulating the case of non-repayment are introduced.

Law on Land: The Law on Land should be interpreted within the constitutional rule, which stipulates that all land in Mongolia is owned by the state. The only exception to this rule is that the state may allocate certain types of private ownership to Mongolians only. It came into force in 1994 and was revised in 2002. The Law on Land defines three different forms of land tenure:

- **Land ownership:** The right to exercise legitimate control over and to dispose of land.

- **Land possession:** The right to use the land him/herself or sub-lease to others. Pursuant to the Land Law, Mongolian citizens and entities can have the right to possess land for up to 60 years, to sub-lease, to transfer with the approval of the land authority, or to pledge it as collateral. The state, as the owner of the land, may grant possession rights over plots of lands only to Mongolian citizens and domestic companies. Foreign citizens and entities cannot obtain possession rights over land in Mongolia.

- **Land use:** The right to utilize the land in accordance with the contract made with the land owner (Mongolian state, citizens or entities) or the holder of land possession rights.

In most countries, real estate usually includes both the land and the building built on this land. Nevertheless, real estate ownership is considerably different in Mongolia and the term “immovable property” essentially refers to buildings and houses. Land is owned by the government, whereas the title to the land belongs to an individual holding possession rights. The building on top of the land may be owned by the land possessor but can also be owned by a third person. Further, the individual with the rights to use the land may be different than the land possessor. Because of this peculiarity of Mongolia, the precise legal definition for the ownership of immovable property is termed as “floating freehold.” It signifies that the property owners hold a freehold over the property, but not over the land on which it is built.

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26 With the revision of the Law on Land in 2002, Mongolian citizens have for the first time endorsed private land ownership.  
28 Jones Lang Lasalle (2013).
Therefore, land ownership is not subject to pledging. Although it is legally possible to pledge the land use (building on top) and land possession (land title) separately, commercial banks usually require the immovable property on a land to be pledged together with the land title, mostly due to deficiencies in the cadastral survey system and practical and legal problems associated with the seizure of it in cases of loan default.

Law of Mongolia on Registration of Immovable Property: This law states that ownership of immovable property and the rights and responsibilities associated with ownership, arise only on registration of the property at Immovable Property Registration Offices (which are located in aimag centers and in the capital, Ulaanbaatar). All transfers and collateralization of immovable property must be registered at an Immovable Property Registration Office.

Draft Bill on Tax Exemptions for SMEs (under discussion): In February 2014, the government initiated amendments to the Law on Value Added Tax (VAT), which was adopted in 1998 and has not been amended since. The aims of the amendments are to support SMEs in line with government’s strategic action plan for 2012-2016. The suggested amendments to the Law on VAT are the following:

- Increase of the VAT payer threshold to MNT 50 million (USD 28,000) from its current level of MNT 10 million (USD 5,500).
- For private individuals or small-scale legal entities willing to be registered as VAT payers, the threshold will remain MNT 10 million (USD 5,500).

The Ministry of Finance estimates that by increasing the threshold amount of the VAT, around 50% of tax payers and SMEs will be exempted from providing VAT tax returns. The draft bill also proposes an amendment to the Law on Income Tax for economic entities. The suggested amendments to the Law on Income Tax are:

- 90% of the amount of tax paid shall be paid back to those legal entities whose annual income does not exceed MNT 1.5 billion (USD 830,000).
- The new amendment does not apply to the legal entities operating in the following sectors: mining, minerals, petroleum products import, oil export, communications, alcoholic beverages and cigarettes production or distribution.

Draft Bill on Pledge of Movable Properties (under discussion): To address the issue of banks not accepting movable property as collateral, the Mongolian Bankers Association (MBA), the IFC and the European Bank for Reconstruction and Development (EBRD) initiated the much needed Secured Transactions Reform in Mongolia to create a legal framework that will ensure secure lending backed by movable collateral.

Secured Transactions Reform involves the creation of a nationwide registry for equipment, accounts receivable, inventory and other types of movable collateral. The registry will provide real-time information on priority interests against competing claims on the same collateral. As SMEs will be able to use more of their assets as collateral, the reform can contribute to increased access to finance. The initiative is funded and implemented by the European Union (EU), the Swiss State Secretariat for Economic Affairs, the EBRD and IFC.

The EBRD’s Legal Transition Team contributed to the reform through a technical assistance program by advising the Ministry of Justice on the draft secured transactions law and other important legal changes required. With respect to implementation, IFC is contributing to the initiative through technical assistance regarding setting up the registry and training lenders on best practices for movable collateral lending.

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29 MAD Research (2013).
31 Unlike many other countries applying a varying VAT rates for different type of products and services, Mongolia has a fixed VAT rate of 10%.
32 Fehrbach (2014).
33 EBRD (2012).
In March 2014, IFC signed a cooperation agreement with Mongolia’s Ministry of Justice to establish a proper legal framework for secured transactions through a new pledge law, to develop an online registry, and to work with the MBA to raise awareness and train industry professionals.\(^{34}\)

A draft Bill on Pledge of Movable Properties was already on the agenda of the cabinet of ministers. As a result of these consultations and technical assistance efforts provided by international institutions, the bill has been developed further by the Ministry of Justice to cover non-material properties. On June 2014, the Ministry of Justice stated that the cabinet decided to submit the Bill on Pledge of Movable and Non-Material Properties to the parliament. All kinds of stocks, shares, designs of products, trademark, creative works of sciences and arts, in addition to movable properties, can be subject to pledge. As to when the movable property pledge will take effect in Mongolia, this is subject to the introduction of a registration procedure that sets out the process for such registration. This would be a significant milestone in Mongolia’s legal framework for lending to SMEs.

**Legal and Regulatory Environment Related to Gender Equality**

Gender equality in legal framework matters for women’s economic opportunities, including access to finance and entrepreneurial activities. The Women, Business and the Law (2014)\(^{35}\), prepared by the World Bank, points out that those countries that were formerly under communist influence resulted in fewer gender differences in their legal systems. This is also the case for Mongolia, where national laws do not differentiate between men and women.

According to the Global Gender Gap Report of the World Economic Forum,\(^{36}\) in 2013 Mongolia ranked 33 out of 136 countries with a score of 0.72 (0 represents inequality and 1 represents equality). Mongolia ranked 1st and 2nd on “Health and Survival” and “Economic Participation” sub-indexes, whereas it underperformed in the “Political Empowerment” component of the overall score. To address the latter issue, the Mongolian parliament adopted the Law on Promotion of Gender Equality in February 2011. The aim of the law is to ensure the equal participation of women and men in all political, legal, economic, cultural, and social spheres. The law prohibits any form of discrimination in these spheres and in family relations. The law also states that gender-based violence and sexual harassment are forms of gender-based discrimination.

The National Committee on Gender Equality (NCGE) was subsequently established to be in charge of the daily activities of the implementation of the law. The NCGE is chaired by the prime minister and works through sub-councils in 16 ministries in Mongolia. It has sub-committees in Ulaanbaatar’s nine districts and 21 aimag centers. The mid-term strategy and action plan on implementation of the law was launched in 2013 for a period covering 2013-2016. The NCGE also initiated the submission of a Draft Bill on Labor Relations to align women’s employment conditions with benchmarks set by the Promotion of Gender Equality Law.

Various other laws, such as the Mongolian constitution, labor law, criminal code, civil code, and family law, contain provisions to promote gender equality. Despite these provisions, the lack of enforcement mechanisms prevents full implementation in some problem areas like domestic violence. According to the 2010 U.S. State Department Report on Human Rights Practices, there are 40 women’s rights service and advocacy groups in Mongolia dealing with issues of maternal and child health, domestic violence, and equal opportunity. In practice,
however, domestic violence is still reported to be a serious problem for women in Mongolia. The parliament adopted a Domestic Violence Law in May 2004. Nevertheless, the law on domestic violence is deemed insufficient because of lack of deterrent measures, inadequate victim protection, and the lack of legislation that would specifically prohibit spousal rape.37

Right to property ownership is a crucial factor in accessing to finance and SME development. Under constitutional law, the civil code and the Law on Land, women and men in Mongolia have equal rights to access to land and they are treated equally as far as inheritance of movable and immovable property is concerned. The family code also stipulates that all property and savings, acquired by the spouses during the marriage shall be deemed the common joint ownership of spouses. However, the common public practice is to have the immovable property title issued under the household head’s name, which is traditionally a man.

2.6 Support Institutions for SMEs and Women Entrepreneurs

Mongolia has recognized the potential of SMEs and has established several programs to support SMEs in the terms of funding and capacity building. The Ministry of Labor (MOL) assumes the overall regulatory role. The SME Development Department unit at the MOL is the only department authorized by law to undertake the regulatory changes relevant for SMEs.

On behalf of the government, the MOL so far has initiated two large-scale national programs for the development of SMEs. While the first program implemented between 1999-2004 prioritized issues related to infrastructure, the second program, launched in 2006 and accomplished in 2012, focused upon enhancement of the legal and policy framework, in particular the law on SMEs, Law on Legal Status of Industries, Law on Science and Technology and the Law on Credit Guarantee Fund enacted in this period. Other programs launched by MOL were the SME support program and SME support fund, providing training through public bodies and loans at below-market rates through commercial banks.

Furthermore, international agencies and NGOs provide various kinds of support to Mongolian SMEs and initiated a series of programs combining capacity building activities and financial support. Some of the support programs are listed below (see also Annex B):

SME Development Center of Capital City operates as a government body for the provision of financial and non-financial services to the SMEs located in Ulaanbaatar. The center’s activities fall under the mayor’s office, which can run programs independently of the central government, but has to comply with general regulations. The center has nine branches in each of the sub-districts in Ulaanbaatar and organizes trainings and mobilizes concessional funding for SMEs.

The Mongolian National Chamber of Commerce and Industry (MNCCI) is one of Mongolia’s leading NGOs. Currently, MNCCI has expanded to include 3000 members (1000 in Ulaanbaatar) and be represented by 20 subsidiary branches in the countryside, hence reaching out across the country. MNCCI’s foremost support to SMEs is in the field of information dissemination, preparation of business plans, organization of trainings and networking events as well as facilitation of business advisory services through experts.

Business Professionals Network (BPN) was established by the Swiss Agency for Development and Cooperation to support Mongolian craftsmen (most of whom own start-ups) on their way to become businesses through trainings, seminars and coaching. BPN

37 The National Center Against Violence (NCAV) estimated that in 2010 one in three women was a victim of domestic violence. Rural populations face the worst domestic violence rates due to a lack of shelters and funding for services and public belief that domestic violence is a private family matter. http://www.stopvaw.org/

38 The Mongolian National Chamber of Commerce and Industry was founded on July 1, 1960 as the “Chamber of Commerce”. Since 1990, MNCCI established itself as a Mongolia’s leading NGO devoted to the development of trade and investment in Mongolia’s business community.
has recently been registered as an NBFI and also provides funding, but the size and scope of its funding is very limited.

SME support institutions in Mongolia usually do not differentiate between male and female entrepreneurs at the program level and women are eligible to apply for capacity-building measures implemented by those institutions. Women-only support programs are provided through a number of NGOs that exclusively address problems faced by women. One of these institutions is the Mongolian Women’s Fund.

**Mongolian Women’s Fund (MONES)** is engaged in raising funds to be disbursed as grants to women involved in small-handicrafts manufacturing. Given the scope of its activities and target group, MONES can be categorized as an NGO supporting micro, women-entrepreneur start-ups.39

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39 Detailed information on activities performed by different NGOs and SME support institutions (only the ones who could have been interviewed) can be found in Annex B.
3. Supply of SME Finance

3.1 Overview of the Financial Sector

The financial sector of Mongolia is a two-tier system, comprising the Bank of Mongolia (BOM) acting as the central bank on the first tier and commercial banks, NBFIs, and SCCs on the second tier.

Mongolia’s financial sector is dominated by banks; NBFIs and credit and savings cooperatives only hold a fraction of sector’s assets. The BOM and Financial Regulatory Commission (FRC) are responsible for financial stability and supervision of the financial sector in Mongolia. The BOM is responsible for supervision of banks, while the FRC is responsible for supervision of other financial institutions including NBFIs, SCCs, insurance companies, and securities firms.

3.1.1 Commercial Banks

There are currently 13 commercial banks in Mongolia (one public and twelve privately owned). The largest five banks (Khan Bank, Trade and Development Bank, Golomt Bank, XacBank, State Bank) make up around 90% of the total deposits and 85% of the total loans in the system. The 14th bank in Mongolia is the Development Bank of Mongolia (DBM) established by the government. The DBM, officially opened in May 2011, has a broad development mandate and is expected to focus on infrastructure and social housing projects. It is independent of the BOM and supervised by the Ministry of Finance.

<table>
<thead>
<tr>
<th>INDICATOR</th>
<th>2012</th>
<th>% IN TOTAL ASSETS</th>
<th>2013</th>
<th>% IN TOTAL ASSETS</th>
<th>2014/Q1</th>
<th>% IN TOTAL ASSETS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Asset Size</td>
<td>11,992</td>
<td>100%</td>
<td>20,884</td>
<td>100%</td>
<td>20,708</td>
<td>100%</td>
</tr>
<tr>
<td>Loans Outstanding</td>
<td>6,941</td>
<td>57.9%</td>
<td>10,716</td>
<td>51.3%</td>
<td>11,332</td>
<td>54.7%</td>
</tr>
<tr>
<td>SME Loans</td>
<td>N.A.</td>
<td></td>
<td>1,805</td>
<td>8.6%</td>
<td>1,853</td>
<td>8.9%</td>
</tr>
<tr>
<td>Loans for Individuals (Mortgages included)</td>
<td>N.A.</td>
<td></td>
<td>3,804</td>
<td>18.2%</td>
<td>4,166</td>
<td>20.1%</td>
</tr>
<tr>
<td>Total Deposits</td>
<td>4,886</td>
<td>40.7%</td>
<td>6,355</td>
<td>30.4%</td>
<td>7,150</td>
<td>34.5%</td>
</tr>
<tr>
<td>Government Deposits</td>
<td>933</td>
<td>7.8%</td>
<td>1,186</td>
<td>5.7%</td>
<td>1,535</td>
<td>7.4%</td>
</tr>
<tr>
<td>Equity</td>
<td>986</td>
<td>8.2%</td>
<td>1,381</td>
<td>6.6%</td>
<td>1,537</td>
<td>7.4%</td>
</tr>
<tr>
<td>NPL</td>
<td>293</td>
<td>4.2%</td>
<td>564</td>
<td>5.3%</td>
<td>593</td>
<td>5.2%</td>
</tr>
<tr>
<td>Loan to Deposit Ratio</td>
<td>99%</td>
<td></td>
<td>169%</td>
<td></td>
<td>158%</td>
<td></td>
</tr>
</tbody>
</table>

Note: All figures in billion MNT. Source: Bank of Mongolia, authors’ calculations.
The banking sector was highly affected by the financial crisis during 2008 and 2009, leading to problems in recoverability of loans and a significant increase in impairment provision rates. The high level of inflation resulted in negative real interest rates on local currency deposits. The fourth largest bank at that time, Anod Bank, was taken under BOM conservatorship and public confidence in the banking sector has bottomed.

