

ONE. INTRODUCTION

In order to develop the legal environment of the capital market in line with international standards as well as to develop and introduce an appropriate regulatory structure, support the activities of professional participants of the market, and build staff competences, the Financial Regulatory Commission (FRC) announced 2007 as the year for capital market development and within this framework, the main objective of the FRC was to implement tasks indicated in the Action Plan of the FRC.

The FRC has completed following tasks in order to achieve its goals and objectives. The Commission has developed appropriate functional structure for the FRC and job descriptions of each departments, strengthened staff capacity, standardized all forms of activities, created and maintained good quality working environment, ensured public awareness on the activities and functions of the newly established FRC, promoted expansion of both foreign and domestic cooperation, and regularized supervisory activities to ensure compliance with relevant standards imposed on entities under the FRC regulation and improved efficiency of both off-site and regular supervisions.

During the reporting year, the Commission convened 18 meetings; discussed and made decisions on 238 urgent matters; issued 215 resolutions and 18 notifications; imposed supervision on the implementation procedures and produced quarterly performance reports, which illustrate that the total number of matters discussed and decided during the year doubled compared to 2006.

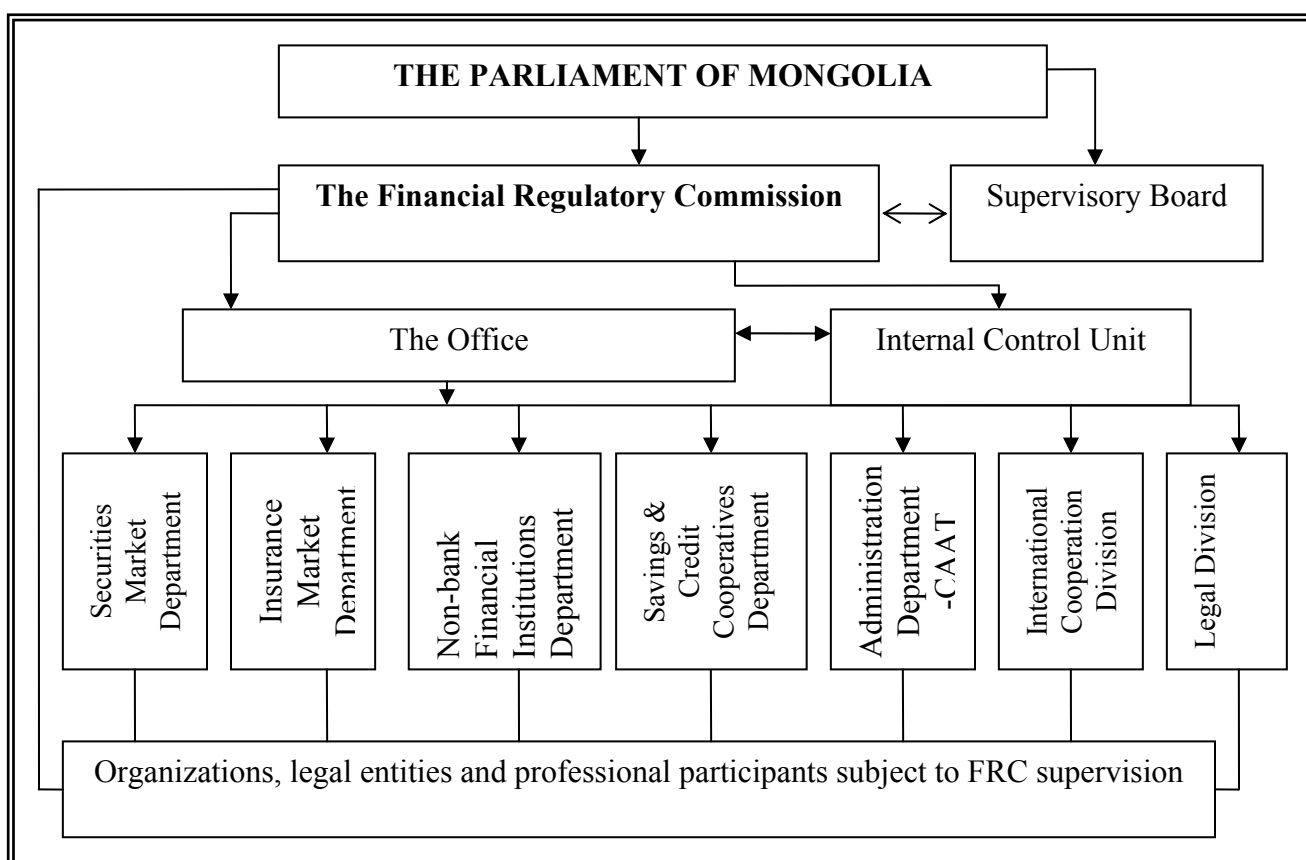
The Commission received total 4398 official letters and facsimiles from both domestic and foreign individuals and organizations and provided responses accordingly. Out of 866 complaints filed to the Commission, 836 were resolved through detailed examinations.

