



# ANNUAL REPORT 2016





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## ABBREVIATIONS

ADB	Asian Development Bank
AFI	Alliance for Financial Inclusion
CBPR	Central Bank Policy Rate
DVP	Delivery versus Payment
FDI	Foreign Direct Investment
FRC	Financial Regulatory Commission
GDP	Gross Domestic Product
IMF	International Monetary Fund
IOSCO	International Organization of Securities Commissions
IPO	Initial Public Offering
JICA	Japan International Cooperation Agency
JSC	Joint Stock Company
LLC	Limited Liability Company
MC	Market Capitalization
MIK	Mongolian Mortgage Corporation
MNT	Mongolian Tugriks
MSE	Mongolian Stock Exchange
MSTAP	Multi-Sectoral Technical Assistance Project
MOCCU	Mongolian Confederation of Credit Unions
NBFI	Nonbank Financial Institutions
OECD	Organization for Economic Cooperation and Development
SCCs	Savings and Credit Cooperatives
SCHCD	Securities Clearing House and Central Depository
SCs	Securities Companies
SMEs	Small and Medium Enterprises
SRO	Self-Regulatory Organization
SPC	Special Purpose Company
UK	United Kingdom
USA	United States of America
USD	United States Dollar

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## MESSAGE FROM THE CHAIRMAN

It has been a challenging and difficult year as Mongolia encountered economic hardship. The consequences of poor governance and government overspending resulting in the loss of investors' confidence, and declining global market prices of mineral resources and raw materials unfavorably impacted the lives of citizens. The economy encountered further hardship as Mongolia's unexpected debt level and payments rose and the credit rating declined constraining foreign direct investment.

In the light of existing social and economic circumstances, the Financial Regulatory Commission of Mongolia (FRC) made major shifts in its policy and operational activities by re-defining its short-term and long-term strategic objectives. However, the FRC remains committed to its supervisory responsibilities including licensing institutions; regulating and developing the financial sector to minimize risks; and to protect the rights and interests of participants. In this respect, the FRC has taken gradual and consistent steps towards achieving set objectives and goals to strengthen the capital market, enhance infrastructure of clearing and settlement system, entice institutional investors, expand the product lines and services offered by the nonbank financial sector, boost competitiveness, and provide an enticing business environment for clients, investors, consumers, and shareholders.

The banking sector is the main platform supporting Mongolia's financial system. We have therefore implemented a counter-cyclical policy as part of

building strong nonbank financial institutions, which is significant to overcoming the existing hardship and difficulty and preventing systemic risk. We believe that reinforcing privately managed asset and financial management firms towards establishing an efficient business sector backed by research and analysis is not only in the greater interest of professional participants but also consumers.

In achieving our future and short-term objectives and defining development policies and strategies, the Law on the Legal Status of the Financial Regulatory Commission and respective laws are presently being revised. Our utmost effort will focus on improving our organizational structure and ensuring regulatory practices in adherence to international standards towards sustainable development.

This report summarizes some of our major achievements, the outcomes of policies we have implemented as well as the strategic objectives for the future and approaches we can take to achieve them. I hereby present you the Annual Report for 2016 of the Financial Regulatory Commission.

Your comments will be greatly appreciated.

Dr. Davaasuren Sodnomdarjaa  
Chairman

## SUMMARY

In 2016, there were adverse impacts to the economy due in particular to the decline in international trade and investment, and uncertainty in legal and regulatory environments. Nonetheless, international regulatory authorities in collaboration with their financial market participants have developed programmes to overcoming the economic downturn at low cost along with their short and mid-term strategies to be implemented in support with their respective governments.

2016 was unfavorable to Mongolia's macro economy with a decline in foreign direct investment, appreciation in foreign currency rate, stagnant economic growth and decreases in mineral and raw material prices. The Government's focus on harmonizing the regulatory environment market capitalization of the nonbank financial sector, which reached MNT20.2 billion, an increase of 20% compared to the 2015. The share of nonbank financial sector GDP was 10.9% an increase of 1.7% over 2015. Although some development indicators rose for some sectors, no relevant improvements were witnessed in terms of quality of their operations. Thus, the legal and regulatory environments of respective sectors must be improved in conjunction with social and economic changes and technology advancement.

The main indicators of capital market development – market capitalization, liquidity and trade turnover; rose in 2016 in comparison with those of last year. This demonstrates the increased interest of foreign and domestic investors and the potential to grow the capital market in compliance with international standards.

Even though most indicators for insurance market are growing consistently, insurance penetration and density are low in relation to the international average, without noticeable improvement in recent years. The latter indicates the necessity to improve public awareness about insurance and at the same time, promote new products and services.

At the end of 2016, the total asset of nonbank financial institutions was MNT787.2 billion, which can mostly be attributed to the resetting of minimal capital requirement and further gradual increase for nonbank financial institutions. The FRC is predicted to rise by 26% to MNT992.5 billion in following given the expansion of inclusive finance.

On the occasion of the 20th Anniversary of Savings and Credit Cooperative, members from 135 cooperatives, guests from international organizations, and Mongolian Confederation of Credit Unions in cooperation with the FRC organized a second national forum, "Together Towards Development." The conference focused on overcoming the economic hardship by promoting low-cost financial products and services, and learning from international, Asian cooperatives.

Ensuring access to affordable priced financial products and services, minimizing unit cost of financial products, promoting the use of advanced technologies, providing infrastructure for sustainable and accessible financial sector, facilitating access of low and middle-income citizens to financial products and services, protecting the rights of consumers, and developing policies consistent with promoting financial inclusion are one of the main objectives of globalization.

The FRC, as a regulatory and supervisory institution, is presently implements and enforces 18 applicable laws of Mongolia. In implementing those laws, in 2016 the FRC conducted off-site and on-site supervision of 302 joint stock companies, 62 securities companies (SCs), 17 insurance companies, 40 insurance intermediaries, 31 insurance loss-adjusters, 3091 insurance representatives, 42 auditing firms exclusive to insurance companies, 518 NBFIs, 280 savings and credit cooperatives, and 1324 entities under regulation to ensure compliance with requirements of financial solvency and prudential ratios. Appropriate measures were taken in cases where laws were breached or violated. Finally, the FRC continued its efforts to protect consumers' rights and ensure implementation of risk-based supervision system in each sector.



# 1

## CURRENT STATUS OF THE FINANCIAL SECTOR

## 1.1. GLOBAL FINANCIAL MARKET TREND

Declining international trade flow and investment, and uncertainty over the legal and regulatory environments imposed additional constraints to the economy. Although global economic growth reached 2.3% in 2016—its lowest point since the economic slowdown; the economies of developing nations are predicted to recover in 2017 with growth expected to reach a rate of 2.7%.

The economic growth of developing nations reached 1.6% in 2016. Due to uncertainty over the decisions of policy-makers and investors and weakening economic productivity, economic growth of developing countries slowed down; and inflation remained at a declining rate. In the upcoming year, developing economies improve and are predicted to reach a growth rate of 1.8%. Economic growth for the next two years is expected to reach 2.2% as major advancements in the agricultural sector of the United States of America (USA) have recently been discovered. Though, this estimation does not take into account regulatory influence, the FRC believes implementing profit-oriented policies will help ensure economic growth. Although inflation is expected to rise steadily in the Euro zone and Japan, the Mongolian growth rate will likely remain below the rate set by the Central Bank.

While economic growth of developing nations increased by 3.4% in 2016, it is predicted to reach 4.2% for the first time since 2013, comprising majority of world's economic growth rate. Stabilizing raw material prices predicted to increase steadily throughout 2017–2019, are likely to affect and support the economies of exporting and developing countries. The 2016 US presidential election resulted in an increased return on investment, which, in turn, caused the economies of developing nations to shrink as their exchange rates depreciated and investment inflow, declined. However, the financial state of these economies is considered stable, except under the above circumstances. Two-thirds of developing countries are reliant on export products such as crude oil, metal, and agricultural products. The fact that the global market price of raw materials

fell by more than 40% compared to 2011 caused trade agreements to decrease by 4% and export of crude oil by 21%. Foreign direct investment, on the other hand, increased by almost three times compared to 2000, which presently constitutes 1/3 of world's total foreign direct investment.<sup>1</sup>

China's major its economic policy shift along with the Federal Reserve's decision to increase its policy rate (CBPR) caused stock prices to fluctuate while, at the same time, the UK's Brexit decision to leave the European Union last June harshly hit the global market. Moreover, US President Trump's election, along with his Administration's decision to decrease tax, de-regulate legal and regulatory environments, increase spending on infrastructure and military budget, have been additional shocks to the capital market.

Revenue growth of global non-life insurance premium slowed down.<sup>2</sup> While the growth of net revenue reached 3% last year, it has increased by 2.4% for this fiscal year and total premium revenue decreased from 2.5% to 1.7% as developing nations faced slowing economic growth and flexible prices of insurance products. As for developed nations, insurance premium revenue increased steadily to 5.3%, reflecting a slower annual growth rate in relation to the average rate of 8% reported for the period of 2000–2014.<sup>3</sup>

The expansion of vehicle-insurance products and services, which constitutes 60% of non-life insurance market<sup>4</sup>, contributed significantly to the growth of total premium revenue of developing nations. In 2016, the global growth rate of life-insurance premium revenue increased to 5.4% compared to 2015. While the revenue growth rate of developing nations reached 3.4% in 2015, it decreased to 2% in 2016. The economic growth

1 World Bank — World economic prospects/Weak Investment in Uncertain Times/ ,January 2017

2 Swiss Re (2016a): Global insurance review 2016 and outlook 2017/18, November.

3 IAIS: Global Insurance Market Report 2016

4 Swiss Re (2016b): The future of motor insurance: How car connectivity and ADAS are impacting the market, March

of developing nations in particular, the increased growth rates of Asian countries influenced the growth of global life–insurance market. The growth rate of developing nations increased by 6.9 units, a reaching 20.1%.

Based on a decision issued by the International Organization of Securities Commissions' (IOSCO) in September 2014 on long–term market–based financing research titled “Financing of Small and Medium Enterprises and Infrastructure Projects”, financial instruments were classified by their respective types classifications took into consideration the targeted objectives of long–term market–based financing, which can be divided in two parts; one supporting small and medium enterprises and the second for improving the infrastructure. The amount of long–term financing provided by the banking sector to small and medium enterprises declined as the Basel Committee on Banking

Supervision set new prudential ratio requirements of private asset and liquidity levels for commercial banks. As a result, both developing and developed nations have been compelled to raise financing via/through the capital market and direct nonbank financial services to support SMEs and infrastructure projects.

As a member of 119 authorities (financial regulatory authorities and central banks) from 95 developing nations, the Alliance for Financial Inclusion (AFI) is presently focusing its efforts in ensuring access to financial services to the poorer population covering 85% of microfinance sector and including policy–makers from developing and developed nations. As an AFI member since September 2016, the FRC is participating in all working groups as part of exchanging expertise and best practices with fellow members.

## 1.2 CURRENT STATUS OF NONBANK FINANCIAL SECTOR

The market capitalization of the nonbank financial sector reached MNT2.6 trillion, an increase on average of 20%. Recent changes to the legal and regulatory environments were the main influencing factors. The share of the nonbank financial sector to GDP stands at 10.9% is an increase by 1.7% compared to 2015.

Market capitalization of two prominent companies, whose IPOs were issued in 2015, were taken into account in calculating the 2016 market capitalization of the banking sector, which have mainly influenced the market capitalization and trade volume to increase. The FRC made amendments to its regulation on Securities Registration to support access to new financial products and services for the securities market and to improve systems of self–regulatory organizations. The FRC regards attaining of these goals as an important step towards increased listings on the Mongolian Stock Exchange JSC, reducing duplication of duties and functions and providing a favorable environment for increasing long–term financing.

The FRC is presently working towards implementing

spot trading in trading agricultural and raw material products and, upon successful implementation of the program, it is predicted that the trade volume and liquidity of raw materials will improve as futures trading starts taking effect in 2017.

In the insurance sector, insurance premium revenue increased by 0.6% while total assets increased by 20.3%. In line with the Government's guideline on preventing risks associated with unexpected weather conditions faced by farmers, the line of agricultural insurance products was expanded and MNT302.4 million of products have been insured through insurance companies. Currently, the FRC is working to optimize the regulations on mortgage insurance.

Since 2013, the number of NBFIs has risen rapidly. Given the FRC's decision to gradually increase the equity share of NBFIs, the number of NBFIs and their total assets have risen by 15 and 26% respectively. This year the number of NBFIs customers fell while the amount of non–performing loan reached 12.4% – a unit increase of 2.6% compared to same period in 2015.

The total assets and number of savings and credit cooperatives rose by 15.8% and 10.7% respectively. The Law on Savings and Credit Cooperatives needs to be revised to ensure compatibility with future social and economic circumstances.