To stop withdrawal of deposits from banks and to restore public trust, the government issued a blanket deposit guarantee on all commercial bank deposits in November 2008, which has phased into a limited deposit insurance scheme in January 2013. With the enactment of the Law on Insurance for Bank Deposits, only a portion of up to MNT 20 million of all deposits (around USD 11,000) is currently covered. According to the EBRD country assessment report in 2013, this provision implies full coverage for over 99% of individual depositors, and coverage of 20% to 30% of total bank deposits.40

Since 2009, the banking sector has consolidated and stabilized, and bank lending has grown rapidly in the last few years. However, the growth in lending has not been broad based and was more visible at the household and corporation level. Household lending especially picked up in 2013 with the introduction of the housing development program by the government comprising a MNT 1,200 billion subsidized mortgage lending (with 8% p.a.) via commercial banks. About 45% of total individual loans are mortgage loans, most of which disbursed within the government’s housing development program.

As a result, while corporate and individual loans reached 47% and 37% of the total loan book respectively, SME loans remained at 16% (about 1800 billion MNT) revealing a low level of commercial-bank penetration (Figure 3).

As of the first quarter 2014, there are 1,455 commercial bank branches across Mongolia, 29% of which are located in Ulaanbaatar. Khan Bank and Savings Bank have 73% of all branches countrywide and also have a significant presence in rural areas. Most of their branches are located outside Ulaanbaatar (Table 6).

Access to financial services in Mongolia appears to be relatively high when measured by the demographic penetration of branches. According to the IMF,41 Mongolia has one of

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40 EBRD (2013a).
the highest bank-branch penetration rates in the world, with 69 branches per 100,000 adults compared to 38 in Russia, seven in China, 1.6 in the Kyrgyz Republic, and ten in Azerbaijan. However, due to its large territory, Mongolia’s geographical branch penetration is one of the lowest in the world. It has only 0.9 branches per thousand km², compared to three in Russia, nine in China, eight in the Kyrgyz Republic, and ten in Azerbaijan.

The low population density makes the provision of traditional banking services outside of the large cities costly. Loan and deposit penetration is high as well. There are 302 bank loan accounts per 1,000 adults, compared to 489 in Georgia and 34 in Cambodia. There are also more than 3,829 deposit accounts per 1,000 adults, compared to 1,074 in Georgia and 145 in Cambodia. While some of the high number of deposit accounts can be explained by people using multiple accounts with different banks (see below), a high and increasing deposit to GDP ratio (67% in 2012, 60% in 2011) indicate a strong saving culture in Mongolia. However, due to financial market development and economic growth during the past years, the importance of borrowing has also increased.

Mongolian banks predominantly offer loans, deposit and savings products, and some trade financing (for instance foreign trade collection services, letter of credit, and export and import support loans jointly offered by Export/Import Banks of other countries) to SMEs.

There is no factoring, and leasing is usually offered via commercial banks’ subsidiaries. But leasing industry can still be considered underdeveloped given its size and the scope of the financing provided. Insurance services are delivered at bank branches in collaboration with a range of insurance companies. Overdraft facilities, which can be initiated for clients with an existing credit line, are not available. Start-up finance is very rare and banks refrain from extending finance to enterprises lacking credit histories and business experience. The table below summarizes the loan products offered to SMEs.

**TABLE 6: COMMERCIAL BANKS’ BRANCHES IN AND OUTSIDE ULAANBAATAR**

<table>
<thead>
<tr>
<th>Bank</th>
<th>Number of branches in UB</th>
<th>Number of branches in aimags</th>
</tr>
</thead>
<tbody>
<tr>
<td>Khan Bank</td>
<td>98</td>
<td>432</td>
</tr>
<tr>
<td>Golomt Bank</td>
<td>63</td>
<td>41</td>
</tr>
<tr>
<td>Trade and Development Bank</td>
<td>35</td>
<td>13</td>
</tr>
<tr>
<td>State Bank</td>
<td>93</td>
<td>438</td>
</tr>
<tr>
<td>XacBank</td>
<td>51</td>
<td>53</td>
</tr>
<tr>
<td>Chinggis Khan Bank</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Ulaanbaatar City Bank</td>
<td>25</td>
<td>0</td>
</tr>
<tr>
<td>Capitron Bank</td>
<td>13</td>
<td>16</td>
</tr>
<tr>
<td>Transport and Development Bank</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>Credit Bank</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>Capital Bank</td>
<td>33</td>
<td>32</td>
</tr>
<tr>
<td>Erel Bank</td>
<td>7</td>
<td>2</td>
</tr>
<tr>
<td>National Investment Bank</td>
<td>4</td>
<td>2</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>425</strong></td>
<td><strong>1,030</strong></td>
</tr>
</tbody>
</table>

*Source: Bank of Mongolia, data as of 2014 Q1*

42 Ibid, figures as of 2012.

43 In Georgia this indicator reached 26% in 2012, in Cambodia 36%.

44 The table was compiled by the authors by combining the data from the questionnaires filled out by several banks.
The infrastructure for electronic payments is growing fast, but remains underdeveloped outside Ulaanbaatar. About 70% of the population in urban areas uses ATMs as the main channel for withdrawals, compared to only 30% in rural areas. New technologies, such as internet banking but especially mobile banking, are growing fast, given the rapid increase in mobile phone users.45 Smart banking services, such as accessing bank services via iPhone, Android or Blackberry, have also grown rapidly as smart phones are increasingly replacing ordinary mobile phones. Smart phone users can easily access their accounts, check their balance, conduct interbank and inter-account transactions, and realize foreign currency transactions and bill payments.

Some banks, especially the ones with a larger market share, have also initiated a number of non-financial services to SMEs46. The most widely known of these services are:

- Sponsorships to annual gatherings, conferences, and trade fairs organized by various sectors that help industry representatives in networking.
- Initiating training, information sharing and networking events for some selected industries.
- Providing business advisory services.
- Organizing financial literacy trainings, also in rural areas.

Commercial banks do not currently collect gender-disaggregated data at the institution level. However, there are some banks that have collected such data on specific programs. For instance, the data collected by one of the large commercial banks in the Wool, Cashmere, Sewing lines, Green House and Intensive Farming Projects, implemented jointly with the Development Bank of Mongolia, the Ministry of Economic Development and the Ministry of Food and Agriculture, shows that about 60% of all loan beneficiaries have been women. Nevertheless, it is still difficult to estimate the overall share of women-owned SMEs given the lack of gender-disaggregated data at the industry/institution level.

Interviews at commercial banks revealed that women are not perceived by the banks as a distinct segment with specific needs. The banks do not disaggregate their SME client data based on gender. The Management Information Systems (MIS) in banks are also not suitable for gender-disaggregated data and need to be upgraded through further investments.

Some banks interviewed stated that they are currently negotiating internally about the development of their own definition for women-owned SME. For instance, one bank mentioned that it has recently prioritized women entrepreneurs as a distinct segment. A women-owned company is defined as a company with the women holding at least 25% of the company

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45 World Bank (2012).
46 More information on non-financial services offered by the banks can be found in Annex B.
shares, or having women at the CEO position. In general, commercial banks do not have specific products/services exclusively offered to women-owned SMEs. However, women-owned businesses are offered the same range of products and services, including trainings, provided to all SME clients.

3.1.2 Non-Bank Financial Institutions

The NBFIs provide a variety of financial services such as loans, payment guarantee, currency exchange, money transfer, remittances, factoring, leasing, short-term investment, trust funds, and electronic payments. However, all NBFIs do not necessarily provide the full range of services. Services to be delivered by each NBFI are determined according to the type of license granted by the FRC.

The number of NBFIs in Mongolia is increasing rapidly. According to the figures provided by Mongolian Non-Banking Financial Institutions Association, there are 303 NBFIs as of May 2014, of which 40 were established after December 2013. The number of companies granted an NBFI license is expected to increase further as it is very easy in Mongolia to become accredited as an NBFI. This surprising rate of expansion in the number of market players creates some concerns, especially for prominent industry players. Interviews conducted during this research revealed that larger NBFIs are concerned that establishment of many small NBFIs with limited resources and no tangible activities might have a negative impact on the whole industry. It is important to note that despite the rapid increase in number of NBFIs, their share in financial system in Mongolia remains marginal (2% of total assets, Figure 4).

To address that potential threat, important market players are pushing the FRC to increase the minimum required capital of an NBFI from MNT 400 million to MNT one billion. The minimum capital requirement of MNT 400 million was agreed five years ago and is now outdated due to depreciation of the local currency in the last two years. However, FRC has so far not given any signal that it might act accordingly.

According to FRC statistics, most NBFIs are located in the vicinity of Ulaanbaatar and only 35 of them are in rural areas. The sector’s aggregate loan portfolio as of 2014 Q1 is MNT 245 billion (~USD 136 million) extended to a total of 288,000 clients; the average loan per client is MNT 850,000 (less than USD 500).47 Interviews with two of the ten largest NBFIs, however, revealed that the average loan size for

**FIGURE 4: DEVELOPMENT OF THE NBFI SECTOR**

![Graph showing development of the NBFI sector](source: Mongolian NBFI Association, Bank of Mongolia, researchers’ calculations)

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47 Information received during the interview with FRC.
the industry leaders is approximately MNT 20 million (~ USD 11,000). While FRC statistics points to 4.5% (as of 2014 Q1) aggregate NPL for the NBFI sector, some prominent NBFI with a larger average loan amount per client state that bad loans take up around 7% to 8% in their portfolios.

NBFI loans have a maturity of up to two years with average interest rates ranging from 3.5% to 4% per month, almost the double of the interest rates charged by banks. Industry observers indicate that despite the much higher interest rates charged by NBFI, they are sometimes preferred by borrowers over banks because of quicker and more efficient loan decision processes and looser collateral requirements. Whereas banks very seldom accept movable property as collateral and mostly in combination with immovable property, NBFI offer loans backed by movable property.

Funding is a big challenge for NBFI as their access to special funds provided by international or governmental organizations is limited. Borrowing from commercial banks comes at a cost and it is not always guaranteed because of banks’ reluctance to lend to NBFI. By law, NBFI are not authorized to collect deposits, but their “trust services” can be considered as a by-product for customer deposits, and abides by law. A “trust contract” is an agreement between an NBFI and an investor about a fixed amount investment into the NBFI for at least one year. The NBFI usually pays the investor a set amount of interest, typically monthly, with a return of capital at the end of the investment term. These trust agreements carry a higher return than bank deposits, but are beyond the scope of the deposit insurance scheme adopted for bank deposits.

Similar to the banking sector, with only a few exceptions (Net Capital, VisionFund Mongolia), NBFI in general also do not collect gender-disaggregated data on SME borrowers. Interviews with some selected NBFI revealed that close to 60% of their clients are women, with the exception of vehicle loans. Although there is no supporting statistics because of the unavailability of a central register for movable assets, stakeholders stated that nearly 70% of vehicles in Mongolia belonged to men and that men usually pledge their car as collateral.

3.1.3 Savings and Credit Cooperatives

According to FRC, there are close to 200 SCCs in Mongolia having an asset size of about USD 40 million in total. Regarding their asset size, SCCs have less than 0.5% share in Mongolia’s financial sector. There are 58 cooperatives in Ulaanbaatar, constituting 75% of total assets at SCCs. In other words, the majority of SCCs are in rural areas, but their scale is almost negligible in the Mongolian financial system.

SCCs serve about 27,000 customers, most of which are low-income rural households. Similar to NBFI, SCCs are licensed, regulated, and supervised by the FRC. The services provided by SCCs are: loans (only to members), payment guarantee, currency exchange, remittances, factoring, leasing, short-term investment, trust funds, and electronic payments. According to the Mongolian Confederation of Credit Unions, most members of SCCs are women. SCCs clients mostly work in the informal sector and have no capacity to borrow at banks or NBFI.

3.2 Programs of International Institutions Targeting SMEs

International Finance Corporation (IFC): IFC provides equity, loans, and trade financing to Mongolian banks to help them increase capital and boost lending to SMEs. It supports the development of Mongolian industries by directly investing in companies with high growth potential, or reaching out to SMEs through loans made available to commercial banks. IFC further provides advisory services to companies, banks and governmental institutions. Advice provided by IFC ranges from best governance practices, international social and environmental standards, regulatory environment and legal
reforms to banking services, such as trade, SME and housing finance, mobile banking, etc.

IFC continues to pursue new investment opportunities, mostly for SMEs involved in agribusiness, logistics, retail, building materials, and manufacturing. Together with the EBRD, IFC invested USD 7.5 million in the first Mongolian private equity fund for small and medium businesses.\(^48\) Going forward, IFC seeks to make strategic investments in insurance, investment banking, and leasing.

**Asian Development Bank (ADB):** Since Mongolia joined the ADB in 1991, ADB has been Mongolia’s largest source of multilateral official development assistance. From 1991 to 2013, Mongolia received 56 loans totaling USD 1,084.6 million, 171 technical assistance projects amounting to USD 100.6 million, 12 concessional Asian Development Fund grants for USD 172.2 million, and 17 Japan Fund for Poverty Reduction grants (USD 33.9 million). The ongoing portfolio, as of 2014, consists of 14 loans (USD 393.9 million), ten grants (USD 146.3 million), and technical assistance in 22 projects (USD 23.6 million).\(^49\)

**European Bank for Reconstruction and Development (EBRD):** Mongolia became an EBRD country of operation in October 2006. Prior to 2006, the bank’s activities in Mongolia were limited to technical assistance programs funded by donors. From 2006 to 2012, the bank signed 52 projects in Mongolia including debt, mezzanine, equity finance and trade finance guarantee facilities for an aggregate amount of EUR 690 million. During the same period, the bank committed EUR 14.6 million in technical cooperation programs through its Legal Transition Program, Enterprise Growth Program, Business Advisory Services and other programs.