The Commission with the guidance of experts from Capacity Building for Financial Sector Reforms project funded by the ADB, undergone some structural changes considering the models of best organizational structures of international counterparts, and reorganized each department based on sectoral model which includes total of 7 units such as Securities Market Department, Insurance Market Department, Savings and Credit Cooperatives Department, Non-Bank Financial

Institutions Department, Administration Department, Legal Division, and International Cooperation Division.

The internal control unit entitled with functions to ensure prompt execution of Office activities, ensure compliance with resolutions and decrees, monitor the budget expenditure and provide advice to executives, worked under the direct supervision of the chairman of the Commission with the purpose of strengthening and expanding the unit capacity and ensuring its independence.

The revised organizational structure of the FRC



The performance agreement was made between the General Manager of the FRC and the General Budget Administrator and product delivery report was created and submitted to the relevant authorities by the General Manager.

The Commission developed and approved its mid-term action plan and its implementation agenda for 2008-2010. Each department of the Commission formulated

their annual and monthly work plans consistent with the mid-term action plan and activities were carried out according to the plan.

Considering insufficiency of office premises of the Commission, the ownership of annex of the Government building IV was transferred to the Commission at its request.

The annex was originally built in around 1960s for the purpose of holding conferences and seminars and since then the quality of the building has deteriorated and no longer satisfies the working safety code requirements as reported by the relevant professional organizations. Following submission of the official request to the Government and the Parliament to construct a consolidated training center for financial education as a replacement of the annex, the financing was approved and allocated in the state budget.

The commission has exerted efforts to expand its cooperation with foreign counterparties in the context of exchanging information and knowledge in order to strengthen the infrastructure of non-bank financial sector, enhance its regulatory system and provide competent staff members and develop non-bank financial sector in line with international standards in a short term. Moreover, within budget limitations the Commission has always been active in participating in important events organized by both securities and insurance international organizations fulfilling its membership role.

Becoming a member of the International Association of Insurance Supervisors on the day of September 19 of 2007 has proved recognition of the Commission on international arena and established the basis to broaden the scope of its cooperation with other Insurance Regulators.

The Commission with 10 other organizations jointly organized specialized trainings and seminars aimed at restoring confidence between the regulator and professional participants, determining their common goals, and promoting cooperation in achieving their common goals for further development.

The Commission has taken steps to build closer relationship with foreign and international financial development organizations as well as resolving many pressing issues in the scope of its powers entrusted within the Law by means of implementing projects and programs.

Within the scope of the objective initiated by the International Organization of Securities Commissions (IOSCO) in which all member countries of IOSCO must sign the IOSCO MOU by Jan 01, 2010, a request was made to the ADB to include the FRC

in the ADB funded program implemented in Asia Pacific Region through which the Commission was granted with 30000 US dollars for an international expert to prepare a diagnostic study to the FRC's compliance with the IOSCO MOU.

The FRC related tasks of ADB TA project 4737-MON "Capacity Building for Financial Sector Reform" have been successfully carried out and completed.