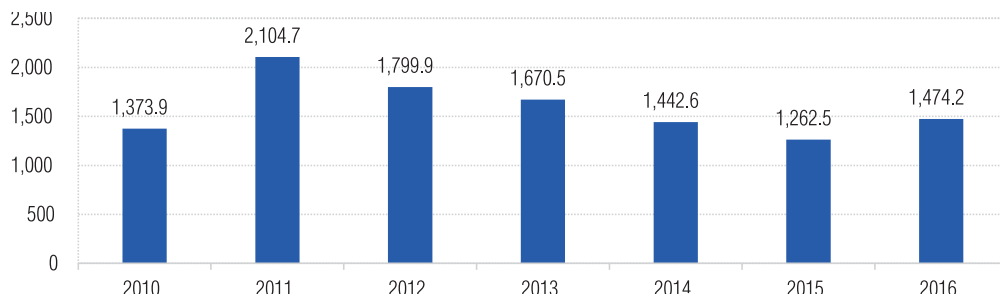
### 1.2.1 SECURITIES MARKET

The International Monetary Fund and the World Bank assess the level of capital market development based on indicators of market capitalization, market

liquidity, GDP share of securities trading, GDP share of market capitalization as well as on stock indices. Based on these indicators, the level of participation of foreign and domestic investors and whether investment prospects are present for countries subject to assessment to compete regionally are determined.

Market capitalization refers to the size of the market and is the main determinant of market growth. It assists in determining the level securities market development, thus evaluating its impact on economic growth.

Figure 1. Market Capitalization /MNT billion/



Source: The Financial Regulatory Commission

As of year-end 2016, securities market capitalization reached MNT1,474.2 billion as opposed to MNT211.7 billion as of last year, an increase of 16.8%. In 2015, 1.6 million shares worth MNT19.5 billion issued by “MIK Holding” JSC and 34% or 33.9 million shares worth MNT6.3 billion, of some prominent joint stock companies were issued and traded as IPOs in 2016. The contributions of these two companies largely contributed to the increased market capitalization figure.

As of second quarter of 2016, the expectation of price increases in global prices of raw materials caused the share prices of several mining companies to increase by 19.1% and the share prices of five prominent joint stock companies on TOP-20 index, which constitute the majority of the percentage share of total market capitalization, to increase by an average of 21.94%. These outcomes greatly influenced the market capitalization increase.

Market Capitalization (MC) as percentage of GDP and liquidity level: as of year-end 2016, MC as percentage of GDP stood at 6.2% which indicates an increase of 0.8% compared to the same period last year. Liquidity, on the other hand, stands at 3.3%, which is an increase of 0.92% as compared to the same period last year.

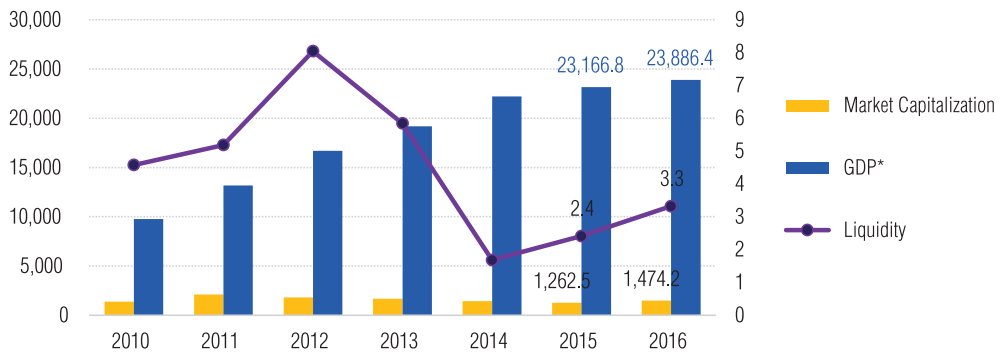
NOTE: Mongolia, with rapid expansion of the mineral industry, reached an economic growth of 17.5% in 2011 and was rated as one of the best-performing economies in regional and international markets. Stock value of mineral companies, main performers of Mongolian Stock Exchange's Top-20 index has risen as a result this rapid growth. Likewise, the number of foreign and local investors, and brokerage firms also increased. Stock market capitalization and market liquidity have however been decreasing as fall in global raw material prices in the mining industry, decline in foreign direct investment (FDI) and resulting economic slowdown persisted since 2012.

Although legal and regulatory environments of the capital market have been improving in recent years and despite the effort to establish optimal system of supervision, lack of solid capital market infrastructure in particular sound clearing and settlement system, lack of cooperation among brokerage firms, poor delivery of products and services, and low trade volume and market liquidity are adversely affecting capital market development.

While 33.9 million shares worth MNT6.3 billion of these 11 companies were traded on the primary market, 41.9 million shares worth MNT34.1 billion of those were traded as portfolio-trading resulting in increased liquidity. Portfolio trading has constituted 69.6% of total stock trading in 2016.

Stock concentration of MSE listed companies, poor governance, low transparency, shortage of financial products and services, and a lack of knowledge on investment and stock trading are indicative of Mongolia's relatively low level of stock liquidity in relation to other developing nations.

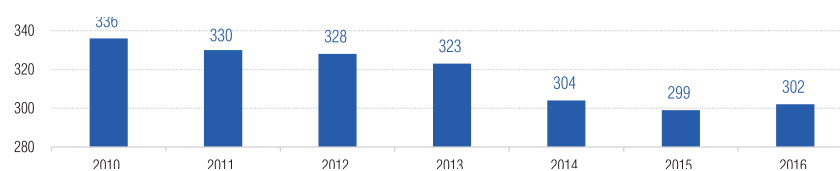
Figure 2. Market Capitalization and GDP



Source: The Financial Regulatory Commission

Market participants: There are total 302 joint stock companies registered in the FRC's securities registration as of this fiscal period.

Figure 3. Number of JSCs



Source: The Financial Regulatory Commission

Table 1. Ownership and numbers of JSCs

Ownership structure of shareholders	FRC	Mongolian Stock Exchange JSC	Securities Clearing House and Central Depository
State-owned	31	19	21
Parastatal	19	15	22
Private ownership	252	185	269
<b>Total</b>	<b>302</b>	<b>219</b>	<b>312</b>

Source: The Financial Regulatory Commission

Professional market participants: There are 62 qualified securities companies, two securities trading, one clearing and settlement company, one central depository, three custodian services, 12 asset investment management companies, one agricultural and commodities exchange, and 37 raw materials exchanges operating under the FRC's licensure. In

2016, it is estimated that the MSE traded a total of MNT348.7 billion worth of securities, a decrease of 36.1% in comparison with the previous year's estimate. 14.1% of total trade volume consisted of shares of stocks with the remaining 85.9% in Government bonds.

Table 2. Trade Indicators

Type of securities		Number of trade	Traded number of stocks /million/	Trade amount /MNT billion/
Share	Primary market	1	33.9	6.3
	Secondary market	244	59.8	42.7
Government Bond	Primary market	31	3.1	280.5
	Secondary market	77	0.196	19.2

Source: Mongolian Stock Exchange

Stock trading: Mongolian Stock Exchange JSC traded 93.7 million shares of 126 companies worth MNT49 billion in 244 trade sessions. 69.6% or MNT34.1

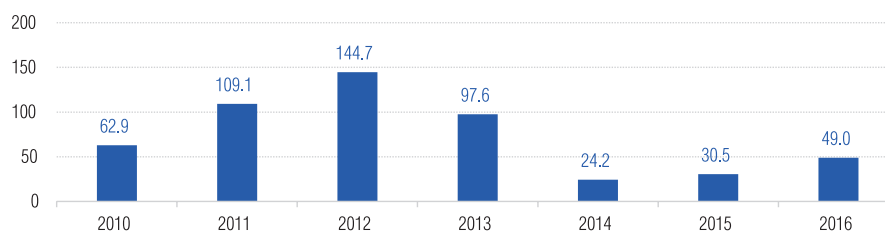
billion worth of stock trading was portfolio trading, while the remaining 30.4% or MNT14.9 billion worth of stock trading was regular trading.

NOTE: Mongolian securities market infrastructure is underdeveloped in relation to other emerging nations in particular clearing and settlement system. Lack of cooperation among professional intermediaries, poor delivery of new products and services, and low trade volume and market liquidities are adversely affecting market growth.

In an effort to enhance the role of market intermediaries and establish professional brokerage companies with competent human resource, the FRC is working towards increasing the participation of foreign and local investors and rebuilding trust in the market by means of establishing payment guarantee fund and introducing DVP settlement system along with transitioning to T+2 and T+3 settlement cycles as a part of second phase of the Mongolia Multi-Sectoral Technical Assistance Project implemented by the World Bank.

As a result of increased number of securities companies with competent human resource and financial solvency operating in accordance with applicable laws and regulations, it is expected that market infrastructure will be improved, payment guarantee fund will be set-up, trade volume and market liquidity levels will be progressed, and transition to T+2 and T+3 settlement system will be successfully implemented.

Figure 4. Stock trading /MNT billion/



Source: The Financial Regulatory Commission

As of 2016, 41.9 million shares of 11 companies worth MNT34.1 billion were traded with 69.6% of total amount of stock trading consisting of portfolio trading.

Asset-backed securities trading: A total of 7730 credit portfolios of four special purpose companies

–“MIK Asset Eight SPC” LLC. “MIK Asset Nine SPC” LLC., “MIK Asset Ten SPC” LLC., “MIK Asset Eleven SPC” LLC., “MIK OSSC” LLC., founded under the parent company, “MIK OSSC” LLC., consisting of asset-backed securities worth MNT501.2 billion were registered within the fiscal period.

Table 3. Asset-backed securities /MNT billion/

No	Asset-backed securities issuer	Issued securities	Registered in SCHCD LLC	Number of creditors
1	"MIK asset one SPC" LLC	328.1	322.9	6,658
2	"MIK asset two SPC" LLC	224.8	222.1	5,290
3	"MIK asset three SPC" LLC	328.5	324.6	6,593
4	"MIK asset four SPC" LLC	459.4	452.3	9,510
5	"MIK asset five SPC" LLC	301.2	294.3	5,805
6	"MIK asset six SPC" LLC	267.8	261.7	5,188
7	"MIK asset seven SPC" LLC	299.6	293.8	5,414
8	"MIK asset eight SPC" LLC	189.8	186.3	3,291
9	"MIK asset nine SPC" LLC	137.5	137.2	1,719
10	"MIK asset ten SPC" LLC	103.0	–	1,585
11	"MIK asset eleven SPC" LLC	70.9	–	1,135
	<b>Total</b>	<b>2,710.6</b>	<b>2,495</b>	<b>52,188</b>

Source: The Financial Regulatory Commission

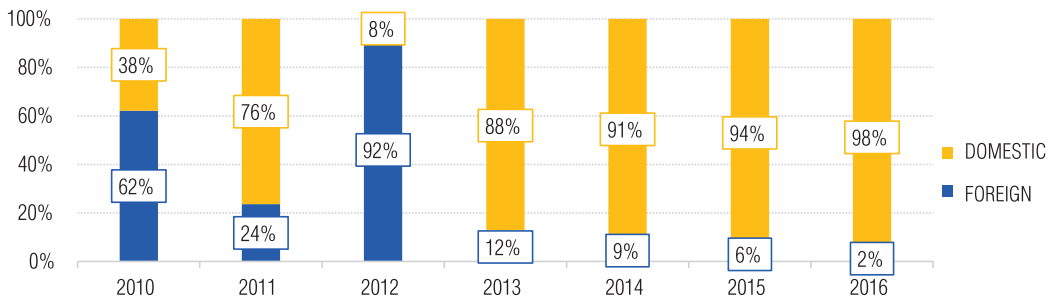
Agricultural Commodities Exchange: "MACE" LLC. traded MNT463 billion worth of commodity products and raw materials through 181 trading sessions, an increase by MNT29.1 billion or 6.7% when compared to last year. The products sold—cashmere, sheep wool, camel wool, unprocessed goat wool, and cattle wool were worth respectively MNT409.7 billion, MNT26.2 billion, MNT3.9 billion, MNT3 million, and MNT70 million traded at "MACE" LLC.

Investors in the securities market and structure of account: "Mongolian Stock Exchange" JSC recorded registrations of 886,590 regular and 139,288 intermediary accounts in the secondary market depository.

Registered accounts consist of 881,962 domestic and 1,920 foreign investors, and 2,530 domestic and 178 foreign entities. Within the fiscal period, the Mongolian Central Securities Depository registered total 81,017 new accounts, of which 80,899 belong to domestic investors, 66 to foreign investors, 50 to domestic entities, and two to foreign entities.

Within the fiscal period, the sum of shares traded by foreign investors and entities in the "Mongolian Stock Exchange" JSC's constitute 2% of total sum of shares traded at the MSE while domestic investors and entities made up the remaining 98%.