According to EBRD’s strategy, the bank will continue to provide support to privately owned manufacturing and service companies in the following sectors: cashmere and wool production, construction materials and pharmaceuticals, agribusinesses, property development and tourism.\(^50\)

**Japan International Cooperation Agency (JICA):** The JICA, financed by the Japanese state, expanded to Mongolia in 1990. Since then, Japan has been one of the most important donors to Mongolia. In April 2012, a new program was approved by the government of Japan. JICA’s activities in Mongolia can be grouped in three categories:

- **Sustainable Development of the Mining Sector:** works on the master planning level and aims at improving productivity and efficiency in the Mongolian mining sector.
- **Enhancement of Ulaanbaatar as an urban center:** aims at improving the infrastructure and focuses on urban planning as well as management.
- **Assisting Inclusive Growth (within which the SME activities fall):** with the aim of increasing employment opportunities and meeting basic human needs.

Activities in the third category of operation comprise training and capacity building activities to SMEs as well as funding. An important program introduced by JICA in 2006 is the Two-Step Loan Project for SMEs Development and Environmental Protection. The aim of the program is to provide long-term funding through Mongolian commercial banks to SMEs. In the Two-Step Loan Program, the Japanese government provides a concessional loan to the Central Bank of Mongolia, which extends it to commercial banks to be on-lent to SMEs. In the two phases of the program, USD 13 million and USD 50 million respectively have so far been disbursed to final beneficiaries.\(^51\)

\(^{48}\) Information gathered from IFC’s website, Mongolia country page; http://www.ifc.org/wps/wcm/connect/region__ext_content/regions/east+asia+and+the+pacific/countries/ifc+in+mongolia
\(^{49}\) ADB (2014).
\(^{50}\) EBRD (2013b).
\(^{51}\) Detailed information about JICA’s and USAID’s activities in Mongolia can be found in Annex B.
United States Agency for International Development (USAID): USAID initiated the Business Plus Initiative (BPI) in Mongolia, which is a finance and capacity-building program composed of two sub-initiatives both aiming at improving quality standards at SMEs and in the general business environment in Mongolia. These two sub-initiatives are:

- Quality Supplier Development Center providing support to SMEs by linking them with buyers through a contract-based relation.
- Quality Management Program providing high-level professional trainings to SMEs delivered by international trainers.
4. Demand Study

4.1 Objectives and Methodology of the Demand Study

A demand survey to analyze the profile of entrepreneurs and their businesses as well as the demand for financial and non-financial services was carried out in June-July 2014. In total 240 interviews were conducted with 121 female entrepreneurs (target group) and 119 male entrepreneurs (control group) in three cities of Mongolia (Table 8). The key criteria for the target/control group for the interviews were the share of the ownership and distribution of management responsibilities in the business. The respondents had to be either majority owner of an SME (more than 50% share) or had to own a share of 20-50% and have management responsibilities at the same time. The definition of SMEs assumed for this study is based on the World Bank SME definition.\(^{52}\)

A sampling approach was used in order to identify survey respondents using a stratified method of sampling.\(^{53}\) The sample population (database of 45,000 registered SMEs) was stratified by gender and city allocation. Then the random sampling from database based on excel-based software was applied to each stratum. The face-to-face interviews were with randomly chosen entrepreneurs, who were contacted by phone to arrange the interview or visited on-site. In cases where the selected companies were not reachable, refused to participate, or were out of operation, the nearest company within a radius of 50 m was contacted. All interviews were conducted by professional researchers and in Mongolian. The questionnaire consisted of 68 questions.

The following analysis of the dataset starts with profiling the entrepreneurs and the businesses. Afterwards, the start-up phase and current challenges are analyzed before access to finance and the relationships to banks are further examined. In particular the current use of financial services and the demand for loans and expectations and caveats of banks are of interest. Of special interest are differences between men and women-owned SMEs as well as between SMEs in Ulaanbaatar and in Darkhan and Erdenet.

| TABLE 8: SAMPLE DISTRIBUTION PER GENDER AND CITY AND RESPONDENT RATE |
|----------------------------|--------|--------|--------|--------|
|                           | ULAANBAATAR | DARKHAN | ERDENET | TOTAL  |
| Male                      | 62      | 30     | 29     | 121    |
| Female                    | 58      | 30     | 31     | 119    |
| Respondent Rate           | 53%     | 24%    | 45%    | 44%    |

Note: The respondent rate is weighed by type of respondent selection and conducted interviews.

\(^{52}\) The World Bank SME definition includes the following criteria: number of employees, total assets and total annual sales. For the purposes of this study we used the criterion “number of employees”: (i) microenterprises < 10 employees, (ii) small enterprises 10 < 50 employees, and (ii) medium enterprise 50 < 300 employees.

\(^{53}\) Stratification is the process of grouping members of the population into relatively homogeneous subgroups before sampling.
4.2 The Entrepreneur

The typical entrepreneur in Mongolia is 43-years-old, has a university degree, is married, and lives together with his/her spouse, one young child and one other person, usually an older child. Female entrepreneurs are on average 46-years-old (Figure 5), older than male entrepreneurs (41-years-old). There is no difference in educational status. In total, 76% of Mongolian entrepreneurs have a university degree and 10% have technical or vocational education (Figure 6).

Most entrepreneurs are married or in a partnership: 83% of women, 80% of men.\(^{54}\) The spouse of the entrepreneur will usually also work, most likely as an employee in another company; but in 36% of the cases he or she works in the same company. In most of these cases (78%), the company is managed by both partners and critical business decisions are made together, regardless of formal ownership.\(^{55}\) Hence 23% of the companies of this sample can be classified as family businesses.\(^{56}\)

Family businesses have, with 4.4 members, the largest household and, with 1.2, also the most (young) children (Figure 7). Enterprises that are owned and managed solely by women have the smallest household size, with 3.6 members. One reason for the smaller household size might be

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\(^{54}\) In Mongolia a registered partnership is a legal civil status with rights and duties similar to a marriage.

\(^{55}\) Of the remaining 15 companies, 14 are classified as man-owned and operated, and one as woman-owned and operated.

\(^{56}\) In the following analysis, the companies are classified as man-owned (41% of the sample), woman-owned (36%) and family business (23%).
that 25% of women entrepreneurs in the sample are divorced/separated or widowed (Figure 8). While these women will naturally manage their businesses by themselves, there are also married women entrepreneurs who make their own decisions and run their business without their spouse’s involvement. This suggests that women entrepreneurs are to a high degree independent in managing their businesses.

4.3 The Business

4.3.1 Business Activities

Mongolian SMEs are typically engaged in a variety of business activities. Of the sample enterprises, 25% are engaged in two or more sectors. This is the case for 40% of family-owned and 17% of women-owned businesses. Of total business activities, the services sector dominates with a share of 47% (Figure 9), followed by trade (wholesale and retail: 22%) and production (16%). Women-owned businesses are more often engaged in services and trade and less often in production and other sectors (in particular construction) than men-owned businesses (Figure 10). This finding correlates with the evidence from different countries that indicate that women prefer to start their business in sectors where women employment is concentrated. The majority of businesses (77%) sell their products or services directly to end-customers; only 11% sell their products or services to retailers or wholesalers. The remaining businesses supply industry (6%) or the public sector (5%).

A high share of businesses is engaged in seasonal activities. In agriculture and mining, the share is above 50%; in production and construction it is more than 40% (Figure 11). Retail trade and services are less often seasonal: this applies to 22% and 31% of the businesses, respectively. In accordance with business activities, women-owned enterprises are the least often engaged in seasonal business activities (26%) compared to men-owned (34%) and family businesses (43%) (Figure 11). Following the assumption that non-seasonal businesses are associated with less risk for the creditor, it can be concluded that women-owned businesses seem to be more risk-averse compared to other types of businesses.

57 On average, an enterprise is engaged in 1.3 different sectors, with family businesses being engaged in 1.4 sectors and woman-owned SMEs in 1.2 sectors.

58 An enterprise is classified as active in a seasonal business if it has more than double as many employees during the season than during non-season.
4.3.2 Characteristics of the Business

In accordance with the sampling methodology and the law,59 87% of the businesses are registered as a limited liability company (LLC). For 10% of the companies, the owner is fully liable, whereas only five companies in the sample are registered as an association and one as a cooperative.60 No company was registered as a joint stock company as this legal form is more common for corporations.

The average number of employees of SMEs in the sample is 7.5 employees in season and 4.5 in non-season. Thus, 76% of the enterprises in the sample fall in the category of micro enterprises (one to nine employees) and 24% in the category of SMEs61 according to the definition assumed for this study based on the World Bank SME definition. Women-owned businesses are on average smaller than men-owned businesses with family businesses being in the middle (Figure 12). However, women-owned businesses employ more women (other than themselves): 52% of their employees are women, compared to 32% of men-owned enterprises. Also family businesses employ more women other than the owner or spouse, but tend to release them during non-season. The average woman-owned business employed 13% more employees during last year (man-owned: 20%, family business: 15% in 2013).

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59 To be eligible for this survey, businesses had to be registered. Businesses can either register as Limited Liability Company (LLC), association, cooperation, sole entrepreneur with liability, or Joint Stock Company.

60 By law a company can be registered as an association if it has at least five persons as owners and as a cooperative if at least nine persons are owners.

61 These figures differ from the official numbers from Table 3. The reason is that numbers of employees fluctuate during the year. For this sample, number of employees during the season has been used.
The sector with the most employees on average is construction, followed by production and agriculture (Figure 13). Retail trade has the lowest number of employees. However, every second employee is a woman. The service sector also employs a high share of women (52%), whereas in wholesale trade (35%) and mining (17%) the figures are lowest.

Growing sectors in number of new employees are in particular construction (+23%) and production (+18%), followed by retail trade (+16%) and services (+17%). Due to the high number of businesses engaged in the services sector, services generate in absolute number the most new employment. In mining there have been on average no new employees engaged during the period of last year.

Most companies were established before the financial and economic crisis in 2009. Of men-owned companies, 57% are older than five years, whereas 60% of women-owned companies are of the same age (Figure 14). Family businesses tend to be even older with a share of 73% being established before 2009. The number of enterprises that have been founded in the last two years (start-ups) is considered low (12.5%, taking into account that the economy has experienced growth rates of above 10% p.a. during the same period.)
Engaging a lower number in employees, women-owned businesses are also smaller in terms of turnover: 63% of these had a turnover of less than MNT 50 million in 2013, while the same figure was reported by 45% of men-owned and 42% of family businesses (Figure 15). Further, women-owned businesses are also less present in the middle segment and with companies with more than MNT 500 million in turnover. Family businesses are more often represented by companies with a turnover of MNT 50 to 250 million. Similarly, companies active in construction have the overall highest turnover (Figure 16), followed by production – in both sectors men-owned businesses and family businesses are more represented. Businesses active in the trade and services sectors, where women are more often active, typically have a smaller turnover.

In the sample 31% of all businesses can be classified as growing. Businesses that grew during the last twelve months in terms of employing new people also had a higher turnover than businesses that did not employ new personnel (Figure 17). Growing businesses in the sample already have a higher turnover than average and can increase it further. They are more often found in production and construction and less often in trade related activities (Figure 18). Of men-owned businesses, 36% are on a growth path, but also 25% of women-owned businesses are growing faster than the average women-owned company.

Note: A business is classified as growing if it employed two or more new employees in 2013.

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62 Here a growing business is defined as a business which employed at least two new employees within the last twelve months.
Businesses were further asked how they foresee their turnover to develop during the next two years. Overall entrepreneurs are optimistic with more than 50% stating that their turnover will increase. Female entrepreneurs are slightly less optimistic than male entrepreneurs and a higher share foresees a decrease (13% compared to 5% in case of male entrepreneurs) in turnover. The most promising sector is construction with 67% of enterprises foreseeing growth, followed by services with 54%. Most pessimistic is the trade sector with about every fifth enterprise expecting a decrease in turnover.

4.4 Challenges for SMEs

4.4.1 Start-up

As Mongolia is a country that has run a free-market system for less than 25 years, the majority of businesses have been established by the current owners; only a negligible number have been bought or inherited. To finance the business establishment from the ground, entrepreneurs mostly use their own or family savings (Figure 19). Very few start-ups obtained financing from banks. Gender-specific differences in terms of sources of start-up financing are marginal, with women entrepreneurs demonstrating slightly higher use of bank and third-party loans as a source of financing. Banks often avoid financing start-ups because of higher risk and it is very likely that those entrepreneurs who obtained a loan could offer private real estate for collateral. NBFIs, credit cooperatives, NGOs, and government programs play no significant role in start-up finance.

Motivation for the establishment of a business per type of business is shown in Figure 20. While “to have a successful career/to fulfil own aspirations” and “to become independent/autonomous” were the most often mentioned answers by male respondents, the prospect of creating a job and earning money were important motivations for female entrepreneurs as well as for family businesses. Hence, becoming an entrepreneur is for female entrepreneurs more often an issue of necessity rather than a choice. This might be the case especially for the divorced/separated or widowed women entrepreneurs.

Also interesting are the differences in motivation between the cities and the date of the business’s establishment. In Darkhan and, to a lesser extent, in Erdenet, the main motivation for starting a business is the perspective of a successful career, while in Ulaanbaatar it is the objective of creating a job for him- or herself (Figure 21). This suggests that the employment situation in Ulaanbaatar is worse than in other cities, possibly due to migration. Furthermore, entrepreneurs who established their business in 2009 or after more often state that they became entrepreneurs to have a job and earn money, compared to businesses that were established before 2009. While migration might also play a role here, this finding suggests that the general labor market situation has worsened and more people have to start a business to make a living.
When starting a business, women entrepreneurs typically have more previous relevant work experience than men entrepreneurs. While most women (51%) have worked more than five years in another company before founding their own, this figure is lower for men (41%). At the same time, 37% of men and 23% of women respondents reported one to five years of previous work experience (Figure 22 shows breakdown per years of experience). The higher share of women with significant experience partially reflects the age difference between women and men entrepreneurs (Figure 5).