The European Bank for Reconstruction and Development made a resolution on providing a technical assistance grant worth of 30000 EUR for the purpose of enhancing the insurance regulation in Mongolia. Further friendly cooperation was established with embassies of Japan and Turkey as well as with Korean International Cooperation Agency, Japan International Cooperation Agency and United States AID in the context of training of employees on the financial market, providing advisory services, and providing opportunities for the FRC employees to participate in various training programs and seminars being held in foreign countries by means of giving financial assistance.

Assignments were carried out within the scope of trilateral and bilateral memorandums of understanding among the FRC, Ministry of Finance, Bank of Mongolia, Ministry of Urban Development and Construction, Mongolian Chamber of Commerce and Industry, "XAC" bank and the implementation unit of the "Index Based Livestock Insurance Project".

TWO. THE SCOPE OF ENSURING STABILITY OF THE FINANCIAL MARKET

The Financial Market Stability is mainly determined by the level of the implementation of interconnected objectives such as ensuring the public confidence in the financial market, raising public awareness on financial market, protecting the legal rights of financial market participants, and minimizing financial crimes and breaches. These objectives have been reflected in the mid-term policy documents.

1. CAPITAL MARKET

"Capital Market Development Year" initiative was aimed at raising both public and Government awareness on the development of the capital market, improving the corporate governance, strengthening the capacity building of the professional participants, establishing appropriate regulatory regime, encouraging investors, and promoting reliability of public information.

A. Promoting Public Confidence in the Financial Market

Improving the legal environment of the capital market has been a priority for the FRC. This is becoming more important as new flow of products rapidly come into the market. In this sense, the regulations on IPO, Consolidated Database for the Securities Market, Service Fees Collection from License Holders, Inheriting Security Backed Ownership Rights, and regulation on registering the securities of Mongolian companies seeking to be listed overseas have been developed and amendments were made.

Substantial amount of mining and mineral resources in Mongolia are becoming the main attractions for foreign investors as expected. The strategic mining sites as well as the possibilities of issuing securities with no less than 10 percent of the capital through the Stock Exchange have resulted the exploration of opportunities for listing of Mongolian stocks on foreign markets and trading of foreign securities on Mongolian market. In relation to this, the draft amendment to the Securities Market Law and related regulations were developed in order to establish a regulatory mechanism for the changing market.

With the purpose of enhancing housing financing and establishing the legal environment for the secondary mortgage market development, the draft Mortgage Law was formulated with the help of relevant organizations and was submitted to the Parliament for passage. In addition, the concept paper and draft Law on Mortgage Backed Bond and Law on Asset Backed Securities have been developed accordingly with the help of international consultants provided by the USAID as well as of other relevant organizations and have been handed to the Ministry of Justice and Internal Affairs. Additionally, the failure of indicating some types of financial crimes in the Criminal Law, has resulted proposals to be made to relevant authorities and gained their approval to add following provisions to the law: Notaries and State Right Registrars violating owner's rights, Violating the Law on Savings and Credit Cooperatives, Violating the Law on Activities of Non-bank Financial Institution and Violating the Insurance Law.

It is becoming increasingly crucial to introduce internationally recognized corporate governance principles that establish mechanisms to ensure that investors and shareholders are fulfilling their responsibilities, sanctions are improved and investors are provided with material facts in a timely manner. Therefore, the Commission, based on the above principles, has developed and approved "Corporate Governance Code" which is not restricted to joint stock companies only, but also it is designed to promote business management and social responsibility for any corporation.

With the view of solving many critical issues on this market that require resources, narrow expertise and knowledge within the short period of time with the united effort of the Government along with international banks, donor organizations, the public, and professional organizations, drafting the “Capital Market Development Program 2008-2011” has been completed and now ready for submission the Parliament for approval.

The stability of market participants and their regulatory measurements are the most important means for any market development. The commission has given an importance and provided its comments to the amendments of the regulation on trading and listing of securities approved by the Mongolian Stock Exchange which is the only securities trading institution in Mongolia.