Figure 5. Investors per trade /percentage/



Source by SCHCD<sup>®</sup> LLC

Despite Mongolia's declining macroeconomic indicators, slowing economic growth, and unfavorable economic circumstances, the indicators of capital market development—market capitalization, liquidity, and stock trade volume rose in 2016, which are incentives to domestic and foreign investors.

The Mongolian Central Securities Depository registered a total of 81,017 new accounts, domestic and foreign investors combined. Within the fiscal period, a total of MNT501.2 billion worth of securities were traded on the primary market for asset-backed securities, which represents prospects for further development of the secondary market and trading more openly.

In an effort to improve the legal and regulatory environment of the securities market and support participation of domestic and foreign investors, recommendations for amending to sector-related legislation and developing laws governing new relations have been put forward in the "General Directives for optimizing Mongolia's Legislations Until 2020" approved by the State Great Khural in 2016.

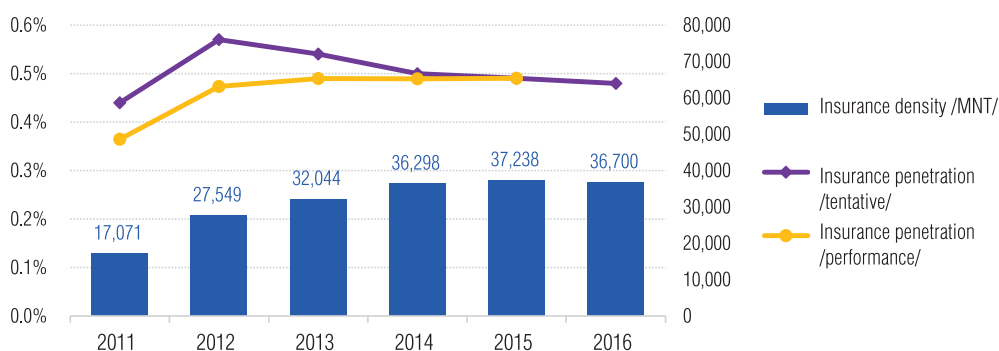
## 1.2.2 INSURANCE MARKET

The insurance sector is responsible for maintaining financial stability and enhancing economic growth through optimizing financial resource distribution and risk redistribution and risk shifting mechanism.

Market capability of insurance sector was decreased by 27.5% from a year earlier and represented 0.87% of Gross Domestic Product (GDP).

NOTE: During the year, gross premium income to GDP or insurance market penetration rate shared only 0.48% of the GDP by which described 5.8 times and 13.5 times lower rates than emerging economies and global average. (Source: OECD, Global insurance trends 2015)

Figure 6. Insurance penetration and density



Source: The Financial Regulatory Commission

At the end of 2016, insurance premium per person had decreased by 1.4% as compared to a year earlier when it accounted for MNT36,700.

## INSURANCE SECTOR INDICATORS

There were 17 insurance companies, 40 insurance intermediary companies, 31 insurance loss adjuster companies, 242 insurance companies' branches, 10 insurance representative offices, 208 insurance intermediaries' companies, 50 insurance loss adjusters' branches and 2 representative offices at the end of 2016.

Table 4. Number of license holders in insurance market

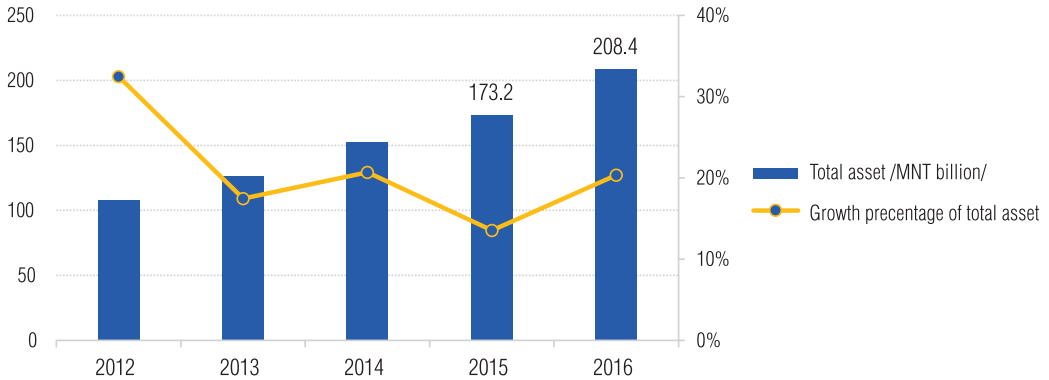
No		2010	2011	2012	2013	2014	2015	2016
1	General insurance company	16	16	17	16	16	15	15
2	Life insurance company	1	1	1	1	1	1	1
3	Reinsurance company	-	-	-	-	-	1	1
4	Insurance representative	2061	2057	2357	3187	3260	3340	3091
5	Insurance broker	9	8	17	20	30	37	40
6	Insurance loss adjuster	6	9	9	14	20	27	31
7	Actuary	12	13	18	15	15	15	15
	<b>TOTAL</b>	<b>2104</b>	<b>2103</b>	<b>2419</b>	<b>3253</b>	<b>3342</b>	<b>3436</b>	<b>3194</b>

Source: The Financial Regulatory Commission

Insurers' assets: Aggregate asset of insurance companies reached to MNT208.4 billion which

represented an increase of MNT35.2 billion or 20.3% from a year earlier.

Figure 7. Asset growth of insurance companies



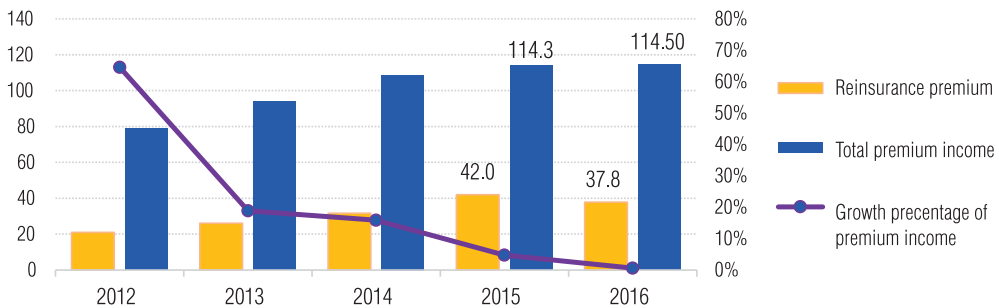
Source: The Financial Regulatory Commission

Assets in insurance accounts made up by 79.6% of nonlife, 16.8% of reinsurance and 3.6% of life-insurance company assets.

During the year, insurance companies sold 1,069,856 policies and raised MNT114.5 billion of premium

income. Nonlife insurance, Life insurance and Reinsurance Company's premium income increased to MNT111.7 billion, MNT1.2 billion and MNT1.6 billion, respectively. Insurance premium income increased by 0.6% or MNT0.6 billion in 2016.

Figure 8. Premium income and reinsurance premium



Source: The Financial Regulatory Commission

Reinsurance premium income has been increasing steadily.

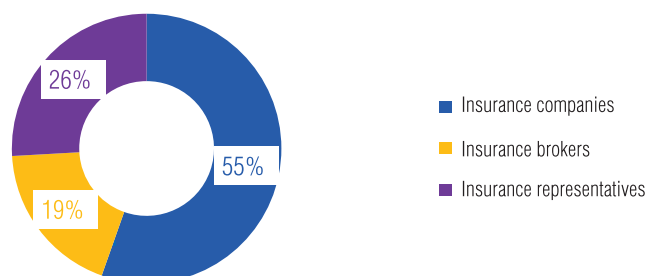
For premium income, accident, health, property and car insurance represented 75.5% of the total premium.

Table 5. Insurance premium income /type/

№	Insurance type	Insurance premium income		Changes +/-
		2015	2016	
1	Accident and treatment insurance	10,612,015,862.3	12,331,737,772.7	16.2%
2	Property insurance	40,884,297,808.4	31,793,234,171.0	-22.2%
3	Vehicle insurance	15,676,414,189.5	14,481,925,482.9	-7.6%
4	Transportation insurance	2,375,826,966.0	1,943,624,943.2	-18.2%
5	Construction insurance	2,002,547,550.0	3,266,532,235.1	63.1%
6	Agricultural insurance		13,699,146.0	
7	Livestock insurance	709,666,385.7	1,158,512,708.2	63.2%
8	Airship insurance	3,489,678,425.5	3,211,073,279.2	-8.0%
9	Driver's liability insurance	389,586,492.0	458,880,469.9	17.8%
10	Liability insurance	7,335,783,807.5	7,857,252,716.7	7.1%
11	Financial insurance	3,197,292,592.5	3,232,588,355.9	1.1%
12	Credit insurance	769,849,914.4	1,032,576,630.7	34.1%
13	Trust insurance	25,292,935.7	280,580,893.7	1009.3%
14	Liability insurance of airship owning, holding and utilization	1,817,649,110.7	2,818,819,047.1	55.1%
15	Driver's insurance	22,927,430,530.5	27,795,509,631.4	21.2%
16	Term life insurance	345,164,043.8	176,891,345.0	-48.8%
17	Life insurance	-	-	-
18	Accumulation insurance	75,148,081.5	69,836,168.0	-7.1%
19	Pension insurance	47,873,111.4	55,043,569.8	15.0%
20	Health insurance	1,184,640,990.9	966,913,930.5	-18.4%
21	Annuity insurance	-	-	-
22	Agricultural reinsurance	-	13,014,188.7	
23	Livestock reinsurance	-	1,543,701,794.6	
	Total	113,866,158,798.2	114,501,948,480.0	

Source: The Financial Regulatory Commission

Figure 9. Insurance premium income

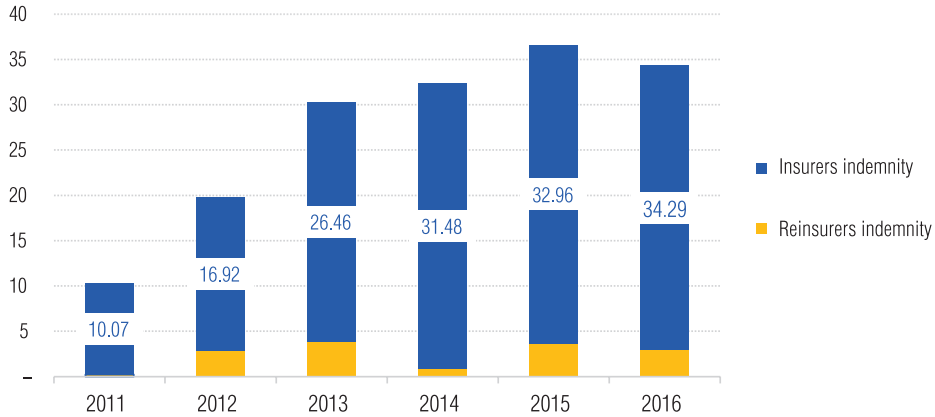


Source: The Financial Regulatory Commission

Insurance indemnity: Insurance companies issued payout amounts for MNT34.3 billion to 64,276

policyholders, which showed a decline of 6.2% than the previous year.

Figure 10. Total insurance indemnity /MNT billion/



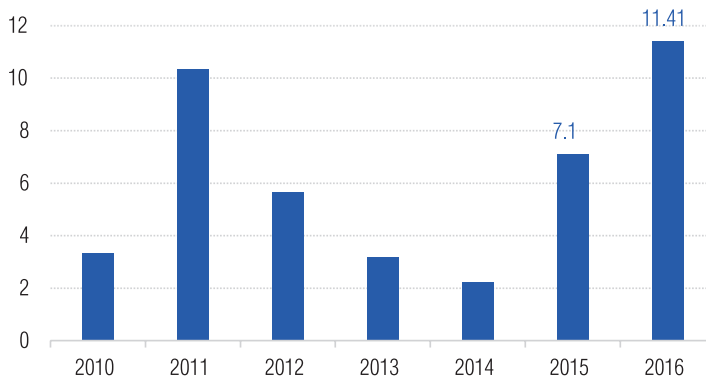
Source: The Financial Regulatory Commission

Companies paid a total of MNT14.8 billion in claims to driver's mandatory insurance policy holders and MNT7.9 billion for car insurance policy holders as highest amount for payout.

Insurance loss ratio: For insurance sector, the loss ratio was 31.4%.

Insurance companies' net income for 2016 was MNT11.4 billion, an increase of MNT4.3 billion from the previous year.