Respondents were asked about perceived key success factors in establishing their business during the start-up phase. While male entrepreneurs said that it was their previous work experience, female entrepreneurs said they worked hard and, to some extent, received family support (Figure 23). While male entrepreneurs also benefited from networks (28%), this factor was less relevant for female entrepreneurs (14%). Sufficient access to capital was not relevant for either category, indicating that access to finance during start-up is a challenge rather than a success factor.
4.4.2 Current Challenges and Needs

Access to capital is the main obstacle enterprises currently face (Figure 24). This is true for start-ups as well as for all other types of businesses, although male entrepreneurs said that more often than female or family businesses (48%, 38%, 39%, respectively). Other constraints are in particular governmental policies and taxes, whereas it is not only the tax rate but also cumbersome procedures. Female entrepreneurs more often respond that high rents and general costs of doing business (raw materials, labor, etc.) are too high. While it can be assumed that female entrepreneurs are more cost sensitive, this finding might also relate to a lack of financial management knowledge.

Gender-specific challenges were further examined by asking the respondents if these challenges would rather apply to men, women, or equally. Overall, 62% of the respondents said that women face more or harder obstacles in doing business than men, while 32% say that there is no difference.

Female respondents in general said more often than men that they face specific challenges, and men acknowledge this (Figure 25). In particular, family and household responsibilities are perceived as limiting factors to 76% of female entrepreneurs. The second main constraint is gaining acceptance from colleagues and customers. Limited access to networking opportunities was also specifically mentioned as a constraint applying more often to female than to male entrepreneurs (29% as noted by men and 28% by women themselves). Moreover, access to land and governmental
support programs, and lack of management experience was mentioned, although most female entrepreneurs recognize these constraints applying to both genders.

Although a wide variety of trainings are offered by several institutions, attendance is generally low for both genders. The most attractive training, attended by 34% of female entrepreneurs, was financing (Figure 26). Although women have attended trainings on cost management, accounting, or marketing, roughly as often as men, they less often attended specialized trainings like logistics, HR, or technical ones, and are also less interested in attending those. However, as women tend to manage smaller enterprises and businesses in the services sector, these trainings seem to be less relevant for them.

The most demanded trainings for both genders are marketing and sales, legal, and cost management. The higher demand of women than men for cost management and legal issues trainings reflect the business challenges currently faced by women (Figure 24). Furthermore,
demand for trainings in financing and accounting is still high and better access to them can significantly improve business performance.

About half of the respondents paid at least a portion of the total costs for trainings provided to them. However, female respondents (54%) paid more often for them than men did (48%). This is surprising, as more women (29%) than men (25%) are members of associations or networking groups, of which many (60%) organize such trainings. It might be the case that female entrepreneurs lack time to apply for free trainings or are not informed about such possibilities. However, it might also be that women are more open to pay at least a portion of the costs for high-quality trainings.

Figures on attendance or interest in advisory services for businesses show a similar pattern. Overall, however, the level of use of advisory services is relatively low (Figure 27). The share of entrepreneurs not interested in contracting professional advisors is high, possibly due to high expected or real costs. Still, with about 50% of entrepreneurs interested in cost-management advice and 45% in financial advisory services, the demand for business advisory services seems quite high.
4.5 Access to Finance

4.5.1 The Relationship between SMEs and Banks

In general, the use of banking services is very high in Mongolia: 95% of male respondents and 99% of female respondents use at least some bank services. The bank most frequently referred to as the primary business bank is Khan Bank followed by TDB, Golomt and XacBank (Figure 28). While TDB and Golomt have a higher share of men-owned businesses, XacBank’s services are more frequently used by women-owned enterprises, as well as by family businesses. XacBank might be preferred by female entrepreneurs because of its historical background as a microfinance institution (MFI) serving female clients and its social mission to reduce poverty. Another reason could however be the better service offered by XacBank. As shown below (Figure 30), good service was the second most important reason for bank preference by female entrepreneurs. Moreover, XacBank clients most frequently stated “good service” as a reason for bank preference.

Differences also exist between microenterprises and SMEs. Khan Bank, XacBank and also State Bank are popular among microenterprises (Figure 29), which is possibly because of historical background of XacBank as an MFI, as mentioned above, and Khan Bank as the former State Bank of Mongolia, in fact a monobank\(^{63}\) for household savings in the Soviet era. TDB and especially Golomt Bank have a substantially higher share in the SME market than among micro enterprises. Some differences in market shares also exist between the cities with TDB being especially strong in Darkhan, State Bank in Erdenet and Khan and XacBank in Ulaanbaatar.

While most SMEs in the sample have a primary business bank (97%), a significant number of respondents (85%) use more than one bank for different purposes. Of male entrepreneurs 57% use a second or even a third bank for their business banking and 28% use another bank for private banking purposes. For female entrepreneurs it is 52% and 34%, respectively.

The use of services from multiple banks can be explained by high competition between banks. Another reason is that interbank transfers can take a few days, so that entrepreneurs choose to have accounts at several banks to simplify transactions with suppliers and customers. In order to have better access to their funds, the customers often make use of the services of the branches of several banks, as the branch network of the banks in Mongolia is not equally extensive. Golomt and TDB are often chosen as the secondary but not primary business bank. State bank services are used by 31% of respondents for private banking and 10% for business banking.\(^{64}\)

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\(^{63}\) Monobank is a term used for a bank in a centrally planned economy like the one of the former Soviet Union, where a single state bank (Gosbank) combined the roles of a central bank and a commercial bank.

\(^{64}\) The government pays out pensions or other benefits through State Bank. Thus many people have an account there.
As the Figure 30 shows, the differences related to preference of a particular bank between male and female customers are not significant; however, female customers appreciate good service and quicker response more often than men. This has obviously to do with the gender role of women for whom building up and maintaining relationship is the key factor in social interaction. Combining these findings with the ones from above, it can be concluded that women appreciate a friendly and good service as well as the provision of adequate information, business support, and simple and understandable products, for example banking packages. Thus, women entrepreneurs tend to favor the relationship banking model over the transaction banking model.

The high share of Khan Bank clients can be explained by its branch network, the largest across Mongolia. Convenient location is often cited as the factor most appreciated by the respondents (77%). For the customers of XacBank (48%) and Golomt Bank (42%), on the other hand, good service is more important than other factors. XacBank is also chosen because of its preferable terms and conditions (45%); TDB’s reputation was the determining factor for it as choice of bank.

Most women entrepreneurs are completely satisfied with their bank. The most complaints, if there are any at all, are unsatisfactory product features like interest rates or collateral requirements but also soft factors like poor
business support and adequate information. Men, on the other hand, are less satisfied with their bank, in particular with collateral requirements (Figure 31).

As for women, specific obstacles in banking, more than 60% of male and female respondents state that women are hesitant to approach a bank (Figure 32). This might be partly explained by the feeling of more than 20% of women entrepreneurs that they are treated differently than men by banks. As mentioned above, the perceptions of many of the stakeholders confirm that women SMEs, but also all SMEs in general, are perceived as a risky segment by the banks.

Lack of collateral is considered by about 40% of all respondents as being a harder constraint for women than it is for men, which confirms stakeholder perceptions of a disadvantaged position for women in terms of property rights for assets.

While more than 40% of men believe that in women-owned businesses the spouse makes the critical financial decisions, only 20% of women respondents agree with this statement. Indeed, other figures of this sample show that it is only in 3% of women-owned enterprises that the spouse makes financial decisions.

FIGURE 31: OBSTACLES IN BANK RELATIONSHIP PER GENDER OF RESPONDENT

Note: Multiple answers allowed.

FIGURE 32: WOMEN-SPECIFIC OBSTACLES IN BANK RELATIONSHIP PER GENDER OF RESPONDENT
Financial advice is an important feature in the relationship between financial institutions and entrepreneurs, in particular women, as mentioned above. However, only 26% of male entrepreneurs and 20% of female entrepreneurs receive advice from banks, and no respondents receive advice from NBFIs or credit cooperatives (Figure 33). This creates opportunity for the banks to differentiate themselves from the competition by offering non-financial services even more extensively.

Also low is the proportion of entrepreneurs using external consultants or accountants, which is in compliance with the low numbers of entrepreneurs receiving advice on accounting (Figure 27). The main sources of financial advice are professional media like newspapers, TV shows or magazines, as well as relatives and friends. While the proportion of male entrepreneurs receiving some kind of financial advice is with 74% quite high, almost 40% of women entrepreneurs do not receive any financial advice.

4.5.2 Use of Bank Loans

Most of the current financing needs of surveyed enterprises are covered by retained profits; and women in particular use this conservative source (Figure 34). More than 50% of the businesses also use bank loans, whereas no significant
difference can be observed between men and women. NBFI have a share of about 2%, in line with their share in the financial sector. Other sources of financing are friends or family members, as well as informal money lenders.

Most entrepreneurs of this sample have tried to obtain a loan (84%). Of those who tried, most were successful (88%). Women entrepreneurs tried to obtain a loan more often than men entrepreneurs, but less often than family businesses (Figure 35). However, while most of the men who tried to get a loan were successful, women entrepreneurs and family businesses were more often rejected. The main reasons stated were lack of collateral and problems in providing financial documents. On the other hand, family businesses use loans more regularly, with 72% of family businesses in the sample currently or recently have a loan outstanding. Although men apply for loans less often, more than half (53%) have or recently have had a loan outstanding. As for women-owned enterprises, this figure is slightly less (49%). This suggests that while women apply for a loan at least once, they do not use loans frequently and prefer to finance growth through own funds. This can, however, also imply that their experience with loan application and repayment was less successful or less pleasant, so that they decide not to approach banks for loans again.

The fact that start-up businesses attain financing less often from banks is illustrated in Figure 36 and in line with other research on this topic from other countries. While 65% of the companies at the start-up stage applied for a loan, only 45% received one. In general, the more mature a business becomes, the more often it applies for loans and has the loan approved. This pattern suggests that banks prefer working with established businesses and regard young businesses as too risky. However, businesses established more than ten years ago finance themselves more often through retained profit, and thus have less need of external sources of funding.

As mentioned above, the loan application process is perceived as complicated and full of caveats. Only 15% of the respondents say that they faced no significant problems. Difficulties in providing collateral are the most often-faced obstacle. Further, the collateral often does not allow borrowing the envisaged loan amount because banks tend to value land and other property pledged as collateral far below the market price due to legal and practical problems associated with seizure and reselling in the case of loan default. It might be that men face this problem more often than women or family businesses because they tend to ask for larger loan amounts, as it is shown below, or simply...
because they have the collateral to be pledged more often than women do.

Women more often than men complained about difficulties in presenting financial documents and the slow processing of loan applications. This might again suggest that women are more sensitive towards service quality and might lack financial knowledge.

The disbursed loan amounts vary widely between men- and women-owned businesses. While men most often get loan amounts of more than MNT 40 million, the majority of women entrepreneurs get loans of less than MNT 20 million. Interestingly, 9% of women-owned businesses get loan amounts of more than MNT 200 million, while only 4% of men-owned companies obtain such large loans. The figures show that women entrepreneurs get loan amounts in the middle range of MNT 40 to 200 million less often than men. This finding implies that either banks grant women smaller amounts than they applied for, or the women themselves request smaller loans because they run smaller businesses, or both could be the case.

A similar pattern is observed in terms of loan maturities. Because smaller loans can be repaid more quickly, most women receive loans for

FIGURE 37: OBSTACLES IN LOAN APPLICATION PROCESS

FIGURE 38: LOAN AMOUNT PER BUSINESS TYPE

FIGURE 39: LOAN MATURITY PER BUSINESS TYPE
less than 24 months. At the same time, men-owned businesses, and even more often family businesses, get loans for more than three years. In accordance with larger loan amounts and longer maturities, but also with a higher share of seasonal businesses, men-owned enterprises are more often granted grace periods than women-owned businesses (Figure 40). Interest rates charged by the banks vary from 1.5% to 2% per month and are thus in accordance with the official rates charged by the main banks for typical loans (Figure 41). However, while most women pay interest rates similar to those regularly offered (47%), men more often get lower rates. But a higher share of men also pay rates of above 2%. Because women get smaller loan amounts, which are typically more expensive to administer, it is reasonable that their average interest rate is a bit higher than for men. Hence, the interest rates mentioned by the respondents seem to reflect the typical rates charged for different business sizes and loan characteristics. However, it might be that women are in some circumstances priced higher than men, for instance because lending to women entrepreneurs is ceteris paribus regarded as riskier than lending to men.65

All banks typically ask for immovable collateral for loan amounts exceeding MNT 10 million. Accordingly, 80% of women-owned enterprises, 90% of men-owned enterprises, and 90% of family businesses provide their private house or another building as collateral (Figure 42). The remaining share of respondents provide their business site as collateral. Banks tend to prefer to pledge private real estate instead of business real estate, probably because of the higher immaterial value. Other collateral types like cars or accounts receivable are also provided, but only to a limited extent. Movable collateral is usually only accepted in combination with immovable property. However, as women generally request smaller loans, they could provide cars, accounts receivable, or personal belongings like jewelry as movable collateral for such smaller loans. Guarantors, although in general accepted by banks to increase the loan amount above the otherwise granted amount, are seldom used.

Most loans were used for multiple purposes by all groups; however, women tend to use a loan more often for only one purpose. This might be explained by the smaller loan amounts or the intention of women to focus

**FIGURE 40: SHARE OF LOANS WITH GRACE PERIOD**

![Graph showing the share of loans with grace period by business type.]

**FIGURE 41: INTEREST RATES OF LOANS PER BUSINESS TYPE**

![Graph showing interest rates of loans per business type.]

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65 Indeed, the correlations show that smaller loan amounts are priced higher as well as loans of longer maturity. A correlation between interest rate and gender is not observed.
upon a single planned investment. Most loans were used for working capital needs and/or for investments into machinery or equipment, but less often for larger investments like real estate. Family businesses more often undertake larger investments and less often use it for immediate needs. Women more often than men used the money for their own or family needs as well as to purchase inventories in cash instead of deferred payment. This might indicate that some women needed the loan to cover immediate expenses. Research and development of products, marketing activities or energy-efficiency investments were practically not made at all. The low share of borrowers who repaid debts with a new loan is very low, suggesting an overall low share of over-indebtedness.