A new “E-clearing house” system was launched at the Securities Clearing and Settlement House and Central Depository (SCSHCD) which safeguards securities and assets worth 1 billion MNT in ownership of approximately 600 thousand citizens and legal entities.

During the reporting year, the Commission renewed the licenses of the Mongolian Stock Exchange, the SCSHCD and 15 Brokerage and Dealer companies and granted licenses to 9 new companies such as “Bats”, “Global Asset”, “Ci Ci Pi”, “Frontier”, “Bloomsbury Securities” which increased the number of Brokerage and Dealer companies to 36 of which 8 began to offer underwriting services. The total of 8 companies were granted additional licenses among which 2 companies offer investment advisory services, and 2 engage in broker and dealer activities respectively. Also 5 of the 8 licensed companies get investment from Japan, South Korea and the United States of America.

The Commission has placed high importance on nourishing investors and encouraging new type of instruments coming into the market aimed at restoring the market activities as well as speeding up the market development. In this context, there were 6 companies, namely “Tuul-Songino Usnii Nuuts”, “Hi Bi Oil”, “Olloo”, “Nako Tulsh”, ”Monfresh Juice” “Moninjbar” filed their documents to the Commission to launch IPO and were granted licenses to issue 145.8 million securities valued at 123.6 billion MNT and 100 million bonds valued at 2.2 billion MNT.

B. Promoting Public Financial Education

Promoting public financial education is becoming increasingly important to the development of the capital market. The reason for that is, during the beginning of 1990, there were many citizens, who were given vouchers to own shares and because of their

lack of knowledge and experience in capital market in general, many have never opened their personal accounts with the SCSHCD and those who opened their accounts have never managed or looked after their accounts.

The Commission, using its resources to the extent possible, published and disseminated brochures and pamphlets to the public about the nature of capital market, its further outlook, and its instruments and mechanism, and have taken specific measures to coordinate and finance those activities. For example,

- “Shareholders’ Day” jointly organized with the Mongolian Stock Exchange aimed at raising public awareness on capital market
- Announced an academic contest titled “Capital Market Development” among scholars and students and published 3 volume books which consisted of academic works written by 36 students and 22 scholars, and 5 students and 4 scholars won the contest and were awarded accordingly.
- Organized a fair titled “Capital Market Development-2007” for the first time in Ulaanbaatar city as well as in all provinces to the general public. Total of 7 thousand citizens attended the fairs. During the fair at the Sukhbaatar Square in the city, approximately 589 people received advice, and brochures and leaflets were disseminated and 394 people opened their accounts with SCSHCD.
- Objectives and Principles of Securities Regulation published by IOSCO was translated into Mongolian and Principles of Corporate Governance issued by OECD was translated and published in Mongolian based on which “Corporate Governance Code” was developed and approved by the Commission.
- Broadcast and publicized measurements implemented by the FRC as well as capital market related information to the general public through radio stations, televisions and newspapers.

As the market develops at its accelerating pace, it necessarily requires regular capacity building of staff of the Commission as well as of market intermediaries. The Commission ensures that its staff receives comprehensive trainings and seminars and other trainings organized by both domestic and foreign organizations. Still this is insufficient for the staff to perform their duties effectively.

During the reporting year, training for the securities market participants to issue licenses was held twice and there were 176 people participated of which 132 received their licenses to run a business on the capital market. In the scope of cooperation, the Commission organized joint seminars with Mongolian National University, Russian Economics Academy named after Plehanov, Bloomberg, Reuters, Asian Development

Bank, Taiwan Securities Exchange, and Financial Services Commission of Korea and the Commission staff actively participated in those seminars.

C. Protecting the Legal Rights of Financial Market Participants

During 1990-2000, embezzling customers' shares allocated during the privatization period and carrying out other illegal behaviors were common among the market intermediaries caused by many market deficiencies such as inadequate regulatory framework, lack of sanctionary arrangements and conduct of market intermediaries and low level of public financial education. The impact of this misconduct is tremendous causing investor distrust and encumbrance to state organizations.