Figure 11. Fiscal year net profit /MNT billion/

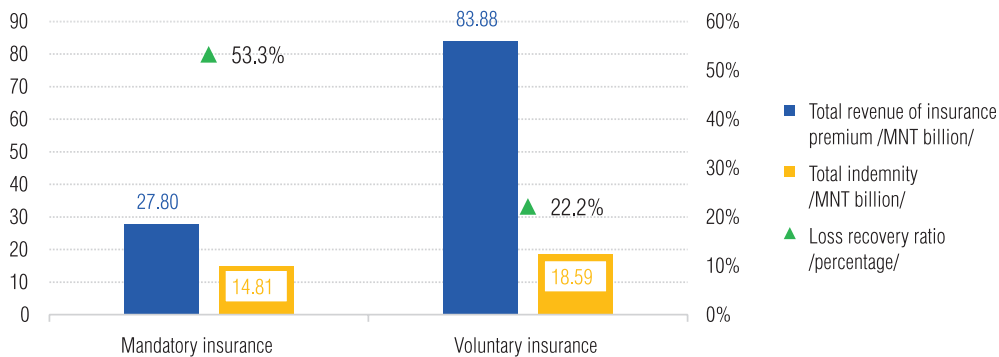


Source: The Financial Regulatory Commission

Mandatory insurance: 15 insurance companies offered driver's mandatory insurance for 463,802

customers and earned MNT27.8 billion premium income, an increase of MNT4.9 billion from a year earlier.

Figure 12. Insurance total premium revenue and indemnity



Source: The Financial Regulatory Commission

The Driver's Insurance Fund accrued MNT3,787.1 million and issued MNT150 million in insurance indemnity pursuant to the Law on Driver's Insurance.

Insurance companies paid MNT37.2 billion, which represented 32.5% of total premium to foreign reinsurance companies, for premium. Thereby, reinsurance premium dropped by 9.9% from a year earlier.

Insurance company's net income increased by 60.5% from the previous year.

Key ratios of the sector were 35.4% for profitability, 49.5% for expense, 42.2% for loss and an expense/loss ratio of 91.7%.

Despite a constant increase in sector performance, the main development indicators of insurance penetration rate and insurance density did not show any increase and main indicator was significantly lower compared with international averages.

Insurance regulators proposed an efficient and inclusive insurance approach to mortgagor insurance and presented to the Financial Stability Council for further decision.

To establish a comprehensive database and augment the information quality of the Fin-A system, insurance company's financial statement starting from 2006 were re-submitted to ensure research and analysis environment of the industry.

### 1.2.3 NONBANK FINANCIAL INSTITUTIONS

To ensure financial stability and supporting activities of the sector and integrated policy, the "Regulation and Guideline on Activities of Nonbank Financial Institutions" and "Regulation on Calculating Prudential Ratio Criteria and Supervision" were revised, and approved by Resolution No.71 and Resolution No.147 respectively to improve the legal and regulatory environment of nonbank financial institutions. Moreover, the minimum share of equity of nonbank financial institutions was re-established in accordance with FRC's Resolution No.271 and the share of equity held by nonbank financial institutions owning special license was set to be increased incrementally.

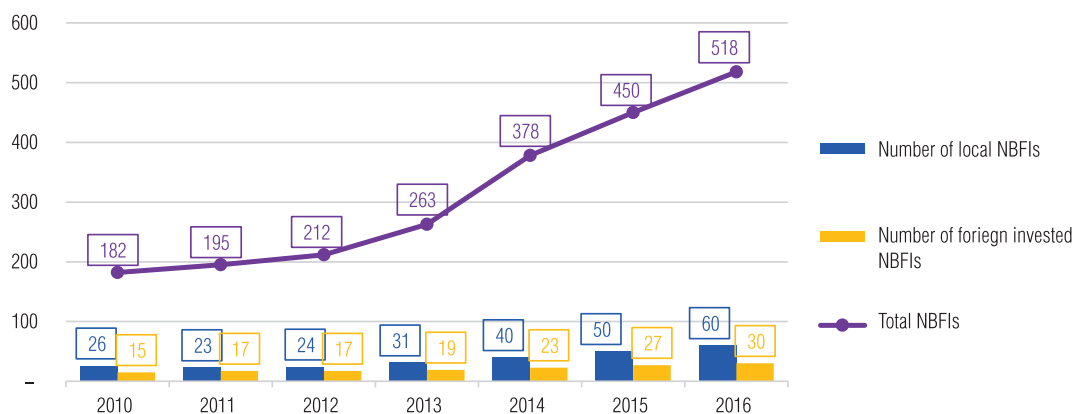
As of year-end 2016, there are 518 NBFIs under FRC's special licensure, which represents an increase of 15.1% in comparison with previous year's performance.

The scope of activities and duties of NBFIs under licensure ranges from granting loans, trustee and factoring services; online clearing and settlement transactions; trading foreign currency; providing investment and financial consulting services to owners of microfinance business, small and medium enterprises and private businesses; to investing in short-term financial instruments and issuing clearing and settlement instruments.

As of this fiscal year-end, there are a total of 463 NBFIs carrying out loans activities, 144 trading foreign currency, 33 providing financial and investment consulting services, 28 providing factoring services,

16 providing payment guarantee services, 12 providing clearing and settlement transactions, and two investing in short-term financial instruments and issuing clearing and settlement instruments.

Figure 13. Changes in NBFIs numbers



Source: The Financial Regulatory Commission

Table 6. Main indicators

№	Main indicators	2015	2016	Changes
		amount	amount	percentage
1	Total NBFIs	450	518	15.1
	Local NBFIs	50	60	20.0
2	Number of Customers	636,341	592,461	(6.9)
3	Number of shareholders	922	1,042	13.0
4	Number of employees	1,995	2,115	6.0
5	Number of branches	116	124	6.9
	Branches in Ulaanbaatar	86	92	7.0
	Branches in local	30	32	6.7
6	Representative offices	4	4	-
7	Total asset	623,172,524.1	787,172,010.1	26.3
	Compared with banking sector	3.0%	3.1%	0.1
8	Debt balance of total credit	391,235,479.1	478,175,223.3	22.2
	Compared with banking sector	3.4%	3.9%	0.5
9	Total capital	424,210,836.2	578,491,202.8	36.4
	Compared with banking sector	16.8%	18.6%	1.8
10	Total equity	308,451,260.0	440,547,491.2	42.8
	Compared with banking sector	65.6%	68.8%	3.2

Source: The Financial Regulatory Commission

As of year-end, 144 NBFIs were granted special licenses to trade foreign currencies, of which 35.4%, or 51 companies, are the principal providers. NBFIs trading foreign currencies bought MNT990.3 billion worth of foreign currencies while selling MNT1,017.3 billion worth of foreign currencies within the fiscal year.

**Total assets:** The total assets of nonbank financial sector reached MNT787.2 billion, an increase of 26.3% or by MNT163.9 billion, compared to

the same reporting period of last year. There was MNT154.3 billion or 36.4%, increase in private asset of NBFIs, of which shared capital increased by MNT132.1, billion or 42.8%, mainly accounts for the increase in total nonbank financial sector assets.

98.5% of total assets are comprised of current assets, of which 55.4% consist of loans and 30.9% of cash assets.

*Table 7. Asset structure*

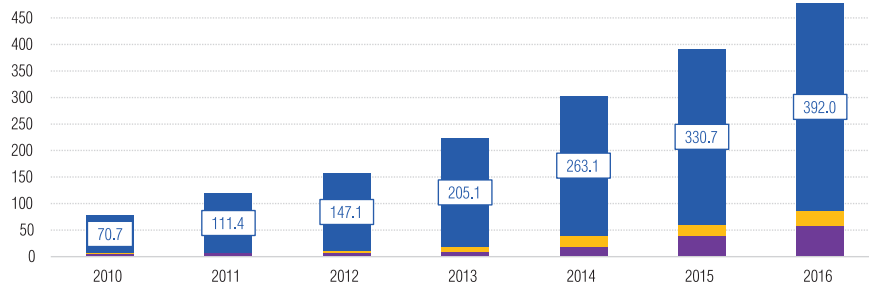
№	Asset	2015		2016		Changes
		Amount	Percentage	Amount	Percentage	Percentage
A	Current Asset	600,422,405.40	96.3	754,283,187.50	95.8	25.6
1	Cash or equivalents	174,217,117.50	28	243,107,520.30	30.9	39.5
2	Total credit	391,235,479.10	62.8	478,175,223.30	60.7	22.2
	(Credit risk fund)	26,556,625.70	4.3	42,065,155.70	5.3	58.4
3	Other current asset	46,944,361.50	7.5	69,275,036.90	8.8	47.6
B	Noncurrent asset	22,750,118.70	3.7	32,888,822.60	4.2	44.6
1	Fixed and Intangible asset	28,541,236.30	4.6	40,100,706.80	5.1	40.5
TOTAL ASSET		623,172,524.10	100	787,172,010.10	100	26.3

Source: The Financial Regulatory Commission

Compared to last quarter, NBFIs' total debt balance rose by 6.8% or MNT30.8 billion, reaching MNT478.2 billion while servicing 66,449 borrowers. Out of total loans, loans issued in foreign currency rose by MNT4.2 billion or 10.8% while loans issued in local currency increased by MNT82.7 billion or 23.5% compared to the previous year's performance.

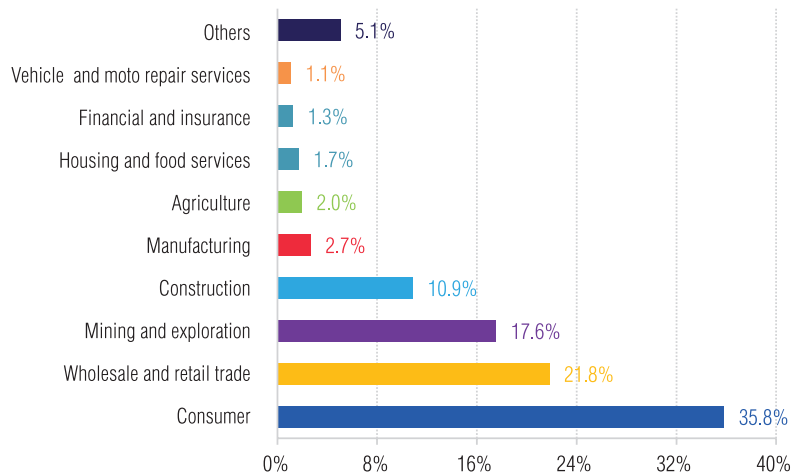
Out of total debt balance, regular loans, overdue loans, and non-performing loans make up 82%, 5.6%, and 12.4% respectively and reached MNT59.5 billion. Although the amount of non-performing loans rose by 55.1%, it fell by 5.8% compared to the last quarter.

Figure 14. Loan portfolio rate /MNT billion/



Source: The Financial Regulatory Commission

Figure 15. Loans by industry

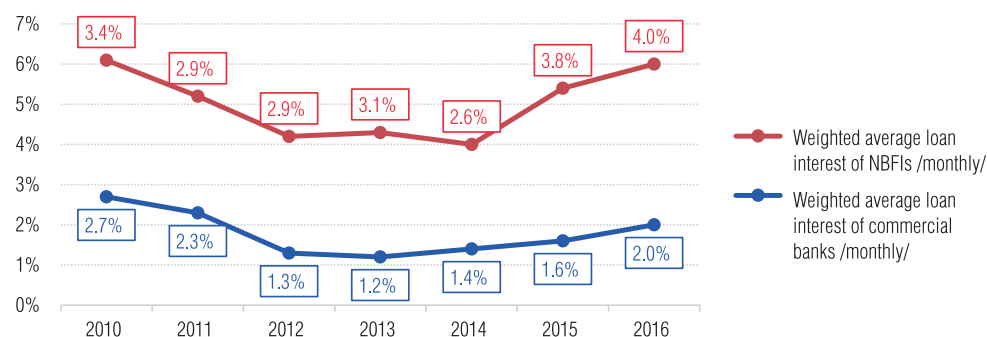


Source: The Financial Regulatory Commission

The weighted average interest rate of 454 NBFIs with credit services licenses reached 4%, a decline of

0.2%. It was 2% higher than the commercial banks' credit interest rate.

Figure 16. Weighted average loan interest



Source: The Financial Regulatory Commission

Asset indicators: Throughout 2016, a total of 16 NBFIs has invested MNT1.3 billion to short term investment instruments. 89.6% out of total invested capital was done by single NBFI.

NBFIs factoring settlement debt balance reached MNT37.8 million and the reserve fund for non-performing loans amounted to MNT30 million.

NBFIs' fixed assets reached MNT40.1 billion and accounted for MNT7.2 billion in depreciation.

Total assets of NBFIs increased by 26.3% from a

year earlier. 26.5% or MNT208.7 billion of aggregate assets were allocated capital and 73.5% or MNT578.5 billion assets were own equity. Equity was composed of share capital (56%), accumulated profit (16.6%), loan (15.4%), trust service debt (3.9%) and other capital. NBFIs own equity increased by 36.4% or MNT154.3 billion over the previous year. Equity increase was due primarily to the increase of share capital (MNT132.1 billion) and accumulated profit (MNT28.4 billion).

