

Mongolia banks under pressure

In Mongolian

Banks in Mongolia are facing weaker profits this year as one of Asia's fastest growing economies cools, triggering a downpour of higher borrowing costs and an increase in non-performing loans, while credit rating agencies are watching the banks' vulnerability to China's continued economic slowdown.

Recent downgrades in Mongolia's credit rating following falls in commodity prices have piled more pressure on the banks by increasing their cost of borrowing in overseas markets. The devaluation of the tugrik, which has lost about a quarter of its value against the US dollar since the start of 2013, has also pushed up the price of new foreign currency loans as well as the cost of servicing existing loans.

Despite the gloomy outlook, banks in this mineral-rich country are working to regain some momentum by beefing up their retail operations. The newly appointed prime minister Ch. Saikhanbileg has promised to clear the way for the delayed second stage Oyu Tolgoi mining project, a \$5bn investment that would help reinvigorate the economy.

Credit downgrades hit banks

The spate of ratings cuts on Mongolia are cooling the appetite for lending to private-sector banks. Standard and Poor's (S&P) cut its long term sovereign credit rating from B+ to BB- in April amidst concerns over the health of the economy and dwindling foreign reserves. Moody's has also flagged its concerns, cutting its assessment of Mongolia's sovereign standing in mid-July to B2, a ranking which denotes high credit risk and maintained its outlook as negative.

Like S&P, Moody's cited Mongolia's strained external liquidity position as well as the government's expansionary monetary and fiscal policies, including providing liquidity injections to the banking system. It also warned that Mongolia is vulnerable to any further slow down in the Chinese economy and a reduction in raw materials exports, which would add pressure to domestic growth and liquidity.

A third agency, Fitch Ratings, set a negative outlook for Mongolia's banks, though it noted domestic lenders have a limited direct exposure to the mining sector because their capital levels are not strong enough to advance big loans. However, any prolonged downturn in the mining industry will impact the overall economy and the banks' loan portfolios.

Weaker outlook

Positive revision to Mongolia's credit outlook is unlikely for now with prices of key commodities coal and copper still weak. Economic growth stood at 7% in the first nine months of the year after the economy expanded by 12.3% in 2013, according to a National Statistical Office (NSO).

In October, the World Bank lowered its growth forecast for Mongolia this year to 6.3%, down from the 9.5% it had predicted in July.

As a result of the contracting economy, banks are likely to see the performance of their loan books deteriorate further. Data issued by the NSO in November showed that outstanding loans stood at MNT12.8trn (\$6.8bn) at the end of October, up 1.8% or MNT222bn (\$118.2m) from the previous month and up 22.4% or MNT2.3trn (\$1.2bn), year-on-year, noting that the pace of non-performing loans (NPL) – up 2.7% to MNT606.3bn (\$322.8m) month-on month – being added to the banks' ledgers was quickening.

At the start of the year, Moody's placed three Mongolian banks, Khan Bank, Trade, Development Bank of Mongolia and XacBank, on negative outlooks, citing risks from rising bad loans, slower economic growth and a deteriorating operating environment.

There is also concern about the cooling of the local property market. House sales in Mongolia are significantly down on last year with apartment sales down to a level five times lower than in 2013 according to some estimates. With banks having extended credit to construction firms and developers, an increase in unsold real estate could drive NPL rates further.

G. Ganbold, CEO of Golomt Bank, said the property slowdown may require banks to adjust their risk exposures in certain areas. "One potential problem area is construction and real estate," Ganbold told OBG. "We faced a big boom in 2011 and 2012, and now there are many unfinished projects or finished developments that cannot find buyers."

Hope from Oyu Tolgoi, retail banking

Despite the weakening outlook, Mongolian banks still see potential for expansion in some areas. Khan Bank CEO, Norihiko Kato, sees growth in retail banking, particularly card and ATM services. "On the whole, there are opportunities to be had and while the banking sector may not grow as quickly as it has in the past few years, its expansion will continue to outpace that of the overall economy going forward," Kato told OBG.

There are also hopes the government will clear some of the logjams that have held up major foreign investment projects, in particular the Rio Tinto project in Oyu Tolgoi, which has the potential to account for a third of GDP when fully up and running. Ch. Saikhanbileg said on being appointed, in mid-November, his main priority in office would be to invigorate the economy.

Onlooker agree it is the most pressing issue that needs to be solved. "If Saikhanbileg does not move quickly to resolve the Oyu Tolgoi impasse and stem the decline in economic growth, investors may choose to stay on the sidelines until after the 2016 elections," said Marius Toime, a projects partner at international law firm Berwin Leighton Paisner in a Financial Times column.

Source: Oxford business group