The majority of the complaints filed by the citizens were related to this specific issue. Resolving these complaints required a lot work hard work, research and evidences. By the decision of the Commission, total of 23 securities transaction involving 3.9 million securities, worth of 614 million MNT which are owned by 24 citizens were revoked. In order to protect investors' legal rights, the Commission has taken part in the court for administrative cases and defended inspectors' position of prosecution for embezzlement and misuse of clients' assets of 23.1 thousand securities worth of 90 million MNT.

When a joint stock company goes private, there is a potential risk that small investors' rights are being violated. This year, the Commission delisted 1.3 shares of 11 companies that filed their request to change their status which was owned by 3926 citizens and 29.2 million MNT of shares were placed in 3839 shareholders' account at the SCSHCD.

Those who own controlling shares of a publicly traded company must make tender offer according to the Company Law if they wish to purchase voting shares of the company. This is particularly important in ensuring the protection of small shareholders' rights. In the framework of ensuring compliance with this requirement, the Commission made legal orders and conducted enforcement actions on tender offers. As a result, controlling shareholders of 7 publicly traded companies filed their statement for tender offer and resolutions were made accordingly. Currently there are 4 tender offers expired, and during the tender offer period, the total of 7.4 million shares were acquired.

In accordance with the Government resolution #155 of 2006, 57870 clients were compensated with 45.8 million MNT for the losses incurred due to failure of custodian banks which was accomplished with the help of SCSHCD.

D. Fighting Against Financial Fraud and Misconduct

The Commission conducted on-site supervision during the first half of 2007 with respect to listed companies as well as market intermediaries to ensure compliance with the “Securities Market Law” and the “Company Law”. 202 of 251 publicly traded companies in provincial areas and 126 of 132 publicly traded companies in the capital city totaling 309 publicly traded companies as well as 25 broker and dealer companies have been involved in this process.

The investigation result shows that there are regularly operating 151 publicly traded companies, poorly operating 62 publicly traded companies and 146 insolvent companies. 67 percent of these insolvent companies’ capital was misused or are incapable of carrying out further operations. This shows that it is already the time to strengthen the MSE listing standards in compliance with international standards, ensure that investors are given fair access to market facilities, and develop the securities market structure and bring it upto internationally recognized level.

During the on-site supervision of Broker and Dealer companies, it was revealed that 4 companies failed to meet minimum capital requirements in accordance with the “Securities Market Law” and 13 companies failed to comply with “Regulation on Capital Adequacy for Market Intermediaries and Loss Provisions for clients”

Following are some of the common misdeeds Broker and Dealar companies engage in:

- Fail to register with State Registration Office whenever amendments are made to the Company Charter;
- Fail to approve and comply with their Company Charter;
- Fail to provide investors with material information, and underperform their duties in terms of examining and resolving client complaints and request in a prompt manner;
- Fail to distribute dividends and capital gains in a prompt manner
- Fail to disclose their financial datas, disseminate relevant information to investors and clients, and file reports of their shareholders meetings to the Commission.

Additionally, misconduct of some of the Brokers led to suspension of licenses and many clients' assets were transferred from the Brokers accounts to other Brokers accounts that are compliant with relevant regulations. However, these Broker companies are appeared to be negligent towards these accounts because of their insufficient capacity to oversee all the accounts they are entrusted with.

The Broker and Dealer companies that are responsible for providing services to Dornod, Sukhbaatar, Tuv, Bulgan, Hentii, Bayan-Ulgii, and Uvs provinces as well as Baganuur district operate regularly and provide services according to their schedule, however; there is no accessibility for the citizens in Gobisumber and Huvsgul provinces for B&D services since there is no existing B&D companies that provide services to clients in those areas such as checking account balances, and making orders to buy or sell shares.