Table 8. Liabilities and Owner's Equity

№	Asset	2015		2016		Changes
		amount	percentage	amount	percentage	percentage
A	Current asset	600,422,405.40	96.3	754,283,187.50	95.8	25.6
1	Cash or equivalent	174,217,117.50	28	243,107,520.30	30.9	39.5
2	Total loan	364,678,853.40	58.50	436,110,067.60	55.40	20.0
3	Other asset	46,944,361.50	7.5	69,275,036.90	8.8	47.6
B	Noncurrent asset	22,750,118.70	3.7	32,888,822.60	4.2	44.6
1	Fixed and intangible asset	28,541,236.30	4.6	40,100,706.80	5.1	40.5
<b>TOTAL ASSET</b>		<b>623,172,524.10</b>	<b>100</b>	<b>787,172,010.10</b>	<b>100</b>	<b>26.3</b>

Source: The Financial Regulatory Commission

NOTE: Throughout 2016, MNT7 billion income tax was allocated to the state budget as a result of MNT63.9 billion net income of total 416 NBFIs.

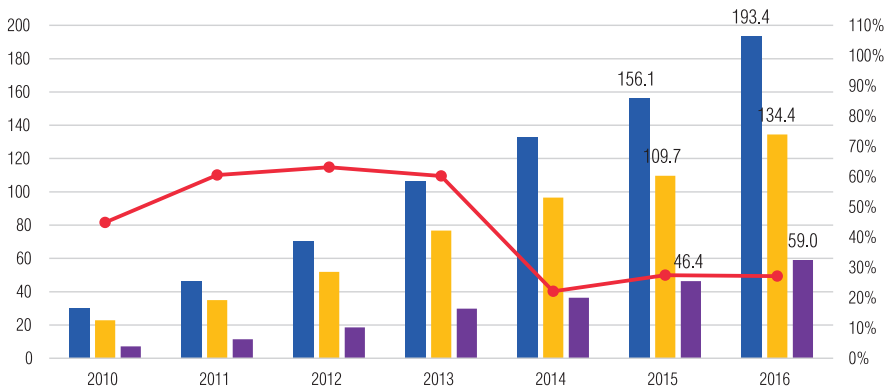
NBFIs profit reached MNT193.4 billion, an increase of 23.9% from a year earlier. Net profit was made up by interest income (70.1%), non-interest income (28.1%) and non-operating income (1.8%).

Expenses of NBFIs reached MNT134.4 billion, an increase of 22.5% over the previous year. The

expense increase was due to the increase of interest expense (2.9%), non-interest expense (24.8%) and income tax expense (14.4%).

Net profit of NBFIs totaled MNT59 billion, an increase of MNT12.7 billion or 27.3% from a year earlier.

Figure 17. Profitability indicator /MNT billion/



Source: The Financial Regulatory Commission

82.4% of registered NBFIs fully complied with the prudential ratios. Remaining NBFIs have not complied one /11.6% or 60 NBFIs/, two /3.7% or 19 NBFIs/, three /1.2% or 6 NBFIs/ and four or more /1.2% or 6 NBFIs/ prudential ratios as specified in applicable legislations, respectively.

Total assets of NBFIs reached MNT787.2 billion and represented 3.1% of the total assets of the banking sector. Debt liability balance numbered MNT478.2 billion which accounted for 3.9% of banking sector. Own equity of NBFIs was reached to MNT578.5 billion which represented 18.6% of total in banking sector. Share capital of NBFIs represented 68.8% of total share capital in banking sector and totaled MNT440.5 billion.

Share capital of NBFIs reached to MNT787.2 billion at the end of 2016 and was projected to increase in 2017 MNT992.5 billion, or 26%. Increase was due

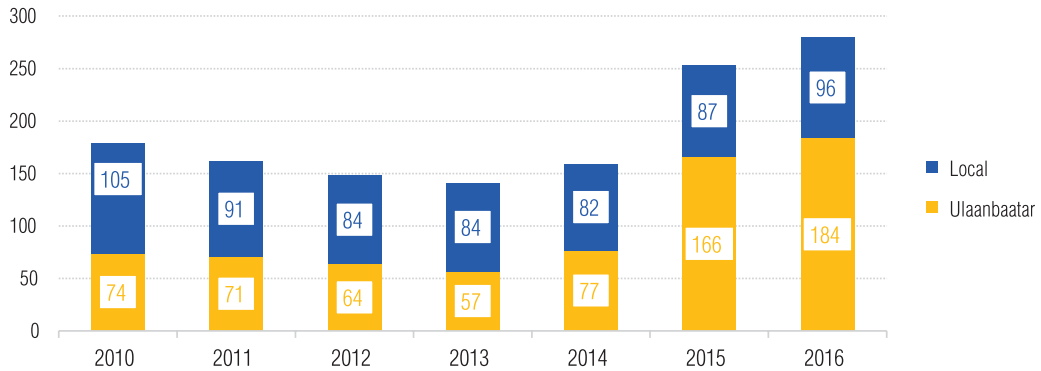
primarily to new capital requirement from the FRC and the decision is expected to enhance financial inclusion and favourably impact on financial market righteously.

### 1.2.4 SAVINGS AND CREDIT COOPERATIVES

As member-owned, non-profit, mutual financial institutions, SCCs strive to increase its members' financial and social well being, support employment and promote financial inclusion. It differs from other financial institutions by being not only capital but also an individual incorporation.

There were 280 SCCs at the end of 2016, 34 special licenses were issued, and seven special licenses were revoked.

Figure 18. Changes in SCCs numbers

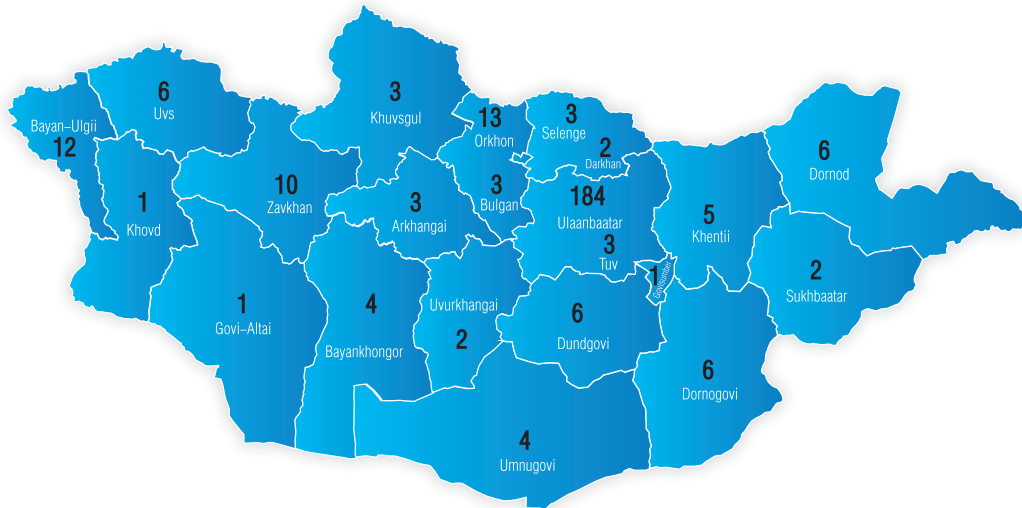


Source: The Financial Regulatory Commission

65.7% (184) of total SCCs operated in Ulaanbaatar and 34.3% (96) of SCCs were located in the provinces. Following centralization of financial services and population density, Chingeltei and Sukhbaatar are the most compacted city districts as well as Orkhon,

Bayan-Ulgii and Zavkhan provinces. However, there were only one SCC has been operating in Khovd, Govi-Altai and Govisumber provinces, respectively.

Figure 19. Number of SCCs /location/

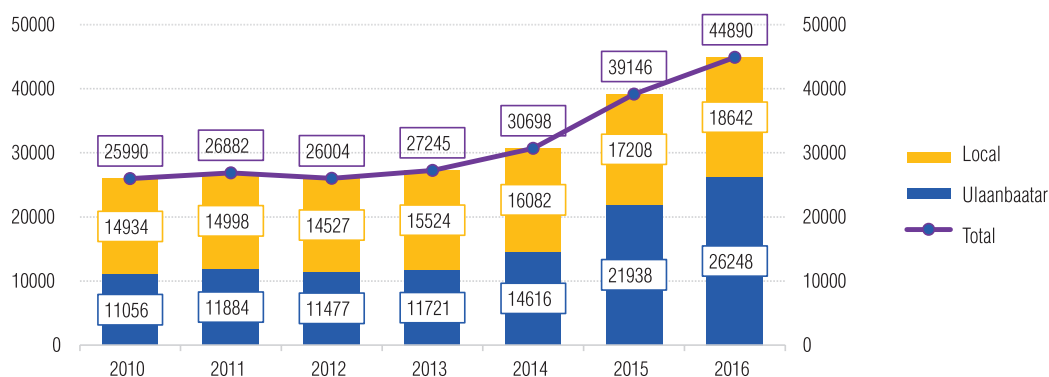


Source: The Financial Regulatory Commission

During the 5th National Forum on Cooperatives, policy issues including implementation of “Sustainable Development” and “Green Development and Green Economy”, objectives the opportunity for improving SCCs participation on “Meat and

Milk Campaign” and “Mechanism of Raw Products Supply”, development of SCCs good governance and the establishment of mutual business new model were considered.

Figure 20. Changes in SCCs' members



Source: The Financial Regulatory Commission

Following changes were made to the SCCs' main statistic indicators compared to the year earlier.

Table 9. Main indicators

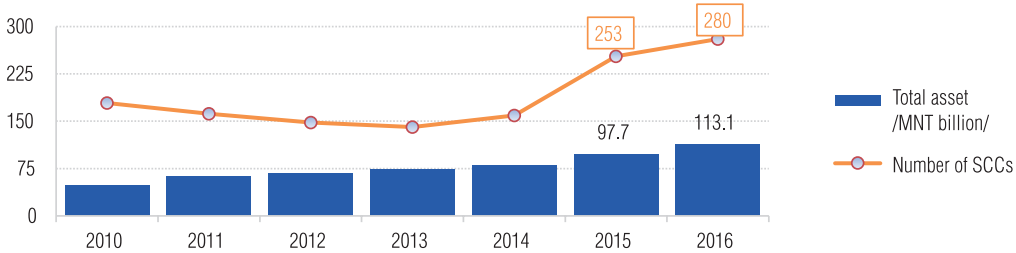
No.	Main indicator	2015	2016	Changes	
				Amount	Percentage
1	Number of SCCs	253	280	27	10.7
2	Number of members	39,146	46,183	7,037	18.0
3	Total asset	97,698,233.8	113,131,578.4	15,433,344.6	15.8
	Comparison per banking sector	0.5%	0.5%	-	-
4	Total balance of loans	75,339,140.6	84,442,032.9	9,102,892.3	12.1
	Comparison per banking sector	0.6%	0.7%	0.1%	16.6
5	Total balance of non-performing loan	3,466,986.9	4,620,960.2	1,153,973.3	33.3
	Comparison per banking sector	0.4%	0.4%	-	-
6	Total balance of deposits	59,262,286.8	68,149,279.5	8,886,992.7	15.0
	Comparison per banking sector	0.8%	0.8%	-	-
7	Total balance of equity	10,637,537.3	12,167,436.5	1,529,899.2	14.4
8	Total balance of members equity	10,569,495.5	12,119,877.0	1,550,381.5	14.7
9	Balance of banks, NBFIs, and projects loans	12,555,227.0	15,481,372.7	2,926,145.7	23.3
10	Total revenue	21,752,831.5	24,709,072.4	2,956,240.9	13.6
11	Total expense	18,507,722.2	20,878,463.8	2,370,741.6	12.8
12	Current profit and loss	3,245,109.3	3,830,608.6	585,499.3	18.0

Source: The Financial Regulatory Commission

Compared to the previous year, numbers of SCCs and members of SCCs have increased by 10.7% and 18.0%. Total asset of the SCCs increased by 15.8% and 74.9% of total asset was comprised of loan portfolio. Increase of total volume of asset and credit was due primarily to implementation of “City program for supporting SMEs and reducing poverty”.

Aggregate amount of credit extended by lending institutions including banks, NBFIs and project funds to SCCs have reached to MNT15.5 billion. Efforts for extending credits and small projects to SMEs through SCCs in particular in rural areas have been made.

Figure 21. Asset growth of SCCs

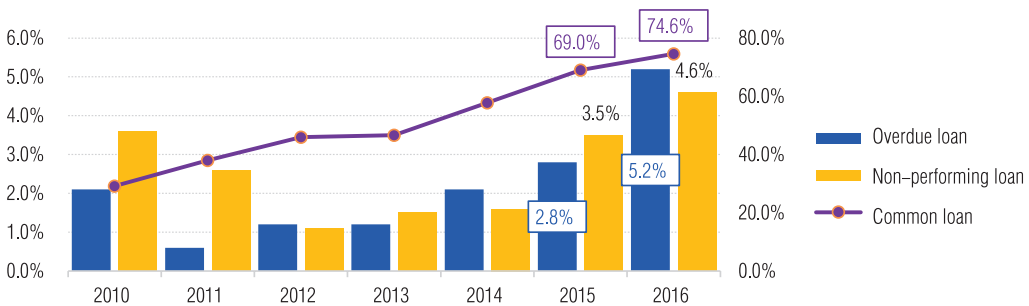


Source: The Financial Regulatory Commission

Total amount of loan portfolio of SCCs reached to MNT84.4 billion in which represented 74.9% of total asset and net loan of SCCs accounted for MNT81.4 billion, 72.3% of total asset as of the end of 2016.

