

CASE STUDY

Supporting Small Businesses through Microfinance



Women borrowers start small businesses in Mongolia's ger areas. Photo credit: ADB.
In Mongolia, ADB supports a new way of banking without collateral to improve credit access for women and small businesses.

Published: 14 October 2019

Overview

A loan by the Asian Development Bank (ADB) to a private sector bank served the financing needs of micro, small, and medium-sized enterprises (MSMEs) in Mongolia. This project highlighted the benefits of promoting private sector development as key driver for strengthening inclusive financial growth, long-term investment, innovation, and access to finance. It complements ADB's support for reducing poverty and improving the living conditions of *ger* areas in Mongolia.

Project snapshot

Dates

- **12 December 2013:** Approval date
- **September 2017:** Extended annual review report date

Cost	<ul style="list-style-type: none"> • \$30 million: Amount of Loan
Institutions and Stakeholders	<p>Executing agency</p> <ul style="list-style-type: none"> • XacBank <p>Financing</p> <ul style="list-style-type: none"> • <u>Asian Development Bank</u>

Context

Micro, small, and medium-sized enterprises (MSMEs) make up 90% of all enterprises in Mongolia, three-fourths of which are microenterprises. More than 30% of small and medium-sized enterprises (SMEs) in Mongolia perceive access to finance as the largest issue for their operations. Only about 10% of around 37,000 Mongolian SMEs regularly access finance through banks. When finance is available to SMEs, loan terms and conditions are characterized by high-interest rates, shorter maturities, and smaller amounts that do not meet the full financial needs of these companies.

Development Challenge

The development of small businesses is critical for the diversification of Mongolia's economy, which relies heavily on the mining industry. The government prioritizes developing MSMEs, enhancing their capacities so that enterprises can create jobs. To support this priority, the government has established development and credit guarantee funds for MSMEs. However, the supply of credit under government programs fell short of meeting the demand for financing by MSMEs. A large proportion of MSMEs in *ger* areas is still seeking access to longer-term finance and formal sources of credit. There is, therefore, a very significant unmet demand for credit from all MSME segments in Mongolia, and commercial banks are seeking to raise additional sources of funding to respond to this.

Solution

To support the financing needs of MSMEs including those that cannot meet the traditional collateral requirements, ADB approved in 2013 a \$30 million loan to provide accessible funds for MSMEs, of which \$6 million would be onlent to those operating in the *ger* areas.

XacBank, Mongolia's fourth-largest commercial bank, was selected as the financial intermediary to channel funds to MSMEs because of its experience in lending to lower-income businesses in *ger* areas. XacBank operates in all 21 provinces and in Ulaanbaatar, serving more than 800,000 customers through its 86 branches. It has about 1,300 staff and 3,000 mobile banking merchants. The shareholders of its parent company, the TenGer Financial Group LLC, include the International Finance Corporation and

the European Bank for Reconstruction and Development.

Results

Better access to finance for MSMEs in *ger* areas, particularly women

In 2016, the project has lent to 21,517 MSME borrowers. Even though XacBank's MSME total loan portfolio declined in USD in 2015–2017 because of a weakened operating environment and depreciation of the local currency, the share of women borrowers has been maintained at almost half of the total MSME portfolio. The project reached 13,346 rural borrowers and extended 882 loans to *ger* areas.

Strong financial capacity and services

The total MSME portfolio of XacBank was \$317 million in 2016. Despite a difficult economic environment from 2015 to 2017, XacBank maintained its MSME portfolio above 60% of the total loan portfolio in 2016. As MSMEs are more vulnerable during the economic downturn, XacBank's nonperforming loan ratio increased significantly, although asset quality subsequently recovered due to strong risk management capacity of the bank. Its capital adequacy ratio stood at a robust 19.2%, above the 18.92% industry average. This performance reflected the bank's stable standing in times of economic stress.

Innovative ways of banking

XacBank introduced innovative and effective banking services to MSMEs under the project. Most MSMEs lack immovable assets such as lands and real estate that can serve as collaterals to secure bank finance making it too risky for commercial banks to lend on unsecured basis. A first in Mongolia, XacBank introduced a new supply chain finance product that discounts invoices issued by multinational companies involved in large mining projects to local suppliers (MSMEs). The financing provided to MSMEs was secured by receivables from large corporations rather than immovable assets.

Lessons

Achieving the project's performance targets was challenging because of the weak economic environment in Mongolia. From 2015 to 2017, the Mongolian economy was constrained by weak commodity prices (mainly in coal) in the international market and its lack of diversification. Despite this, ADB disbursed the loan to XacBank, adding a significant boost to MSMEs' operations. This is a vital factor that helped MSMEs during the economic downturn. Given the current improvement in the economy, XacBank will further grow and expand its services to MSMEs, including those in the *ger* areas.

Resources

Asian Development Bank. 2013. *Report and Recommendation of the President to the Board of Directors: Proposed Senior Loans XacBank and Tenger Financial Group Supporting Micro, Small, Medium-Sized Enterprises and Leasing Finance in Mongolia*. Manila.

ADB. 2017. *Extended Annual Review Report: Senior Loan XacBank Supporting Micro, Small, and Medium-Sized Enterprises in Mongolia*. Manila.



Biao Huang

Unit Head, Private Sector Financial Institutions, East Asia Private Sector Operations Department, Asian Development Bank

Mr. Biao Huang leads the debt and equity transactions of private-sector financial institutions at ADB's East Asia Private Sector Operations Department. Prior to joining ADB, he was a senior consultant at a UK-based consultancy firm and a researcher at the University of Oxford. He received his PhD in Economics from the University of London and is a CFA charterholder.



Asian Development Bank (ADB)

The Asian Development Bank is committed to achieving a prosperous, inclusive, resilient, and sustainable Asia and the Pacific, while sustaining its efforts to eradicate extreme poverty. Established in 1966, it is owned by 68 members—49 from the region.

Its main instruments for helping its developing member countries are policy dialogue, loans, equity investments, guarantees, grants, and technical assistance.

Follow Asian Development Bank (ADB) on