4.5.3 Demand for Bank Loans

The loan demand is high and exceeds supply. When asked about the interest in future loan, 95% of men entrepreneurs, 93% of women
entrepreneurs, and 96% of family businesses expressed their wish to obtain one. Most entrepreneurs ask for loans in MNT (94%), while 6% would like to get a loan in USD. The average loan amount requested is MNT 315 million (USD 175 000). Men-owned and family businesses ask for considerably larger loan amounts than women-owned businesses (Figure 44). Further, micro-enterprises ask for an average loan amount of about MNT 200 million, whereas SMEs ask for three times the amount (MNT 600 million). The largest capital needs are demonstrated by businesses active in construction and production, while businesses active in trade would like smaller amounts.

The total loan demand for all enterprises in this survey is about MNT 72 billion. However, some enterprises ask for unrealistic loan amounts. Correcting for outliers,66 a more accurate average demanded loan amount per enterprise interested in loan is MNT 161 million67 and the total medium-term loan demand of enterprises in this sample would be MNT 34.4 billion.

The total additional loan demand of all Mongolian SMEs is estimated at MNT 9,022 billion (USD 5 billion).68 This takes into consideration the roughly 55,000 enterprises and applies to the shares of women- (38.9%) and men-owned enterprises (61.1%) as of total enterprises estimated by the Enterprise Survey (2013). It also includes the share of women (93%) and men (95%) interested in obtaining a loan. Of this loan demand, 24% or MNT 2,165 billion or USD 1.2 billion accounts for demand from women entrepreneurs.

The entrepreneurs surveyed ask for longer maturities than typically offered by the banks. Only 20-25% of the entrepreneurs would like loans with durations of less than one year, and 42-58% with a maturity of more than five years. This implies that less working capital but more investment loans are demanded. Whereas men-owned and family businesses have investment plans that would need more than five-year financing, women more often foresee repayment within three to five years.

Grace periods can help make long-term and large investments more affordable. Grace periods are requested by 71% of entrepreneurs. About half of all respondents would like to have a grace period of up to six months and 29% for more than six months. As for the sectors,

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66 A total of 31 enterprises asked for loans that are much higher than their turnover. These have been corrected by applying a medium-term loan demand of three times the turnover.
67 By business types, the average loan amount requested by men-owned businesses after correction is MNT 208 million, by women-owned businesses - MNT 111 million, and for family businesses MNT 158 million. By gender, men ask for MNT 216.4 million, women for MNT 106.5 million.
68 The additional loan demand by women-owned SMEs is calculated as follows: 55,000 enterprises*38.9% of which are women *93% interested in obtaining a loan*106.5 million average loan requested=MNT 2,125 billion. The additional loan demand by men-owned SME average loan demand: 55,000*61.1%*95%*MNT 216.4 million average loan requested =MNT 6,897 billion. Total additional loan demand is MNT 9,022 billion (USD 5 billion).
it is in particular production that needs long-term financing while services and construction more often ask for short-term loans of up to 24 months.

With more than 70% asking for loans with an interest rate of less than 1% per month and 90% asking for loans priced with less than 1.5% per month, the vast majority would like to borrow at considerably lower rates than the banks offer (Figure 46 and 41). While loans of less than a 1% interest rate per month probably cannot be offered under current circumstances, every decreased digit will help to decrease the credit gap.

Most entrepreneurs could provide some kind of collateral for a loan. Private houses or other real estate can be provided by more than 80% of the respondents (Figure 47). Furthermore, the business site, machinery or equipment, and cars, can be provided by more than 10% of the respondents. Guarantees by individuals or a group cannot be provided regularly. Women are not less capable of providing collateral than men or family businesses.

Most entrepreneurs would use the loan for medium-term investment purposes like equipment or machinery but less often for

FIGURE 45: REQUESTED LOAN MATURITIES PER BUSINESS TYPE AND BUSINESS ACTIVITIES

FIGURE 46: REQUESTED INTEREST RATES PER BUSINESS TYPE AND BUSINESS ACTIVITIES
long-term investments into real estate or refurbishment (Figure 48). While this is also true for women, women would use a loan more often for working capital than men-owned or family businesses and less often for investments. In comparison to usage of current loans, research and development is more often on the agenda. In total, most loans would be used for productive purposes and a very small proportion for personal/family needs or to repay old debts.

4.5.4 Usage and Demand for Other Banking Products

Besides loans, other banking services are also frequently used by entrepreneurs, both male and female. However, regarding private banking, these other products are limited to current and savings accounts, term deposits, and insurance. The latter two are used by only about half of the respondents (Figure 49). The various loan products requested were only used by some respondents. Thus, it has to be assumed that the respondents did not fully understand the differences since a larger proportion gave details about their current loans. In particular, respondents were interested in overdraft facilities and private credit cards.

When asked about business banking products, respondents reported low use of private banking products. This indicates that private banking accounts are often used for business purposes.
or the same account is used for both purposes. In the case that entrepreneurs use a separate account, most (91% of women, 96% of men) use it as current account; 20% of women and 22% of men use a commercial loan line (Figure 50).

Mongolian banks offer different delivery channels, and customers tend to use them frequently. However, the branch remains the central contact point and most customers tend to go at least once a month, if not weekly and some even daily (Figure 51). This explains the importance of convenient locations of bank branches as well as complaints about overloaded branches and long waiting time.

Mobile banking is very popular in Mongolia with 57% weekly usage by male as well as female respondents. This is considerably higher than internet banking usage, and of those who do not frequently use internet or mobile banking, more are interested in using mobile banking. The interest in profiles of banks in social media is also quite high. Still, online or mobile banking services are mostly used for complementary services like checking the account balance, less for money transfer\(^69\) and

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\(^{69}\) Most mobile banking services only offer money transfer between bank accounts of the same bank and are thus less useful for payments.
cannot yet replace the visit to the bank branch. Direct promotion of banking products, in other countries important especially for insurances or investment products, are neither regularly used nor of greater interest for entrepreneurs, although this might save considerable time. Furthermore, with relatively low distribution of credit cards, usage of point of sales (POS) is also low with less than 50% using it at least monthly. Gender-specific differences are only observed in internet banking and bank’s social media usage, confirming that personal service is of greater importance for female than for male entrepreneurs.

**FIGURE 5: USAGE AND INTEREST IN BANKING SERVICE DELIVERY CHANNELS PER GENDER OF RESPONDENTS**

<table>
<thead>
<tr>
<th>Service</th>
<th>Male</th>
<th>Female</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank’s social media</td>
<td>16%</td>
<td>49%</td>
</tr>
<tr>
<td>P.O.S.</td>
<td>36%</td>
<td>41%</td>
</tr>
<tr>
<td>Direct promotion agents</td>
<td>7%</td>
<td>6%</td>
</tr>
<tr>
<td>Mobile Banking</td>
<td>57%</td>
<td>57%</td>
</tr>
<tr>
<td>Internet Banking</td>
<td>36%</td>
<td>24%</td>
</tr>
<tr>
<td>ATM</td>
<td>88%</td>
<td>82%</td>
</tr>
<tr>
<td>Branch</td>
<td>83%</td>
<td>84%</td>
</tr>
</tbody>
</table>
5. Constraints Perceived by SMEs and Women-owned SMEs

As mentioned in the introduction to this study, the key objective of this research has been to explore the constraints and opportunities that SMEs in Mongolia face in accessing financial and non-financial products and services, obstacles in doing business associated with the economic situation, legal and operational framework. A special focus while conducting interviews with stakeholders and male and female entrepreneurs themselves was put on the specific constraints faced by women-owned businesses.

In the following, we outline some constraints this research identified separately for SMEs and women-owned SMEs through interviews with key stakeholders in the sector and a survey of male and female respondents. It should however be noted that this separation is done on purpose to reveal whether any gender-specific implications can be derived from general findings.

As described in the conclusions below, however, most of the stakeholders as well as the evidence of the quantitative data obtained rather prove that women-owned SMEs represent a sizeable market segment, not necessarily explicitly distinct from men-owned SME segment. The gender-biased perceptions by the stakeholders, in particular financial institutions, are not necessarily based on experience with women-owned SMEs, but often on conjectures and lack of awareness about the potential of women entrepreneurs as a profitable market segment.

5.1 Constraints Perceived by SMEs

Despite recent efforts by various stakeholders, there are several factors that constrain the development of SMEs in Mongolia. Below are the most frequently mentioned obstacles for business development cited by the respondents of the survey, as well as those highlighted by various stakeholders.

Access to Finance: Problems experienced by SMEs in accessing finance have been revealed in a recent survey conducted by the MNCCI, with only around 30% of the SMEs in Mongolia found to have ever benefited from a government-funded SME loan program. The same survey by MNCCI revealed that accessing loans funded by the banks themselves is considered even more difficult by SMEs. The World Bank’s Enterprise Survey 2013 shows similar results with access to finance being the most important constraint reported by Mongolian companies. More than 30% of firms in Mongolia perceive access to finance as the biggest problem to their operations (higher than the average of 17% in the EAP region). 70

The survey undertaken for this paper has shown that difficulties in accessing finance have been raised by 47% of male and 36% of female entrepreneurs as the challenge currently critical

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for development of their businesses. In general, lack of collateral and difficulties in pledging collateral, as well as short loan maturities and high interest rates and fees, are main factors limiting access to finance.

On the other hand, loan demand is high among SMEs. It is estimated that 95% of the enterprises in Mongolia demand for loans in the medium-term. Total loan demand is estimated at USD 5 billion of which USD 1.2 billion is demanded by women-owned enterprises.

**Lack/insufficiency of collateral:** With very few exceptions, the Mongolian banking system is based on collateral-based lending and commercial banks are strictly implementing it by asking for immovable property as collateral. Because of a missing central property register for property, banks accept movable collateral only for very small loan amounts (< MNT 10 million) or in addition to immovable collateral to avoid the multiple use of the same collateral for several loans. Further, banks tend to value collateral far below market value, mostly because collecting property is difficult and time-consuming due to complicated jurisdiction related to resolving disputes. Unlike banks, NBFI also accept movable property as collateral on a contractual basis, however, at the cost of significantly higher interest rates. Difficulties in presenting collateral have been mentioned by 63% of male-owned and 48% of female-owned enterprises in the survey as the most important problem they face during the loan application process.

However, this study did not reveal that women face more severe challenges with providing collateral than men, as most of the research suggests. We believe this finding can be justified by the fact that most of the key business decisions are taken by men and women together. As stakeholder interviews revealed, the decision on whether men or women apply for a loan often depends on availability of valid documents for immovable property and the employment status of family members. Typically, property is registered in the name of the male spouse.

**Unsuitable loan conditions:** Nearly one third of all men- and women-owned SMEs indicated that high fees charged by banks are a problem for them. The survey conducted by the MNCCI among its members revealed similar findings with SMEs complaining about loan conditions being highly inflexible given their needs. This argument is mostly related to high interest rates, fees and commissions charged, as well as short loan maturities. Monthly interest rate charged by commercial banks fall within the range of 1.5% to 2.5%, the lower end is usually applied to large corporations. Monthly interest rates at NBFI can be as high as 3.5% to 4%, as NBFI do not have access to governmental SME support programs and mostly fund themselves via commercial banks. Nevertheless, SMEs often prefer borrowing at NBFI because of their shorter loan processing time and more flexible collateral requirements.

**High taxes:** SMEs also complain about the high taxes they face in running their business. Some 40% of men-owned and 43% of women-owned enterprises find the prevailing tax rates too high to profitably run their operations. Regulatory authorities are aware of their complaint on taxation and formulated a draft bill on tax exemptions for SMEs, which is still under discussion in parliament.

**Government policy:** SMEs perceive the current government policy to be an obstacle for them. In other words, SMEs believe that there is no government policy committed to the development of SMEs. This may be justified by the fact that government-led SME support programs are too small in size and far from meeting the demand of SMEs. Further, many entrepreneurs might not be aware of existing support programs. Additionally, the funds dedicated to SMEs might be channeled to other client segments able to meet banks’ requirements, especially on collateral. While 37% of male entrepreneurs see government policy as an obstacle to their business, this ratio increases to 44% in the case of women entrepreneurs. It can be concluded that women-owned SMEs are more sensitive to the lack of supportive government policy.
Long processing time at banks: Lending procedures at banks is perceived cumbersome and time-consuming by SMEs, with 26% of men-owned and 38% of women-owned enterprises complaining about it in the demand survey. Commercial banks themselves admit that loan approval can take from two weeks to one month. SMEs are thus forced to search for alternative, and often more expensive, funding sources. For example, despite interest rates of 3.5 to 4.0% per month, NBFIs are often approached because of faster loan processing and loan disbursement.

High costs of doing business, including high rents: In general, SMEs in Mongolia are of the opinion that they are constrained by high costs, including high rental costs: 29% of male and 37% of female entrepreneurs think that the overall cost of running their business poses them a challenge to run their operations profitably.

Lack of skilled workforce: The NSO reports that the literacy rate in Mongolia is quite high: nearly 98% of Mongolian citizens are literate. However, there seems to be a mismatch between the skills demanded by employers and skills possessed by employees, as 17% of men-owned and 13% of women-owned enterprises raise the issue of unskilled staff as an obstacle. One reason might be that during times of transition, many young people who constitute now the labor force, in particular male, dropped out of school and/or did not get tertiary education. Some stakeholders also relate the problem to the entrepreneurial spirit of Mongolians, suggesting that people above average skills find it more attractive to become an entrepreneur than working for the financial benefit of others.

Lack of capacity at SMEs: Besides external factors, SMEs themselves acknowledge responsibility for the limited outreach of SME finance in Mongolia. They usually suffer from lack of capacity in preparing a sound business plan and satisfactory cash-flow projections. They neither have thorough understanding of the market they operate in; nor can they closely follow the technological developments, or changes in supply and demand conditions.

Some SMEs are aware of the capacity problems they face, as 26% of male and 36% of female respondents acknowledged that they faced difficulties in preparing financial documents while applying for a bank loan. Women entrepreneurs seem to be suffering more from it, highlighting the need for financial literacy trainings for women-owned SMEs being more explicit than their male counterparts.

5.2 Constraints Faced Specifically by Women-owned SMEs

Women-owned businesses share many barriers with those owned by men, e.g. access to finance, high taxes, and complex governmental procedures. Commenting on the results of the demand survey and findings from interviews with industry stakeholders, additional constraints faced by women-owned SMEs are the following:

Lack of networking opportunities: Industry stakeholders are of the opinion that one of the most important constraints Mongolian women face in doing business is the lack of networking opportunities. While it is mostly men who come together in the evenings for socializing and to exchange business-related information and ideas, women are more often tending to children, the elderly, and general household duties. As a consequence, women usually are disadvantaged as far as networking opportunities are concerned. This is of particular importance given that small enterprises that are a part of a supply chain have higher chances to grow and sustain their activities if taking advantage of networking opportunities.