Non-performing loan percentage among total loan has increased by 5.5% than the year earlier, which resulted to the non-conformance with the prudential ratio.

Figure 22. Comparison of Loan portfolio changes

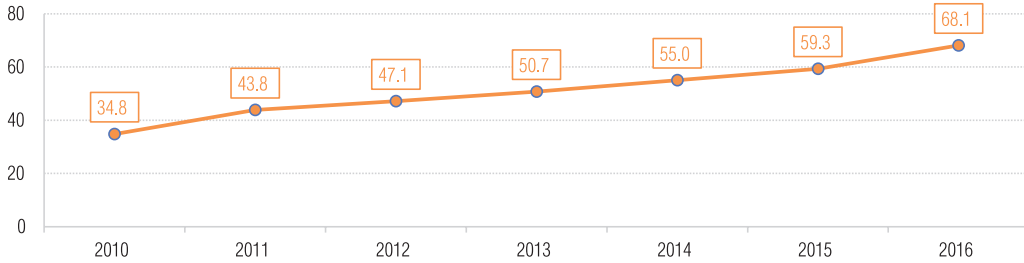


Source: The Financial Regulatory Commission

Deposit totaled MNT68.1 billion in 2016 and represented 60% of total asset. 95% of total deposit

(MNT64.9 billion) was term deposit and 5% of total (MNT3.2 billion) was on-call deposit.

Figure 23. Savings growth of SCCs



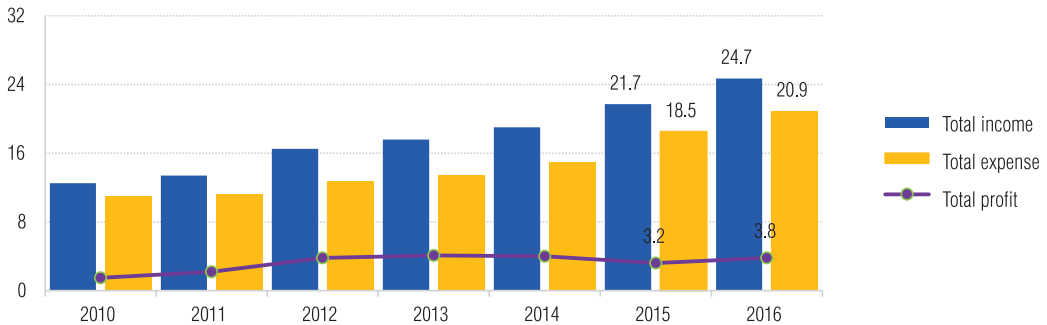
Source: The Financial Regulatory Commission

Total amount of members' equity has reached to MNT12.2 billion and amounted to 10.5% of its seed capital.

Gross income has reached to MNT24.7 billion, an increase of MNT2.9 billion or 13.6% than the

previous year while expenses has amounted to MNT20.9 billion, an increase of MNT2.4 billion or 12.8%. Net profit of the sector has reached to MNT3.8 billion, an increase of 18% from the year earlier.

Figure 24. Profitability



Source: The Financial Regulatory Commission

Savings and credit cooperatives extend financial services including loan, deposit, financial leasing, project funding, e-settlement, insurance agent, money transfer and accumulated fund management.

Compared to the previous year, numbers of SCCs and members of SCCs have increased by 10.7% and

18.0% while it has been shown an increase of 15.8% to the total asset. As a result, total asset and loan volume in banking sector have increased by 0.1%. In addition, starting from the second quarter of 2016, total amount of asset of SCCs have reached MNT100 billion for the first time.

# 2

## IMPLEMENTATION AND ENFORCEMENT OF LEGISLATION

In the framework of enforcing the Law on Legal Status of the Financial Regulatory Commission and other applicable legislations, departments responsible for

policy coordination and supervision have developed necessary regulations and guidelines for approval by the FRC.

## 2.1. POLICY AND REGULATION

Policy departments of the FRC took responsibility to carry out duties to ensure sustainable growth in the regulatory environment under new organizational structure approved by Resolution No.261 in 2016.

### 2.1.1 SECURITIES MARKET

The FRC developed six regulations and amended five regulations related to investment fund and securities market professional participants to supporting market development, enhancing investment and establishing optimized regulatory environment.

Plans were also set to increase minimum capital requirements in line with current economic circumstances and the capacity of intermediaries with the goal of improving operation quality of financial intermediaries and strengthening professional intermediaries' software systems, human resources and financial capabilities in the capital market.

Thereby, establishment of DVP settlement procedure, transitioning to T+2 and T+3 settlement cycles and formation of primary dealers of intermediaries are important advancements towards increasing securities trading and market liquidity.

Within the objective of establishing a consolidated exchange capital market, the FRC held discussions among associated state organizations, Mongolian Stock Exchange JSC, Mongolian Securities Exchange LLC, Agricultural Commodity Exchange LLC, professional participants and market infrastructure institutions. They agreed to start a central securities settlement system. In addition, the parties initiated a mechanism preventing the risks associated with the currency fluctuation and tax exemption and deduction for investors and professional participants.

In accordance with the "General Directives for Optimizing Mongolian Legislations until 2020", the FRC proposed to develop, amend and revise

applicable legislations—i.e, the Law on Securities Market, the Law on Agricultural Products and Raw Materials Exchange, the Law on Company, the Law on Crowd-funding, the Law on Investor Protection Fund and the Law on the Mineral Exchange in order to optimize the regulatory capital market environment, stimulate domestic and foreign investor participation, improve the environment of mutual and private investment fund to enhance economic circumstances. In this regard, the FRC established a working group composed of public organizations and professional participants to draft legislation and a concept paper including, justification, introduction and preliminary research comparing international legislations in the securities market.

The Action Plan on Economic Revitalization Program was approved by Resolution No.71 of the State Great Khural in 2016 in which policies for the development of the capital market were specified.

The FRC presented its operational report, applied policy measures current situation and future prospects for the capital market to the Economic Standing Committee of the State Great Khural on 22 November 2016. To improve the legal and infrastructure environment, enhance economic benefit and raise competitiveness of the capital market, the FRC developed the "Action Plan on Capital Market Enhancement – 2022" on the basis of "Capital Market Strategy" developed by the Multi-Sectoral Technical Assistance Project, the World bank.

### 2.1.2 INSURANCE MARKET

The FRC has been actively participating on the working group drafting the Law on Private Pension Insurance and the Law on Crop Insurance in association with its public and private partners.

The FRC approved a “Regulation on Solvency Assessment of Nonlife Insurance Companies” by Resolution No.105, in 2016. As a result, data related with the solvency assessment of nonlife insurance companies is now received electronically through/ via Fin-A, the FRC’s internal reporting system.

Quality examination trainings organized through Mongolia’s Insurers’ Association, Mongolia’s Insurance Intermediaries’ Association and Mongolia’s Loss Adjusters’ Association were conducted.

Revisions were made to the following regulations to ensure a clear legal and regulatory framework for the insurance market.

- Revision of “Regulation on Issuance of Actuarial License, Actuarial Standard and Actuarial Risk Assessment and Supervision and Reporting of Actuary” by Resolution No.50 in 2016;
- Revision of “Regulation on Requirements and Guidelines for Insurers” by Resolution No.48 in 2016;
- In accordance with Resolution No.49 approved by the FRC, financial statement forms have been changed pursuant to the “Accounting Instruction” and “Financial statement form and disclosure” approved by the joint order of the Chairman of the FRC and Minister of Finance in 2015;
- Revision of “Regulation on Setting, Spending and Supervision of Nonlife Insurance Reserve Fund”;

Considering current economic and business circumstances and insurance company financial solvency capabilities the time-frame for achievable minimum capital requirement of insurance companies, as stated in “Renewal of Minimum Capital Requirement of Insurance Companies” approved by Resolution No.355 in 2012, was extended to 30 June 2018.

Changes were made to the regulation approved by Resolution No.407 of the FRC. Insurance companies and insurance professional participants are required to inform and register changes in equity ownership below 10%.

Reinsurance was classified as part of voluntary insurance types under amendment to Resolution No.235 approved on 15 June 2016. In accordance with “Modification on regulations and instructions of insurance companies and insurance professional participants” approved by Resolution No.202, 10 June 2016, several articles were amended.

Insurance regulators designed a proposal on efficient and inclusive insurance for mortgagors and presented it to the Financial Stability Council for decision.

### 2.1.3 NONBANK FINANCIAL INSTITUTIONS

Resolution No.71 was revised “Regulatory Regulation and Instruction on Nonbank Financial Institutions” in 2016 to facilitate the licensing process, establish an auspicious environment for business, enhance the operational framework of nonbank financial institutions and consolidate regulatory checklists. Following the approval of the regulation, nonbank financial institutions were classified into three categories based on their type of operation and licensing requirements and regulatory principles.

For improvement of risk tolerance and establishment of suitable structure of equity and seed capital of nonbank financial institutions, the FRC approved “Regulation on Supervision and Assessment of Nonbank Financial Institutions’ Prudential Ratio” by Resolution No.147 and amended by Resolution No.269 in 2016, respectively. As specified in the regulation, nonbank financial institutions are required to report in detail its prudential ratio in relation to its operational type.

Minimum capital requirement has been renewed by Resolution No.72 of 2016 in pursuant to improving financial inclusion, reducing services cost, increasing responsibilities, enhancing risk tolerance and competitiveness and maintaining sustainability. By the end of the year, 96% of nonbank financial institutions have complied with the requirement.

Resolution No.271 of 2016 by which nonbank financial institutions were imposed to gradually increase capital requirement also made changes to the minimum capital requirement.

#### 2.1.4 SAVINGS AND CREDIT COOPERATIVES

The FRC conducted an integrated research to identify market trends, project outcomes funded by the Asian Development Bank and City Council and the efficiency of policy measures put forth by the FRC and the MOCCU.

The research was carried out among 83 SCCs financed by the ADB fund and 104 SCCs financed through the City Council. It concluded that market

equity and public confidence in SCCs increased as a result of the ongoing projects.

In addition, SCC regulators are currently working to establish a Depository Insurance Fund and Stability Fund as specified in the Law on Savings and Credit Cooperatives together with technical assistance from the ADB.

The stability fund is comprised of financial institutions to protect financial institutions, prevent systemic risk and ensure solvency of financial institutions.

The Deposit Insurance Fund in SCC sector is regulated by individual legislation as an international practice and the Stability fund is responsible for deposit insurance and stability in some countries simultaneously.

## 2.2. REGISTRATION AND LICENSING

In accordance with the Law on Legal Status of the Financial Regulatory Commission, the following decisions were made in relation to issuance, suspension, retrieval and revocation of licenses.

For the securities sector, four asset-backed securities companies, five asset management companies, one asset trust management company, eight audit services companies and four legal firms were either newly formed or newly licensed.

*Table 10. License and authorization /Securities market/*

No	Description of license and authorization	Numbers
1	Appointment of authority	9
2	Change of company name	3
3	License issuance of branch	1
4	Modification of equity capital and equity ownership	16

*Source: The Financial Regulatory Commission*

Seven audit companies, five insurance loss adjuster companies, three insurance intermediary companies

and twenty-eight insurance intermediary branches has been newly licensed.

*Table 11. License and authorization /Insurance market/*

No	Description of license and authorization	Numbers
1	Appointment of authority	25
2	License revocation of branch	5
3	License issuance of branch	31
4	License issuance of insurance agent	149
5	License revocation of insurance agent	405
6	License issuance of insurance broker	28
7	Modification of equity capital	6
8	Modification to equity ownership	9

Source: The Financial Regulatory Commission

In addition, 72 companies newly formed, 4 companies dissolved and one company retrieved its license in nonbank financial institutions.

*Table 12. License and authorization /NBFIs/*

No	Description of license and authorization	Numbers
1	Change of company name	6
2	License issuance of branch	9
3	License issuance on financing service	1
4	License issuance on trust service	2
5	Modification of equity capital and equity ownership	170

Source: The Financial Regulatory Commission

For savings and credit cooperatives, 34 SCCs were newly formed, 2 SCCs' licensed were suspended, 7 SCCs' licenses were revoked and 48 SCCs' licenses were extended.

*Table 13. Registration and authorization /SCCs/*

No	Description of license and authorization	Numbers
1	License on project implementation service	9
2	License issuance on financial leasing service	1
3	License issuance on insurance agent service	1
4	License issuance of branch	1

Source: The Financial Regulatory Commission

The FRC issued a total of 2017 licenses for entities and 3741 for individuals in accordance with applicable nonbank financial sector legislation.