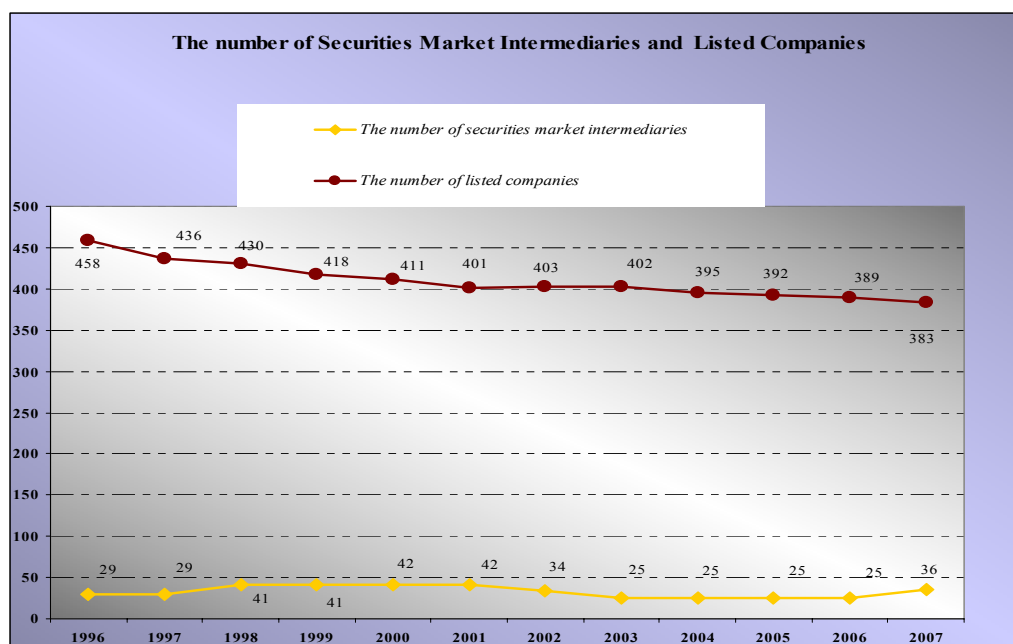
On the other hand, it is evident that B&D companies, an important securities market intermediary, face challenges of being financially sound as well as being profitable from their operations as we can see that during the year of 2006, 14 out of 25 B&D companies have lost 60 thousand to 5.6 million MNT and 10 have lost 42.3 thousand to 47.2 million MNT.

Measurements have taken against misconducts revealed during the supervision process and imposed administrative sanctions and fines for 1.5 million MNT to individuals and companies that violated related legislations.

E. The Current Situation of the Market

Following the rapid growth of the economy, positive signs are seen and the main indicators of the market are showing some dramatic growth.