The survey however revealed that women-entrepreneurs in the survey tend not to perceive this constraint as specifically applicable to them. Only 28% of women-owned SMEs compared to 29% of men-owned enterprises think that limited access to networking opportunities can indeed be a challenge in the case of women-entrepreneurs, while 58% of survey respondents in each gender perceive the issue as being a major challenge for men.
Perception of women by financial institutions:
Financial institutions in Mongolia generally perceive SMEs as a high-risk segment. Although nearly all institutions interviewed indicated that loan repayment rates are higher in the case of women entrepreneurs, this perception of women-owned businesses does not change the fact that they are typically characterized as having insufficient assets and low capitalization. They are thus considered more risky compared to men with a larger business and/or more collateral. Along with the typically smaller size of the business, this might explain why women entrepreneurs are granted smaller loan amounts on which they then have to pay higher interest rates.

The demand-side analysis revealed that 36% of women entrepreneurs find it difficult to present financial documents requested by banks at the loan application process, which was also confirmed during some interviews with stakeholders. This might partly be explained by the general lack of financial knowledge, especially among women entrepreneurs. Although it cannot be generalized, some women entrepreneurs may also lack autonomy to interact with financial institutions or conduct financial transactions on their own also restricting themselves in running their business effectively. This is also reflected in responses of the women, 60% of which acknowledge that they are hesitant to approach a bank, most probably because they lack financial knowledge and/or are insecure about dealing with financial issues.

Combining work and family responsibilities:
Women entrepreneurs consider family and household responsibilities to be one of the factors that limit the development of their businesses. That family and household responsibilities are more challenging for women than for men entrepreneurs has been stated by 76% of female respondents and 47% of male respondents. Women are the primary caregiver for children and elderly family members as well as responsible for household chores, and work longer hours. They thus also have limited time to involve themselves in business-related activities such as networking and training opportunities. Although childcare services exist, kindergartens - especially in outer districts of Ulaanbaatar - tend to be overcrowded. Further, for families that do not have the chance to enroll their young children in kindergartens, the burden of childcare usually falls on the shoulders of the mother.

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7 To present financial documents means that business documentation is not satisfactory as well as that women entrepreneurs have more difficulties in writing a business plan.

20 UNICEF calculated that Mongolian women on average work 44 minutes a day longer than men. There are also several reports referring to UNDP findings highlighting Mongolian women spending as much as 25 hours a week on household chores in addition to their responsibilities at work.
6. Conclusions and Recommendations

Access to finance is crucial for SME development, not only in Mongolia but also in other developing economies. SMEs in Mongolia, be it male- or female-owned enterprises, face a number of impediments, including difficulties in accessing finance, the high cost of financing and running a business, and insufficient support mechanisms.

Problems related to access to finance stem mainly from collateral requirements of financial institutions and the non-existence of a central registry for movable properties. Commercial banks in particular are perceived as exercising high and strict collateral requirements. Borrowing from NBFIs comes at a higher cost and is also, in most cases, not collateral-free.

One of the reasons for difficulties in accessing finance experienced by SMEs is the general reluctance of commercial banks to serve the SME sector. While some banks recently discovered the SME segment as a replacement for a declining corporate sector (in particular mining), the banking sector in the country has not yet felt significant margin squeeze. The central bank’s policy easing has improved banks’ liquidity. Apart from policy-rate reductions and fiscal spending, the government also provided liquidity to the banking system, to be on-lent to targeted industries. As a result, in 2013 bank assets grew rapidly by 74% and loans by 54%. Large banks in particular benefited from the easing of monetary policy owing to their stronger franchise network. In other words, banks are still operating successfully in their accustomed environment and are not yet interested in reaching beyond to the new, riskier sectors like SMEs.

However, Mongolian SMEs themselves are also responsible for the financial sector’s lack of interest. They are usually weak in capacity, face difficulties in preparing business plans and cash-flow projections, and cannot conduct market research on their own. While several governmental support programs as well as other initiatives have started to offer trainings or advisory services at discounted prices or on a cost-sharing basis, these programs lack scale and often quality, and are not sufficiently accessible for entrepreneurs.

Although women-owned SMEs mostly experience similar problems faced by their male counterparts, they perceive themselves more constrained in operating their business given household and family responsibilities. Time constraints are, in particular, affecting business size and growth potential though lack of capacity to attend trainings and to network. Furthermore, although access to land and equal property rights are in general stipulated by law, Mongolian women are often unable to enter contracts in their own name. They do not control and possess an equal share of assets or property within marriage because of several relevant reasons: the traditional perception of their social role and a lack of awareness about their property and land ownership rights.

While Mongolia’s SME sector faces challenges that limit its growth, it has considerable potential. Despite significant challenges in access
to finance and other issues, most of the SMEs are positive about the development of their businesses in the future. One third of the SMEs surveyed in this study have grown at a swift pace in the recent past. Moreover, 55% of these entrepreneurs expect their business to grow in the next two years, whereas only 28% believe that the business will experience no changes.

Moreover, the demand for SME loans is estimated at USD 5 billion, of which USD 1.2 billion is demanded by women entrepreneurs. Considering the current SME loan portfolio of the banking sector of USD 1 billion, it can be concluded that there is a significant unmet loan demand that could be covered by banks in the future.

Based on the findings of the survey, the authors formulated a number of recommendations for different stakeholders engaged in development of SMEs and women-owned businesses in Mongolia.

**Recommendations for International Financial Institutions**

- **Increase Technical Assistance (TA) to commercial banks in the field of SME finance**: SMEs in Mongolia face a domestic banking system that lacks the capacity to assess their creditworthiness, and hence is unable to lend significantly to SMEs. Banks should be supported in acquiring SME lending capacity not only to facilitate lending to this customer segment, but also to develop awareness of future downsizing at banks. As argued by some stakeholders, ideally the capacity building should precede making funds available for commercial banks.

- **Establish a risk-sharing mechanism with commercial banks**: Future loan programs targeting SMEs can be structured in a way to include a risk-sharing mechanism between the IFIs and beneficiary banks. For example, IFIs can share the risk with the bank on a portion of the banks’ SME portfolio.

- **Provide long-term financing in MNT**: Most SMEs need longer-term financing in the local currency. Limited long-term financing in MNT and limited hedging opportunities translate into SME loans of short maturity and/or high interest rates. Due to access to better hedging conditions and access to financing at lower interest rates, IFIs could provide long-term credit lines in MNT to commercial banks in Mongolia with better conditions passed on to SMEs.

- **Design loan programs exclusively for women entrepreneurs (WEs)**: There is definitely an interest in and economic necessity of loan programs targeting WEs in order to increase their overall access to finance. Such loan programs introduced at commercial banks should be accompanied by TA in order to help partner banks realize the “business case” for women entrepreneurs. Obviously, the commitment of the banks as well as readiness to invest in development of own institutional capacities should be given. The TA measures to be implemented together with the banks could include the components of developing the gender-related measuring indicators to track the performance of women clients, as well as establishing networking platforms for WEs, etc. Smaller awareness-raising programs could be offered in advance to TA measures as a pilot to identify the most committed FIs and promote the WE program.

- **Capacity building to banks and SME support centers in provision of trainings and advisory services**: One of the major obstacles for SME development is access to non-financial services such as trainings and business advisory services. These include financial as well as vocational and business management-related topics like logistics or marketing. While some IFIs have their own initiatives, more dedicated support could be provided in cooperation with banks, governmental support centers, and private initiatives. Targeting women entrepreneurs.

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73 Most of the banks interviewed indicated their interest in similar programs should those be available.
entrepreneurs in particular is recommended as they might benefit significantly from such services. Those initiatives should also facilitate the cooperation between banks and SME support centers like SME incubators. Although some banks, like Golomt and Kapital Bank, cooperate with those providers, a lot more can be done to build up mutual trust between banks and SME support initiatives. Thus, joint networking events and trainings on client financial education, for instance, could be supported by IFIs.

**Recommendations for Governmental/Regulatory Authorities:**

- **Incentivize the business registry:** SMEs that are not registered at the tax authority are frequent in Mongolia. Businesses that are not registered have no access to loans and limited access to governmental support programs and other support initiatives. While the process of business registration has been simplified during the past years, businesses still perceive the process as cumbersome and/or are not informed about the changes. The government is recommended to organize an information campaign about business registration and offer incentives for business registration. Additionally, IFIs could be approached by the government for specific support in the frame of targeted programs similar to IFC’s Secured Transactions and Collateral Registry Program.

- **Enforce collection of gender-disaggregated data:** Statistical information is necessary in order to understand the real situation of women. Most gender-disaggregated statistics on social, economic and business indicators are currently lacking in Mongolia. The governmental agencies responsible for collecting national data or conducting surveys should formulate their questionnaires in such a way that data can be disaggregated by gender in order to better interpret the situation of women and men in a particular sector.

- **Enhance the existing credit information system:** Mongolia is lagging behind most countries in emerging Europe and Central Asia in terms of legal framework and economic efficiency of its credit reporting system.\(^74\) In addition, according to Doing Business (2014), only 13,309 enterprises (13.4% of registered enterprises in Mongolia) are covered by the credit information system. Therefore, the related infrastructure of the credit information system should be upgraded for a more effective use of it, especially in assessing SMEs.

- **Enhance regulation on bankruptcy and simplify the collateral collection process:** In the event of bankruptcy, or in the case of a dispute between the bank and the borrower about loan conditions, the borrower can take advantage of the complicated process and make it difficult and drawn-out for the banks to collect the collateral. Banks incorporate this possibility and value collateral significantly below market value, resulting in lower loan amounts or in rejection of the client. The current regulations should be revised and for movable collateral simplified enforcement mechanisms should be considered.

- **Facilitate factoring and leasing practices:** To overcome the obstacle of collateral, authorities can encourage leasing and factoring by: (i) providing VAT tax incentives in the leasing law for the leased equipment; (ii) reviewing the legal framework governing contracts between parties; (iii) setting up a legal framework and enforcing environment for the collection of receivables.

- **Establish a credit guarantee fund for WEs:** Although a credit guarantee fund has recently been established, there is no information as to the share of women-

\(^74\) Isakova et al. (2012).
owned SMEs that have benefited from it. A CGF serving exclusively women-owned SMEs can be initiated to address the issue of lack of collateral, which is the most important obstacle for WEs obtaining a loan.

- **Extend the network of SME Development Center and Business Incubation Centers:** These centers, which provide training and capacity building services for SMEs, exist only in Ulaanbaatar. Their expansion beyond the capital city, as well as the opening of more of such centers in Ulaanbaatar, can create a valuable source of information and networking for SMEs.

- **Improve childcare facilities:** According to Member of Parliament Ms. Luvsan Erdenechimeg, kindergartens in the outer districts of Ulaanbaatar are over-crowded.75 Only half of the children in the regional districts have places in public kindergartens. Women are thus often forced to stay at home. Therefore, childcare facilities that currently suffer from a lack of funding and over-crowding, particularly in Ulaanbaatar, need to be improved in order to increase the participation of Mongolian women in business life.

- **Increase coordination among public and SME support institutions:** In Mongolia, there are a number of institutions/committees/support organizations in charge of regulation of the financial sector (Bank of Mongolia, Financial Regulatory Commission, Mongolian Bankers Association), promotion of gender equality (National Committee on Gender Equality), and development of SMEs (Ministry of Labor, Mongolian National Chamber of Commerce and Industry, SME Business Incubation Centers, SME Development Center of Capital City, Credit Guarantee Fund). Therefore, effective coordination among all these stakeholders is crucial for well-planned and comprehensive SME finance schemes. Regulatory authorities are recommended to take efforts to coordinate actions and exchange information between all of these institutions and NGOs involved in capacity building with SMEs and women entrepreneurs.

**Recommendations for Financial Institutions:**

- **Develop internal capacity to implement cash-flow-based lending:** Cash-flow lending is a suitable strategy to lend to SMEs at low risk even without full securitization. FIs should consider implementing a cash-flow-based approach by organizing workshops to internally promote SME lending. Through TA, FIs could receive trainings and advisory services from international SME experts on how to set up a cash-flow-based lending mechanism within their institutions.

- **Adopt risk-adjusted pricing models:** Banks above all can find ways to incorporate the perceived high risk of financing SMEs by developing a multiple-pricing strategy and can charge a higher price to companies that they perceive to be more risky, rather than avoiding the risk. Over time, the banks will build up a “corporate memory” as well as a track record for the SME segment. They will also benefit from a higher return than they are used to earn with the corporate and commercial segments.

- **Make use of the credit guarantee fund and other insurance products:** Activities of the Credit Guarantee Fund in Mongolia started only last year and its portfolio is still nascent. Banks and NBFI s can make better use of this resource in lending to SMEs that do not meet collateral requirements. In collaboration with insurance companies, banks can also develop special lending products for small enterprises. For example, financing herders is perceived to be risky due to unpredictable natural conditions, drought, and high animal mortality rates. The government of Mongolia and the World Bank have already initiated an index-based insurance program based on livestock.

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75 Tolson (2012).
mortality rates by species and soums. The pilot project proved to be successful and some banks already offer discounted loans to herders who insure their animals. Nevertheless, in practice, these insured herder loans are still not implemented by many financial institutions and can be explored by the whole sector.

- **Offer trainings to SMEs on business planning and loan application:** SMEs in Mongolia usually lack capacity to prepare a sound business plan and satisfactory cash-flow projections. They also have no thorough understanding of the market they operate in; nor can they closely follow the changes in supply and demand conditions. Even those who possess that capacity are often not able to demonstrate it to the creditors. Therefore, financial institutions could offer (or expand) trainings on business plan writing to their customers and potential customers either on their own or through cooperation with SME support institutions. Certain banks like Khan Bank and Golomt Bank already practice those trainings but could expand their outreach.

- **Offer networking opportunities for SMEs, women-owned SMEs in particular:** Some financial institutions are already engaged in sponsoring or organizing networking events for enterprises in their priority sectors. Such activities can be expanded to target WEs disadvantaged in networking.