## 2.3. SUPERVISION

The FRC conducted oversight of its reporting entities, – i.e., 302 joint stock companies, 62 securities companies, 17 insurance companies, 40 insurance intermediaries, 31 insurance loss adjusters' companies, 518 nonbank financial institutions and 280 savings and credit cooperatives throughout the year and took corrective measures for disclosed misconducts and violations in accordance with applicable legislations.

Increasing numbers of reporting entities, falling of financial circumstances and insufficiency of adequate human resources have been curtailing frequency of onsite supervision in rural areas, in particular. Thus, the FRC has been working to set up risk based supervision approach. Supervision has been conducted through onsite inspection and offsite supervision approach.

Offsite supervision: Reporting entities are required to submit financial statements by monthly, quarterly and yearly basis. Following submission, supervision regulators oversee the solvency ratio; the prudential ratio and other requirements verified financial statements. Data interval of the Fin-A system has been augmented by the financial statements of reporting entities from 4<sup>th</sup> quarter of 2015 and 1<sup>st</sup> to 3<sup>rd</sup> quarter of 2016.

Reporting entities subjected to the FRC's offsite supervision showed common deficiencies of late reporting, non-compliance with the prudential ratio and audit disengagement. Enforcement actions including monetary penalties, suspension and revocation of licenses, further onsite inspection and recommendations for corrections were taken against companies.

Onsite inspection: Throughout 2016, the FRC conducted onsite inspection for 238 reporting entities.

Securities supervision: Securities regulators conducted onsite inspection of 60 securities companies in collaboration with Mongolia's Association of Securities Dealers. A shortage of experienced human resources, inadequate software systems and nonconformity with the minimum capital requirements were the main violations by the examined entities.

Based on received complaints and offsite supervision findings, several companies were subject to onsite inspection to protect the rights of small investors. In addition, regulators' notifications in need of corrections including organizing of board of directors meeting and measures for solving property dispute have been ordered and necessary tasks and sanctions imposed under its supervisory mandate.

Insurance supervision: Following complaints from insured/policy holders, findings of offsite supervision and the FRC's onsite inspection plan, six insurance companies and Mongolia's Association of Mandatory Insurers were inspected. Sale of unregistered insurance product, unreported address change, noncompliance with accounting rules and regulations were the common deficiencies among the companies and necessary assignments and sanctions were imposed in need for corrections.

Nonbank financial institutions supervision: 123 NBFIs were inspected in 2016. Unclaimed cash in vault and asset misplacement of NBFIs have been identified as the main violations. As a follow-up, regulators took actions to correct the errors and wrongdoings in line with the applicable legislations. In addition, NBFIs regulators have conducted supervision for seven NBFIs in collaboration with the National Policy Agency.

Savings and credit cooperatives supervision: 141 SCCs implementing "City program for supporting SMEs and reducing poverty" have been inspected partially under the guideline of proper expenditure of the funding provided by the "City fund for SMEs financing" and compliance of applicable legislations. Inspection findings, assessments and further actions' proposal have been submitted to the City Council for reference. For SCCs that were found to have performed negligent operation, sanctions ranging from mandatory recommendations from regulators and corrections following the examination report were taken.

Enforcement of the Law on Conducting Settlement in National Currency: The FRC inspected a total of 11 entities' including schools, hotels and jewel stores, pursuant to the joint order of the Governor of Mongolbank and the Chairman of the FRC. Enforcement actions were imposed for company violations of the law.

# 3

## SUSTAINABLE DEVELOPMENT OF FINANCIAL MARKET

### 3.1. ENHANCING FINANCIAL INCLUSION

For establishing environment to deliver financial services at affordable cost, reducing unit costs of financial services, developing policies to promote usage of innovative technologies, establishing regulatory scheme for sustainable and inclusive financial sector and delivering financial services for disadvantaged and low-income of society, robust and practical financial inclusion policy became one of the key priorities of countries.

#### 3.1.1 ENHANCING FINANCIAL LITERACY

The following activities were conducted to enhance financial literacy of public in collaboration with associated organizations.

“Seminar on IPO and Dual-listing” for professional participants, stock issuers and public in collaboration with “Project for Capacity Building of Capital Market”, Japan International Cooperation Agency was conducted.

“Conference on Consolidated Goal and Solution” held in collaboration with “Project for Capacity Building of Capital Market”, Japan International Cooperation Agency and Mongolia’s Association of Securities Dealers with the purpose of enhancing financial literacy and promoting capital markets.

In respect to improving the public’s basic knowledge of capital markets, training materials on shares, corporate bond, debt instruments and derivatives were developed for websites publications.

Efforts were made to improve the financial literacy of citizens living in rural areas through a project on improving basic knowledge of finance and investment and establishing national investment platform with the support of AFI /Alliances for Financial Inclusion/.

- Three days of knowledge sharing training for insurance professional participants supported by the World Bank;
- Training on Actuary for insurance professional participants supported by MON/004 project;

- “Training on Insurance Regime, Mandatory Insurance and Loss Adjustment” organized in collaboration with the Ministry of Finance, Mongolia’s Association of Mandatory Insurers, Mongolia’s Association of Insurers and Mongolia’s Association of Loss Adjusters and Korea’s Association of Loss Adjusters;
- “Training on Risk Based Supervision” conducted with the support of the World Bank;
- “Training on Actuary” in collaboration with the Mongolian Society of Actuaries and Mongolia’s Insurers Association;
- Insurance knowledge-sharing day;
- Roundtable discussion on insurance indemnity, insurance products and proposed legislation for the insurance sector with private partners;
- Roundtable discussion on Enforcement of the Law on Driver’s Compulsory Liability Insurance with Traffic Police and insurance professional associations;
- Roundtable discussion on market prospect with the World Bank consultants, executives of insurance companies and management team of the FRC;

“National Forum on Development of Financial Market – 2016”, “Working Group Meeting on Small and Medium Enterprises Financing” of Alliances for Financial Inclusion and “National forum on Development for Savings and Credit Cooperatives” were successfully held. In addition, training for provincial representatives was conducted.

### 3.1.2 PROTECTION FOR RIGHTS OF CONSUMERS AND INVESTORS

The number of complaints the FRC processed in 2016 numbered 442, a 14% increase from the previous year.

Figure 25. Complaints from investors and consumers /sector/



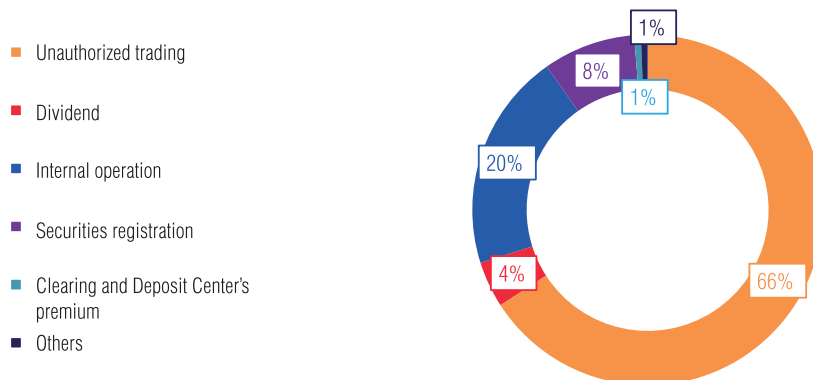
Source: The Financial Regulatory Commission

Insurance-related cases numbered 46% of total complaints. Compared to the previous year, savings and credit cooperatives-related cases (41%), nonbank financial institutions-related cases (82%), insurance-related cases (9%) and securities-related cases (5.3%) increased.

Complaints related to the securities market: Due to growing interest and enhanced financial literacy

of public in capital market, numbers of complaints related to securities companies increased to 168 in particular complaints against unauthorized trading which was commonly done from 1996 to 2005 without prior notice to blue and pink sheet holders represented 66% of total complaints, an increase by 2.5% than the previous year.

Figure 26. Securities market complaints

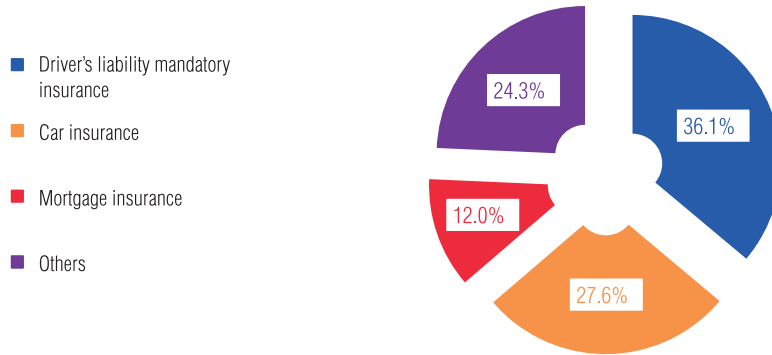


Source: The Financial Regulatory Commission

Complaints related to the insurance market: Consumers filed 202 complaints related to insurance sector. For insurance sector, complaints related to

driver's mandatory insurance totaled 36% (35% in 2015) and car insurance represented 28% (39% in 2015).

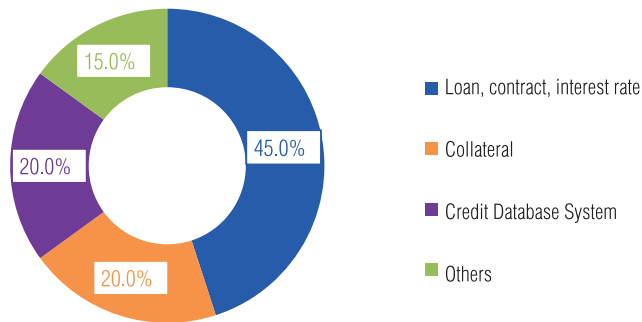
Figure 27. Insurance market complaints



Source: The Financial Regulatory Commission

Driver's mandatory insurance and car insurance represented 60% of total insurance policy, which influenced higher percentage of complaints in the sector.

Figure 28. NBFIs complaints

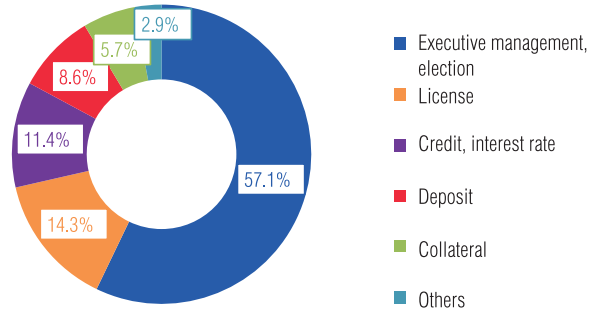


Source: The Financial Regulatory Commission

Complaints related to the nonbank financial institutions: Complaints related to NBFIs increased by 82.3% which the FRC received 31 complaints in 2016. 45% of complaints were attributed to loan

contracts and loan interest rate. This increase is due primarily to the dismissal of time-to-time update of credit history to the Credit Database System.

Figure 29. SCCs complaints



Source: The Financial Regulatory Commission

The FRC received 41 complaints related to SCCs, 41% point increase from the previous year. Complaints against executive management and internal election process represented 57% of total

complaints. In particular, numbers of complaints on collateral, interest deduction from the received credit and misunderstanding between management team has increased by 50% than in 2015.

### 3.2. LEGAL ENVIRONMENT

The FRC is responsible for enforcement of 18 legislations under its regulatory and supervisory mandate for nonbank financial sector. In addition, implementation of approximately 210 regulations, rules, instructions on operation, registration issuance of licenses and special licenses approved by the FRC. Changes needed to be made in light of approval of the General Administrative Law, which was put in effect on 1 July 2016.

The FRC took active part in optimizing legal environment of nonbank financial sector and submitted proposals to renew, revise and amend 17 legislations to the Government which later included to the “General Directives for Optimizing Mongolian Legislations until 2020”. Research have been conducting in the framework to developing new legislations including the Act on Real Name Financial Transactions, the Law on Crowd-funding, the Law on Hospital Professional Liability Insurance,

the Law on Lawyers Professional Liability Insurance and the Law on Investor Protection Fund. In addition, the FRC officials have been partaking “Optimizing legal environment of bank, finance and insurance sector, developing policy documents and formulating market development proposal of insurance and securities sector” working group established by the Prime Minister’s Order No.76 and working group for developing and submitting “National Program for Development of Financial Market – 2025” to the Government for approval established by the Financial Stability Council.

The FRC took active part in endeavors to develop state financial policy documents including “General Directives for Development of Mongolia’s Economic and Social Wellbeing – 2017”, “General Directive for State Monetary Policy – 2017”, “Economy Revitalization Program” and “Government Action Plan 2016 – 2020”.

# 4

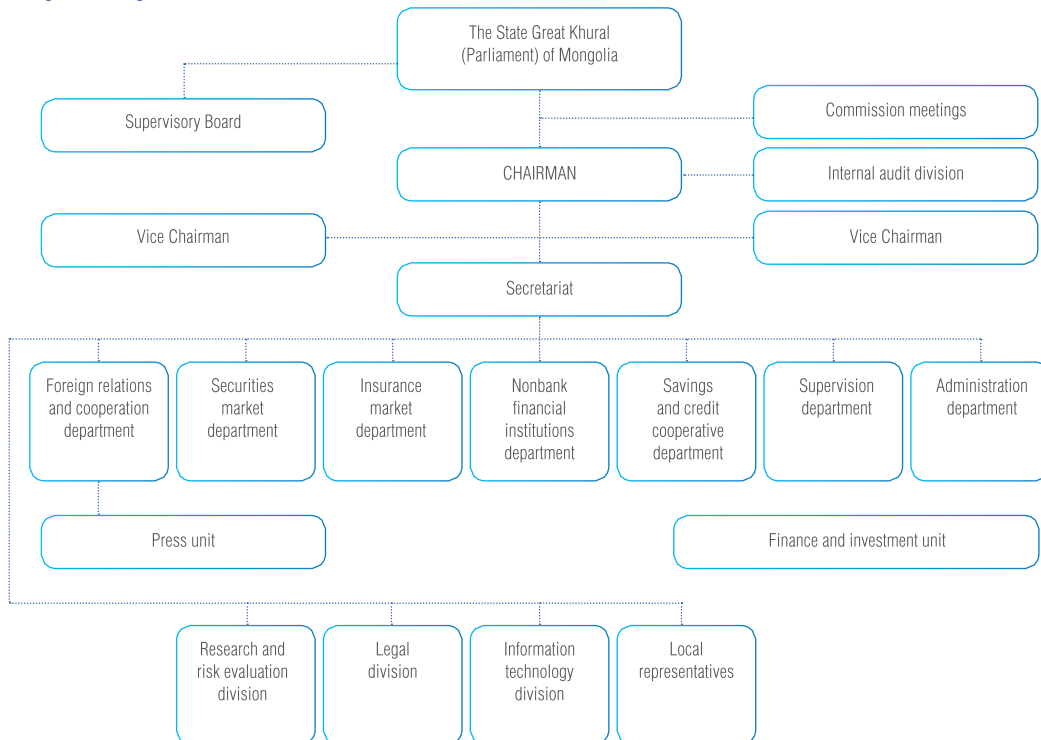
## OPERATION OF THE FRC

### 4.1. ORGANIZATIONAL STRUCTURE

The FRC has been re-structured its organizational structure to eliminate duplication of duties and reduce the operation cost. Prior to re-structuring its organizational structure, the secretariat of FRC was disciplined with a total of 30 executives of 7 departments, 16 divisions, and 3 units.

In August 2016, the FRC was re-structured its secretariat with a total of 16 executives of 7 departments, 4 division, and 2 units.

Figure 30. Organizational Structure



Source: The Financial Regulatory Commission

## 4.2. INTERNAL ACTIVITIES

**Performance:** The FRC has planned to execute 123 actions with 3 sections in 2016. In addition, The FRC ensured 15 resolution compliances and 73 action compliances of the President of Mongolia, the State Great Khural of Mongolia, the Standing Committees, and the Government of Mongolia and delivered progress report to the competent authorities. We practiced revised law (374) of Mongolia and resolutions (121) of the Parliament and began to use “verification card” for implementing resolutions that directly related to our daily basis activities.

The preliminary draft of “Current circumstances and future trends of the capital market” was introduced to the Standing committee on Economics and decrees of the State Great Khural of Mongolia from 2013 to 2016, sector law enforcement, and program implementation were reported to the secretariat of the State Great Khural of Mongolia.

“2014 – 2016 aimed at creating a market interest rate environment reduced in the approved within the medium-term program implementation” was submitted in the second quarter of 2016.

The FRC took active part in endeavors to develop state financial policy programs including “General Directives for Development of Mongolia’s Economic and Social Wellbeing – 2017”, “General Directive for State Monetary Policy – 2017”, “Economy Revitalization Program” and “Government Action Plan 2016 – 2020”.

The FRC participated in 27 working group in collaboration with the State Great Khural of Mongolia, government and other government authorities.

**Regular meetings:** 329 issues associated with nonbank financial sector were solved within 17 regular meetings of FRC in 2016. Within the

nonbank financial sector, six regulations were issued, 14 regulations were renewed, seven regulations were revised, five regulations were amended, 15 regulations were revoked, and one regulation was partially revoked. The approved regulations are intended to ensure compliance of microfinance, insurance, and securities markets with international standards, facilitate the introduction of new financial products and services, elevate requirements of market participants, protect the rights of investors, reduce market risks, and increase market participation incentives for local and foreign investors.

**Training:** In collaboration with professional associations, a number of training for insurance intermediaries, insurance brokers firms, loss adjusters, securities intermediaries, investments firms, and professional participants being granted rights to provide professional services were organized. The FRC also held 21 additional training programmes for its personnel to strengthen their professional skills.

In addition, 48 FRC personnel participated in 23 training programmes and events abroad. Two people were approved for a MBA scholarship program implemented by the Government of Japan, one person was granted for a MBA scholarship program implemented by the government of Republic of Korea, and one person was accepted for a MS scholarship programme in actuarial science by the Asian Society of Actuaries.

**Archive:** Within the fiscal year, the FRC received and replied to 9998 documents and 500 claims, and addressed 3956 documents abroad. Moreover, 8662 referrals were provided to individuals from 12,353 archived files.

Table 14. Documents

No.	Received documents and applications	2016
1	Total document circulation /by number/	14454
2	Total document /by page/	213327,5
3	Documents per day /by number/	57,4
4	Documents per day /by page/	846,5
5	Document units in archive	12353
6	Referral	8662

Source: The Financial Regulatory Commission

### 4.3. COOPERATION

The FRC is the member of three international financial organizations and has signed Memorandums of Understanding with seven foreign financial regulatory organizations to enhance its foreign affairs, ensure compliance with regulatory and supervisory international standards, and share information. In addition, a total of four ongoing projects were implemented at the FRC.

The FRC successfully hosted the 6<sup>th</sup> meeting of the SME Finance working group of the Alliance for Financial Inclusion (AFI) in Ulaanbaatar, Mongolia. The meetings, foremost subjects included; the current situation of Mongolian financial inclusion and its goal and challenges, the financial reform of SMEs and its process, the financial inclusion policy, a consolidated database, and the infrastructure of member countries.

Moreover, the FRC assumed leadership of the Agricultural finance-working group to promote and develop SMEs and introduce agricultural infrastructure as strategic goal.

The FRC held seven trainings and seminars for its employees as well as eight trainings for securities companies with the cooperation of Japan International Cooperation Agency on "Project for Capacity Building of Capital Market in Mongolia". Trainings included development of the capital market, issuance IPO and dual listing, and activities of SRO. Within this project, one FRC personnel has been granted for the three-month training program of Japan Financial Services Agency in Tokyo, Japan.

In the area of combating money laundering and terrorism financing, the FRC established a regulation on "Guidelines of the Risk-Based Supervision" with the support of consultants of the IMF to enhance nonbank financial sector supervision. A meeting of Mongolian combating money laundering and terrorism financing on "Evaluating the National Risk Assessments" was held.

Within the project framework "Multi-Sectoral Technical Assistance Project" (MSTAP) being implemented by the World Bank, the current financial status of Mongolia, initiating programs of the government and the State Great Khural were discussed with financial sector's representatives of Asia and Pacific as well as the policy of the FRC, its regulatory statement and implementation of the second phase of MSTAP.

"Promoting Inclusive Financial Services for the Poor" project supported by Asian Development Bank was completed in April 2016. The continuous collaboration between the FRC and ADB, another technical assistance project document has been signed on 2 November 2016 by two organizations. Within the framework of this project, we are focusing on developing a favorable legal environment for members of savings and credit cooperatives, strengthening their capacity, and working with international and national consultants.

"Capacity Building of Financial Market and Training Project MON/004" was supported by the Government of The Grand Duchy of Luxembourg and was productively completed in June 2016.

One of positive results of this project was the FRC further enhances cooperation with international consultants and is approved to have 40 days of training sessions for the FRC personnel by House of Training of Luxembourg in 2017.

In an effort to transparent of activities, a Memorandum of Understanding was established between the FRC and media organizations to communicate the FRC decisions and information on financial markets to the public.

In cooperation with professional associations, the FRC have organized several events, i.e., a discussion on “One goal – One Solution” was coordinated with Mongolian Association of Securities Dealers,

a seminar on “Insurance System, Mandatory Insurance, and Insurance Loss Adjusters” was arranged with Ministry of Finance, Mongolian Insurers Association, Mongolian Association of Mandatory Insurance and Insurance Loss Adjusters Association of South Korea, and training on actuarial was organized with Mongolian Insurers Association and The Society of Actuaries of Mongolia.

Furthermore, examination content for rights to practice professional services as a member of the Mongolian Association of Securities Dealers was revised by the FRC. The higher standard and was approved by the “Professional Counsel”.

#### 4.4. BUDGET AND FINANCE

The FRC’s fiscal year 2016 budget was approved for MNT2,713.6 million. In order to provide the FRC’s main functions, such as regulation of local entities, on-site inspection in accordance with citizens’ complaints, enhance public financial knowledge, and introduce legislation, the approved budget was insufficient. Therefore, the FRC requested that the Ministry of Finance, the Standing Committee on Economy, and the Standing Committee on Budget increase funding.

The FRC’s budget was re-approved at MNT110.3 million within Mongolian Supplementary Budget and was financed at MNT2, 823.6 million in September 2016.

The FRC planned to allocate MNT822.4 million to the Treasury from its 2016 operating revenue, MNT1,190.9 million was allocated to the State Budget an increase of 44.3%. Moreover, MNT96.4 million of fine revenue and MNT50.2 million of fee incomes were allocated to the Treasury.

Table15. Budget revenue and expense /MNT million/

No.	Budget	Amount
1. Budget revenue		
1	State budget revenue	1,735.3
2	Main operational revenue	1,190.9
3	Grant fund revenue /ADB/	172.6
4	Total revenue	3,102.1
5	Approved budget	2,823.6
2. Budget expense		
6	Salary and social insurance expense	1,822.5
7	Office rent and utilization expense	343.2
8	Membership fee of international organizations	142.7
9	Other expenses of services /projects and programs/	172.6
10	Procurement and material expense	194.7
11	Total expense	2,675.5
12	Balance	147.9

Source: The Financial Regulatory Commission

## PLANNED ACTIVITIES

The FRC plans to take action on shifting domination of commercial banks to developing the nonbank financial sector, strengthening competitiveness, enhancing market participants in nonbank financial sector, developing policy on creating new multi-pillar structure and developing a favorable legal environment for the financial market.

To accomplish this the FRC will be participating in working groups on “The Concept Paper for Mongolian Sustainable Development – 2030”, “The Monetary Policy of Mongolia – 2017”, “Economic Revitalization Program” which were approved by the State Great Khural.

The FRC is expanding its supervision and regulation of the financial sector. Currently, more than 20 laws and over 200 regulations and guidelines on the FRC activities were approved and implemented. In addition, 2,017 organizations and entities, 3,741 individuals were regulated by the FRC. Furthermore, the FRC will be revising its legislation.

In the enhancing risk based supervision, the FRC will be expanding research on supervision methods and techniques for inspecting regulated entities. Moreover, it will be taking actions on developing the infrastructure of capital market, clearing and settlement system, and resolving current challenges. The FRC will also seek to create more professional and institutional investors in capital market and establish more investment funds.

The draft proposal on creating a regulatory environment for developing life insurance, inclusive insurance and expanding the pension fund will be developed. The regulatory environment for new products of mortgage insurance will include a financial literacy program for insures. A regulatory

environment for activities for nonbank financial Institutions will be developed as well as and a revised law on activities of nonbank financial institutions will be drafted. A midterm development program from 2017 to 2021 for savings and credit cooperatives will be composed consistent with the corporate strategy of the FRC and a project on amendments to regulations of saving and credit cooperatives.

### THE FRC'S STRATEGIC PLAN INCLUDES:

- Improving the legal and regulatory environment;
- Developing the market infrastructure;
- Strengthening capacity of professional participants;
- Introducing new financial products and enhancing financial inclusion;
- Protecting financial consumers' right;
- Cooperating with international organizations;

In the future, the FRC will expand its internal cooperation with the State Great Khural of Mongolia, the government of Mongolia, the Ministry of Finance, the Mongolbank as well as collaboration with international organizations. Moreover, the FRC will wholeheartedly dedicate itself to achieve greater success as part of the “Develop Sustainable Financial Sector Ensuring Best Compliance with Internationally Recognized Standards and Practices” initiative.



FINANCIAL  
REGULATORY  
COMMISSION