- **Collect and analyze gender-disaggregated data on SMEs:** As the research reveal, most of the banks and FIs do not collect gender-disaggregated data and/or do not analyze it in a systematic way. This represents a challenge for them partly on technical reasons (MIS) and would cost an extra effort to collect the data manually. Additionally, apart from several NBFIs, which are obliged to report gender-disaggregated data to their investors and shareholders, banks and NBFIs generally do not see a rationale for collecting this data, which makes it difficult to analyze the profitability of women-owned SMEs in the total SME portfolio. Collecting and analyzing gender-disaggregated data, however, could be the first step on the way to grasping women-owned SMEs as an underserved yet profitable client segment.

**Recommendations for SME Development/Support Institutions:**

- **Provide an office space for start-ups:** A public area can be reserved at SME development/incubation centers for joint use of entrepreneurs/start-up business owners that do not have the capacity of opening up an office or refraining from it due to high rents.

- **Upgrade and expand the scope of trainings provided to SMEs / E-learning:** SME development institutions already provide a set of trainings to SME applicants. However, these trainings usually do not focus on sector specific and technical issues. Also trainings on marketing and sales, cost management, legal and tax issues are in demand and could be provided by such institutions. SME development/support institutions are advised to develop seminars and trainings in a format suitable for remote learning with the help of the government and/or donor organizations. Thus the content of those can be transferred to e-learning platforms and proposed to SMEs in online modules.

- **Forge partnerships with banks in supporting SMEs:** SME development/support institutions can establish partnerships with banks for provision of trainings, advisory services and organization of networking events targeting SMEs, hence lowering the cost of such services for either partner. Some initiatives already exist (for instance, SME Business Incubation Center of Chingeltei District in Ulaanbaatar cooperates with Golomt bank and Kapital Bank), these partnerships should be facilitated. SME development centers should proactively seek cooperation opportunities with banks.
• **Establish supply chains:** Chambers of Commerce, for instance, can form supply chains among its members, monitor the relations between the various parties through the supply chain, perform quality control checks at different levels, and can finally link them to a financing institution to get finance. Supply-chain finance mechanisms can be promoted as an alternative to factoring, which is currently does not exist in Mongolia.

• **Organize informational campaigns about land registry / property rights that also reach out to women:** Despite the revisions in the Land Law, land possession process in Mongolia is still perceived to be complicated. It is also common that, due to time constraints, women refrain from visiting the registry office to obtain the certificate of land possession. In other words, bureaucracy associated with the land registry process is also impeding women in accessing property ownership. Additionally, women are often not aware of or do not value their ownership and property rights. Concrete efforts could be made to raise awareness about their property and land ownership rights. SME development institutions can provide educational sessions/informational campaigns on the subject directed at women.
References


## Annex A: List of Persons Interviewed

### Governmental / Regulatory Bodies

<table>
<thead>
<tr>
<th>Name &amp; Surname</th>
<th>Institution &amp; Position</th>
<th>Tel.</th>
<th>E-mail</th>
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<tbody>
<tr>
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### International Financial Institutions / Finance Programs

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### SME Development/Support Institutions

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Annex B: Brief Overview of Stakeholder Interviews

Banks

Khan Bank: Khan Bank was established in 1991 as the Agricultural Cooperative Bank in connection with the dissolution of the State Bank of Mongolia. The bank inherited most of the assets and businesses of the state bank in rural Mongolia. In 2003, the bank was successfully privatized. Today, the bank operates with 500 branches. It is the largest branch network across Mongolia with about 100 branches in UB and more than 400 branches in rural Mongolia. It has an office in every aimag capital (21 aimags) and soum centers (circa 20 soums in each aimag). The bank is organized in three regional directorates: the east, the west and the UB regional directorate. Through his extensive network, Khan Bank provides comprehensive banking services to individuals, SMEs and corporate customers.

The bank provides services and facilities to about 1.8 million customers, including SMEs. In 2013, Khan Bank’s total assets increased by 72% and reached MNT 4.8 trillion (USD 2.7 billion). Total loans grew by 42% to reach MNT 2.5 trillion (USD 1.4 billion). Programs implemented by the Central Bank of Mongolia through commercial banks (i.e. government mortgage loan program) had an impact in this growth. The bank currently has USD 170 million outstanding with various IFIs (IFC, EBRD, JICA). The bank’s market share in banking sector total assets, loans, deposits is 25%, 23% and 29%, respectively. In addition, 40% of all bank branches across the country belong to Khan Bank.76

About 50% of the loan portfolio is distributed to legal entities, of which 60% is to SMEs and 40% to corporates. Legal entities are defined as SME if the turnover does not exceed MNT 1 billion. SME lending is considered as the less risky business compared with lending to the mining sector, with the current NPL being 1%-2%. Khan Bank’s loan portfolio concentrates mainly on the following sectors: wholesale and retail trade, construction, mining, transportation and agriculture. Khan Bank branches are granted a loan approval authority of up to MNT 100 million (USD 55,000). Loan requests exceeding this amount have to be approved by the head office sub-credit committee and then to the head office credit committee. A typical loan application is processed within 2-3 weeks.

Khan Bank does not collect gender disaggregated data, but the CEO shared his observation that there are many female customers at the managerial level of an institution and/or owning/managing a business. Mongolian women’s engagement in the tertiary education is also higher than that of men (70% of students are female). Another observation is that families often own several businesses, which often forces the bank to compile up to three financial statements.

The bank operates three SME centers in Ulaanbaatar focusing on lending to SMEs. No retail activities are offered in those business centers. Khan Bank also set up a Business Incubator Center with the mission of increasing capacity of SME business owners. In 2013, the bank organized about 20 training seminars for SMEs and around 350 entrepreneurs were trained free of charge through these seminars.

Two major obstacles in SME lending were mentioned during the interview. First, movable collateral cannot be used because of a missing movable assets registration system. So far, movable collateral is only used on a contractual basis for small amounts and to well-known customers or as additional collateral to immovable collateral. Second, SMEs lack the capacity to produce proper financial statements and do not use auditors’ services. Khan Bank reviews tax reports, however, these do not necessarily give the real picture of the enterprise. It was further noted that land only is not

considered as reliable collateral. It is pledged in combination with the buildings on it.

Khan Bank perceives the following issues in need of improvement for the Mongolian banking system:

- Establishment of a check-clearing house.
- Establishment of a movable assets registry system.
- Development of the hedging mechanisms.

**Trade and Development Bank:** Trade and Development Bank (TDB) was established in 1990 and has become a leading bank in Mongolia especially in corporate banking and trade finance. TDB's corporate clientele are mostly engaged in the mining, foreign trade, construction and manufacturing sectors. Clients are served through 47 branches with most of them located in urban areas and Ulaanbaatar (35).

As of April 2014, TDB's asset size reached USD 2.8 billion of which 52% are loans. The number of corporate customers (including SME clients) reached 26,700 with a total outstanding loan portfolio of USD 1.1 billion.

The bank does not have a clear SME definition; SME clients are segmented by loan size. Due to this, the management admits that there may be some large corporate clients in their loan portfolio that have benefited from an SME-focused loan program as many corporate clients are sometimes in need of a smaller loan (small expansions, equipment investment, etc.) and can be funded via loan programs designated for SMEs. TDB does not collect gender-disaggregated data, but the management has observed that women’s presence in managerial roles is quite visible.

TDB management mentioned that the average loan maturity is around 18 months apart from the project loans with a special funding scheme (KfW and JICA project loans are offered). Further, SME loans are estimated to be typically within the 300,000 to 600,000 USD range.

Branches have up to MNT 100,000 loan approval authority. Loan requests exceeding that amount come to the head office sub-credit committee that is held three times a week and having a credit approval authority of up to MNT 350,000. Any loan above this amount is subject to approval of the central credit committee. TDB is also engaged in financial leasing activities via TDB Leasing and has so far leased equipment to companies in mining, construction and cashmere production with a supplier buy-back guarantee.

**Golomt Bank:** Golomt Bank was established in 1995 as a wholly owned subsidiary of Bodi International L.L.C., one of the major players in Mongolian social and economic arena. Principal activities of Golomt Bank include: savings, loan services, card services, guarantees and letter of credit, money transfer, sales, purchase, deposit and trading of foreign currencies/precious metals, foreign settlement, issuance and trading of securities, financial leasing service and other financial services not restricted under the legislation and other activities accepted by the Central Bank, as well as other governmental agencies.

In terms of assets, Golomt Bank posted an increase of 48% in 2013 and the bank's total assets reached MNT 3.7 trillion (USD 2.1 billion), 60% of which is loans. The bank operates with about 100 branches in Mongolia, of which around 60 are located in UB. Golomt is present in most of the aimag centers.

SME lending is for Golomt Bank a strategic business and is currently improved by the introduction of new products and the declaration of 2014 as the “SME support year.” Golomt Bank defines enterprises as SME when the asset size is 150 million to 3 billion MNT and sales between 300 million and 5 billion MNT. Enterprises with assets or sales below are served through the retail department, larger companies are classified as corporate finance clients. The main challenge mentioned in the context of SME lending and, in particular, lending to women-owned SMEs is shortage of
collateral. Credit guarantees or loan insurance were referred to as possible solution for the banks to lower interest rates as well as to increase loan to value ratio.

Although the corporate decision has currently not been taken, the bank’s management is considering an internal definition for women-owned businesses. These are entities where women owners hold at least 25% of the company shares and at the same time manage the company. The bank is also willing to upgrade its MIS system to collect gender-disaggregated data, which is currently not available.

Other highlights of the interview conducted with Golomt Bank concerning SMEs and women-owned SMEs were:

- Traditionally and culturally Mongolian women are strong and dominant; they prefer to be engaged in business life either as an employee or entrepreneur.
- However, men are usually more informed about government programs and trainings as women lack networking opportunities.
- Women-owned/run businesses create lower NPLs as men sometimes take risks beyond their capacities.

**Non-Bank Financial Institutions**

**Transcapital:** Transcapital was established in 2001. As of today, it operates through eleven branches, serving about 14,000 clients. To serve clients’ financial needs, the company is providing micro and small businesses with loans along with various consumption loans. It mostly provides services in Ulaanbaatar and other urban areas. Expansion to the rural areas (currently two branched) is not considered due to high competition.

The average loan size is 3.5 million MNT (excluding micro businesses it is MNT 8 million). Besides immovable collateral, household appliances, jewelry and movable property are accepted. Most clients (about 70%) are female. The share of female loans in the total loan portfolio is about 60%. It is observed that men have on average larger businesses. Female clients are perceived as less risky, as they are more responsible in terms of loan repayment and loan use. The interest rate charged by Transcapital is slightly more than 2%, whereas 3% is reported as an average interest rate per month for the non-bank financial sector. Along with the individual lending, Transcapital offers group loans. However, the share of group loans does not exceed 25% of the total portfolio.

Transcapital observes that it gets more difficult for microenterprises to borrow from banks, whereas banks increased their efforts in targeting SMEs due to the lower performance of the mining and other corporate sector businesses. Accordingly, there is a concern that the banks would decrease their lending to NBFI in the future.

**Net Capital:** Net Capital is established in 2008 and currently employs 60 staff members. The NBFI has five branches across the country and serves around 10,000 clients. It is considered to be one of the leading NBFI, taking the 3rd or 4th position in the sector per asset size.

Net Capital provides business loans, consumption loans, leasing and trust services. The average loan size is MNT 4 million. The loan portfolio currently comprises 3,500 loans outstanding. The interest rate charged is 3.5% to 4% per month; however, lower rates are offered to repeat clients. Most clients (about 70%) are men. Net Capital accepts vehicles as collateral which are usually owned by men. The CEO interviewed mentioned the risk of over indebtedness, since due to the absence of the registry of moveable assets, vehicles can be used as double collateral. Several comments raised by Transcapital, Net Capital, and the Non-Bank Financial Institutions Association:

- The number of NBFI in Mongolia is increasing very fast (a fact also confirmed by the Mongolian Non-Bank Financial Institutions Association). As of today, the total number of NBFI is around 300 and it continues to increase.
• This rapid increase may create problems in the future as so many very small NBFIs with no tangible activity have been established recently.

• Larger NBFIs are pushing the FRC to increase the minimum required capital to establish an NBFI from MNT 400 million to MNT 1 billion. MNT 400 million minimum capital requirement was agreed five years ago and it is now outdated due to depreciation of the local currency in the last two years.

• The sector’s average loan tenor is twelve months with an average monthly interest rate of 3.5-4% per month.

• There is no gender-disaggregated data on the sector, but observations reveal that close to 60% of clients are women with the exception of car loans. Female clients are much more disciplined in repayments.

• Loan processing time is rather short compared to banks and disbursements are usually done within one to two days;

• Around 40% of NBFI clients do not have a registered business.

SME Development/Support Institutions

The Credit Guarantee Fund of Mongolia: The Mongolian Credit Guarantee Fund is a public non-profit financial institution established on 6 November 2012 under the provisions of the Law of Credit Guarantee Fund. Its mission is to help develop SMEs and start-ups, especially those that face problems in meeting collateral requirements imposed by the commercial banks. Although establishment took place in 2012, the real activities picked up in 2013 with the issuance on the first guarantee on 1 June 2013.

The Guarantee Committee at CGF in charge of issuance of guarantees is composed of:

• the executive director of CGF;

• the Ministry of Labor representatives;

• the representative from each of the three commercial banks (Khan Bank, XacBank, Golomt Bank).

CGF currently has a guarantorship agreement with eight banks and three NBFs. Total guarantee portfolio issued to five commercial banks has been MNT 3.7 billion (~USD 2 million) as of 2014, with 58% of this volume realized by Golomt Bank. Some 75% of the guarantees are issued for companies located in Ulaanbaatar and nearly 70% of guarantees are issued for companies engaged in manufacturing. CGF does not ask any type of collateral from guarantee beneficiaries.

As though the CGF currently enjoys a 0% NPL rate, the interviewee at the CGF also admits that there is no specific clause in the law regulating the CGF as far as potential non-payments are concerned.

SME Development Center of Capital City: The center operates as a government body for the provision of financial and non-financial services to the SMEs located in Ulaanbaatar. Its activities fall under the UB’s mayor’s office, which can run programs independently from but complying with those of the central government. The center has nine branches in each of the sub-districts in UB. It was established in 2011 and operates since 2012, offering trainings and advisory services.

The center has conducted own research to identify the challenges SMEs in UB city are currently facing, as well as to reveal some information on their profile. 3,025 SMEs in the last two years were covered under this survey. The major findings of the survey can be summarized as follows:

• Access to finance is a key obstacle. SMEs stated that commercial banks always ask for immovable property as collateral. Even if they can provide it, banks value their collateral much lower than its market value. Other problems in access to finance are lack of documents and lack of financial history.

• Lack of capacity at SMEs is an obstacle, including lack of business skills, information, training, as well as a suitable workforce.

• Around 62% of the SMEs/entrepreneurs who participated in the survey were women.
• Many businesses also operate as family businesses where it is common that the wife has decision-making authority.

• About half of the enterprises are well run, whereas the other half has larger problems. In particular, within the last twelve months more businesses closed then than in previous years.

• About 25% of the businesses are successful businesses.

• About 10% of the businesses formalized within the first two years of operation. The low formalization rate can be explained by lack of capacity of SMEs to register and the difficulty in handling tax declarations afterwards.

• Nearly 25% of the total sample does not have a stable and regular business activity. Operations tend to be irregular and/or seasonal, 85% of survey respondents have one to nine employees.

Based on the findings of the research, the mayor’s office took the following initiatives, some of which will be implemented by the SME Development Center of the Capital City:

• Initiated a training and capacity-building program for SMEs in each of the nine individual sub-district SME development centers. Trainings covered topics like how to write a business plan, practical business environment, production management, accounting and financial literacy. The SME development center cooperates with Golomt Bank on financial literacy trainings.

• So far 1,362 SMEs/entrepreneurs have been trained via this program, out of which, 791 have already prepared a business plan. About 80% of the beneficiaries were women.

• The cost of this training is around MNT 200,000 for each applicant. The center was providing these trainings for free, but a small contribution by the entrepreneur (MNT 30,000) has recently been introduced,

• MNT 20.2 billion (~USD 11 million) of concessional funding (with 1% p.a. interest rate) is allocated for SMEs;

  ✓ MNT 15.2 billion of which (~USD 8.5 million) will be channeled through cooperatives. As Savings & Union Cooperatives are known to charge a very high interest rate, the center is taking such an initiative to overcome this problem.

✓ And MNT 5 billion of which (~USD 2.8 million), is to be disbursed via five commercial banks with +5% interest margin. (Additional funding up to MNT 30 billion (~USD 17 million) is intended for this component through time).

SME Business Incubation Center, Chingeltei District: The SME business incubator was established in 2011 and started its operations in 2012 in the Chingeltei district of Ulaanbaatar. The center operates in this district with around 150,000 people in four branches, providing training and business advisory services to mainly start-up, small and family-owned businesses and households.

The center conducts its own research among the beneficiaries of its services. The recent report revealed the following challenges for (start-up) SMEs:

• High costs of renting a workplace: most of the businesses conduct some work-related activities at home;

• Lack of workforce: salaries that business owners pay to their workers are low compared to other sectors;

• Access to finance: most of the businesses need financing to cover working-capital needs and expand their business. Without credit history those businesses are excluded from banking services;

• Distribution of products, marketing and sales: businesses lack or are unaware of distribution channels, and face difficulties with marketing and promotion of their products. Attempts are being made to organize points of sale;

• Lack of networking opportunities: businesses lack opportunity, time and space for networking and information-sharing.

• High taxes are often the reason for start-up businesses not to register. Tax requirements are often not clear to entrepreneurs.
The ultimate goal of the incubation center is to formalize businesses. So far, however, the rate of the successful registrations has been low (10% of all 700 beneficiaries received their tax book in 2013). In total, there were 1,500 beneficiaries of the services in two years of operations.

The typical women businesses are tailoring/sewing, food production, and production of leather souvenirs, whereas men are engaged in construction, and furniture-making.

It has been observed that it usually takes about two years from start-up to maturity stage of the business development. Not many businesses reach this stage after two years. Many lack capacity and the necessary financing to survive.

Trainings provided by the SME incubation center are financed through the district budget. Cooperation experience with the banks has so far been rather modest (Kapital Bank, Golomt Bank). It has been noted that banks often do not trust to the incubator centers. They should become more proactive since both parties would benefit from such cooperation.

**Chamber of Commerce:** The Chamber of Commerce (CoC) is not a direct source of statistics on SMEs. However, it conducts market surveys to reveal the challenging areas for SMEs with the aim of relating these challenges to the regulatory bodies. The surveys conducted through the members of the CoC revealed that only 30% of SMEs have benefited from government-funded programs. It also highlighted the following challenges for SMEs:

- Low access to finance, mainly due to lack/insufficiency of collateral.
- Inflexible loan conditions, including high interest rate and low loan maturity.
- Lack of Interest at commercial banks for SMEs.
- Lending procedure at banks is cumbersome and time-consuming.
- Lack of coordination among public institutions.
- Government-loan programs not reaching out SMEs.

Nevertheless, the CoC is of the opinion that SMEs are also responsible for this unsatisfactory status of finance. SMEs in Mongolia usually suffer from lack of capacity in preparing a sound business plan and satisfactory cash-flow projections. They also do not have a thorough understanding of the market they operate in; neither can they closely follow the technological developments, nor changes in supply and demand conditions. Even for those that have a better understanding of these issues, they usually are unable to demonstrate their knowledge to creditors. They are also not financially disciplined and can get simultaneous loans exceeding their real needs, which is always a concern for commercial banks and NBFI.

In addition to previously mentioned problem areas, SMEs in rural areas face challenges, such as:

- Small market size;
- Weak purchasing power;
- Restricted access to energy sources;
- Poor infrastructure (poor road conditions, difficult transportation).

CoC also sees limited capacity of public employees in charge of implementing the SME programs as a bottleneck for the development of the SME segment.

**Business Plus Initiative (USAID)** is a finance and capacity-building program funded by USAID and implemented by Chemonics, addressing the issues of trade facilitation, taxes, construction permissions, and business registration. So far, the project has addressed these issues successfully. However, two issues remain critical: registration of movable assets and a functioning credit-information bureau. Access to finance is not addressed by the project. Insolvency and enforcement procedures remain weak and archaic in Mongolia, and need improvement. They will be in the focus of the program in the future.
BPI in the course of its activities has set up a number of institutions (to institutionalize its efforts in training and capacity building. The examples are:

**Banking and Finance Academy (BFA)** provides banking related training, owned by the banks now, established five years ago.

**Corporate Governance Development Centre (CGDC)** – the diagnostic and rating toolkit on corporate governance was developed and distributed to more than 500 companies-beneficiaries (in available in English and Mongolian).

**Quality Supplier Development Centre (QSDC)** – was initiated to address the issue of quality in production, provision of services, value chain, and capacity (how to help companies grow and meet specific demands). The mechanism of support to individual businesses (SMEs) is buyer or contract-based (transaction-based). This means that the institution identifies what large buyers of the SME are specifically looking for, what are the buyer’s standards and requirements. Based on it, the financial support and advisory is provided to an SME. It is also possible to initiate the project by contacting the supplier or the third party involved in the contract or relationship between supplier and buyer.

The QSDC is the first non-grant type of an initiative at USAID as it intends to function as a revolving fund in the future. The SMEs that can be provided with TA and financial support are selected based on three criteria: 1) their sales with support of the program should increase by 5 USD per invested 1 USD; 2) they should be registered and have a contract with the buyer of the products. To avoid the issue of double accounting, the cash flow is analyzed; 3) risk sharing, the company should be able to contribute to investment (program does not finance working capital needs). The decision is made on a case-by-case basis as per internal rating (a least 75 out of 100 points). The amount of the fund approved by USAID is 450 thousand USD. Currently 14 projects are in the pipeline. The procedures are however still at the fine-tuning stage (checklists developed). The team consists of two advisors, one senior advisor and one senior trainer will be employed in the future.

Trainings provided by the project: quality management training program; food safety management system; hazard analysis and critical control point; six sigma training (for senior management); etc. In 1,5 years, more than 300 participants representing 100 companies have benefitted from the trainings. Participants pay full price ranging from 200 to 400 thousand MNT. It was noted that trainings provided are of high level with certified international trainers.

**Japan International Cooperation Agency (JICA):**
Japan’s Official Development Assistance (ODA) expanded to Mongolia in 1990. In April 2012, a new program was approved by the government of Japan. JICA’s activities in Mongolia can be grouped in three categories:

1. **Sustainable Development of the Mining Sector:** works on the master-planning level and aims at improving productivity and efficiency in the Mongolian mining sector.

2. **Enhancement of UB as an Urban Center:** aims at improving the infrastructure and focuses on urban planning as well as management.

3. **Assisting Inclusive Growth:** (including SME activities) with the aim of increasing employment opportunities and meeting basic human needs.
Activities in the third category of operation can be summarized as follows:

JICA organizes capacity development programs for SMEs consisting of a six-week training course conducted over six months (one week training each month). The total cost of the training is born by the participants (MNT 600,000 fee charged for the training). In the last 12 years, around 700 people attended these trainings representing about 300 SMEs.

JICA also introduced the Two-Step Loan Project for SMEs Development and Environmental Protection in Mongolia in 2006. The aim of the program is to provide long-term funding through Mongolian commercial banks to SMEs. The objectives of this assistance also include the promotion of environmental preservation measures, which is an area of concern for Mongolia. In this program, Japanese government provides a concessional loan to the Central Bank of Mongolia and the Central Bank of Mongolia extends this loan to commercial banks to be on-lent to SMEs. In the two phases of the program, USD 13 million and USD 50 million respectively have so far been disbursed to final beneficiaries.

JICA does not have a women-entrepreneur-specific program, but WEs can also apply as long as they qualify for the program and the on-lending banks’ lending criteria. The program also requires applying SMEs to submit an Environmental Impact Assessment Report, the cost of which is covered by the government office.

JICA is not involved in any direct lending activities with commercial banks and/or final beneficiaries and can only support the sector via governmental institutions. Another activity of JICA within ODA has been the grant aid provided through the Ministry of Economic Development. The program was based on grants to SMEs. Nevertheless, the Japanese government decided to stop the grant component of the program as the World Bank now classifies Mongolia as a middle-income developing economy.

Business Professionals Network: Business Professionals Network (BPN) is a non-governmental organization and foundation based in Bern, Switzerland, currently active in Kyrgyzstan, Rwanda, Benin, Nicaragua and Mongolia. BPN’s office in Mongolia opened up two years ago to support the Mongolian’s craftsmen (most of which are start-ups) on their road to becoming businessmen through trainings, seminars and coaching, as well as through funding, albeit to a lesser extent.

Enterprises enrolled with BPN’s capacity building program can be registered or unregistered enterprises. Nevertheless, BPN also encourages them to get registered. BPN’s activities are centered in the capital city and only entrepreneurs based within the 100 km periphery of UB can take part in their program. Program lasts for four years and covers the following areas in 4-5 days training courses; business administration, financial management, marketing and leadership. Trainees cover about one-third of the total training cost.

The program can continue with or without the credits support by the BPN. If the applicant is found eligible for financing, a loan up to USD 20,000 can be extended with two to three years maturity and 1% monthly interest rate. BPN recently has received its license as an NBFI. Despite the detailed analysis of the entrepreneur and the project, funding provided by BNP is not free of collateral.

PBN applies certain selection criteria to identify beneficiaries for its program. The most important criterion, the business has to have potential to develop. Since the start of activities in Mongolia, BPN received hundreds of applications, 40-50 of which are selected to enroll in the training program. Only ten entrepreneurs have been granted a loan.

BPN does not have a gender-disaggregated data, but the program manager for Mongolia said that 57% of the program participants in 2013 were women. This rate is 42% thus far in 2014.
Governmental Bodies / Regulatory Institutions

Ministry of Labor: The Ministry of Labor (MoL) assumes the overall regulatory role for nationwide SMEs. The SME Development Department at the MoL is the only department authorized by law to undertake regulatory changes and make arrangements for SMEs. The Mongolian government has thus far implemented two national programs for the development of SMEs:

- First program implemented between 1999-2004 prioritizing the issues related to infrastructure of SMEs;
- The second program between 2006-2012 focusing on enhancement of the legal and policy framework such as the enactment of the Law on SMEs, Law on Legal Status of Industries, Law on Science and Technology and the Law on Credit Guarantee Fund, etc.

The responsible governmental authorities are continuing their discussions on a third program. The five targeted goals of the new program can be categorized as follows:

- Creation of product marketing and selling opportunities for SMEs;
- Cluster development;
- Capacity building at the SMEs;
- Capacity building for the MoL staff at UB city center and aimag centers;
- Ensure harmonization between the laws.

Two international institutions are active cooperating partners to MoL: JICA (in the field of capacity development) and EBRD (concerning legal advisory). A sizeable portion of SMEs in Mongolia are unregistered. The MoL is also working on developing an incentive system to encourage SMEs to register.

MoL is not directly in charge of collecting data on SMEs in Mongolia. SME data is rather collected by two other sources: National Statistical Office and the Tax Office. MoL admits that there is currently no gender disaggregated data on SMEs.

Legal Company

Anand Advocates: Anand Advocates is recognized as one of the leading professional law firms in Mongolia. The company operates since 2003 and provides services in all areas of Mongolian law as well as international commercial and business law with over 20 qualified lawyers. The firm’s practice areas are:

- Banking & Finance,
- Corporate and M&A,
- Natural Resources & Energy,
- Tax Advisory Services,
- Litigation and Bankruptcy,
- Real Estate.

Below are the issues highlighted by Anand Advocates regarding the business enabling environment and finance sector in Mongolia.

- The Law on the Credit Guarantee Fund (CGF) was enacted in February 2012 and the Credit Guarantee Fund of Mongolia started operations in 2013. Nevertheless, the existing law does not specify the collection procedures for the CGF in case of a default.
- Business registry is not a major concern for enterprises as far as the time to register a business is concerned. Nevertheless, registry office employees lack the knowledge and information demanded by the entrepreneurs. They are also not very service-minded;
- Closing a business requires the inspection by tax authorities, who usually act slowly;
- Registry of movable property remains an obstacle, especially for SMEs and the draft bill on the pledging the movable property should be discussed and finalized as soon as possible;
- In case of default, the value of property can be an issue of dispute between the borrower and the creditor. The court procedure may take very long as consensus between parties on the selling value of the property under hypothec is required for the property to be sold.