1. Market Intermediaries

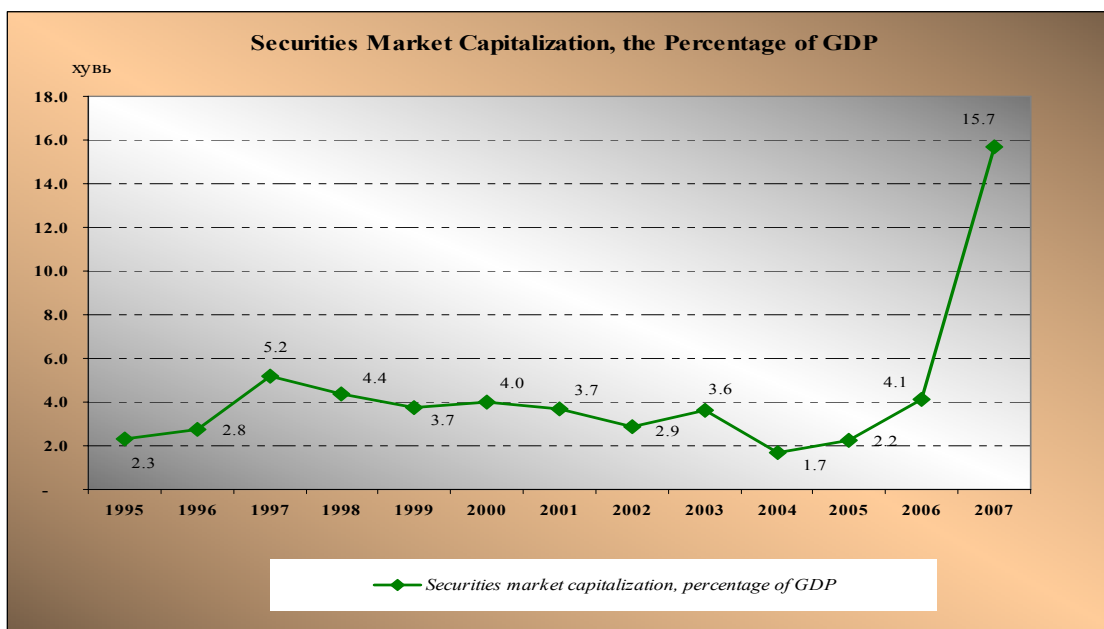


The decreasing trend of listing of shares on the MSE is related to the fact that the ending of accumulation process of securities, as well as growing interest of shareholders who hold controlling shares of a publicly traded company to change their company status to a private company. Only 10 percent of total of 2.5 shares of 383 listed companies are being actively traded on the MSE which makes it necessary to revise the MSE listing and establish listing categories on the MSE.

During the years of inactive securities trading, the number of B&D companies stayed unchanged until the market has become more active and national companies started offering IPO's which increased the total number of B&D companies by 11 new companies that are offering broker, dealer and underwriting services.

During the year of 2007, 119 joint stock companies held their shareholders meetings, 138 joint stock companies submitted their financial statements to the Commission and 28 joint companies distributed dividends for 7.4 billion MNT.

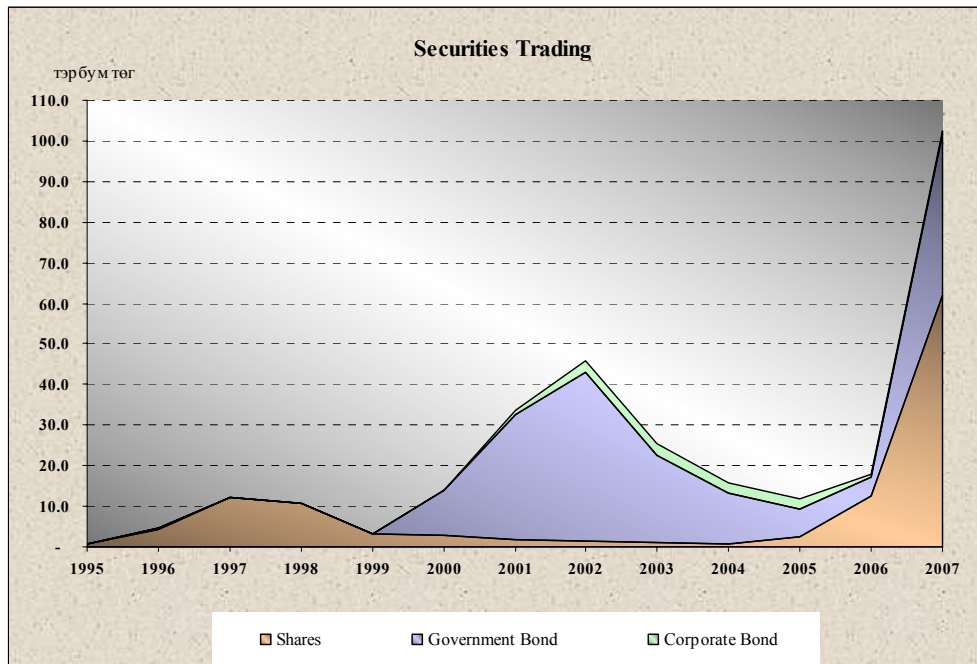
2. Market Capitalization, Percentage of GDP



During the reporting year, the market capitalization increased to 716.6 billion MNT from 131.9 billion MNT in the last year which indicates that the market capitalization grew by 585.7 billion MNT which is 5.4 times as large as the previous year.

During the last 10 years, the market capitalization has been 3.2 percent of GDP, however, during the reporting year, the value of the stock market capitalization increased by 11.6 percent of GDP due to increased prices of actively traded securities as well as growing number of IPO's

3. Trading of Shares

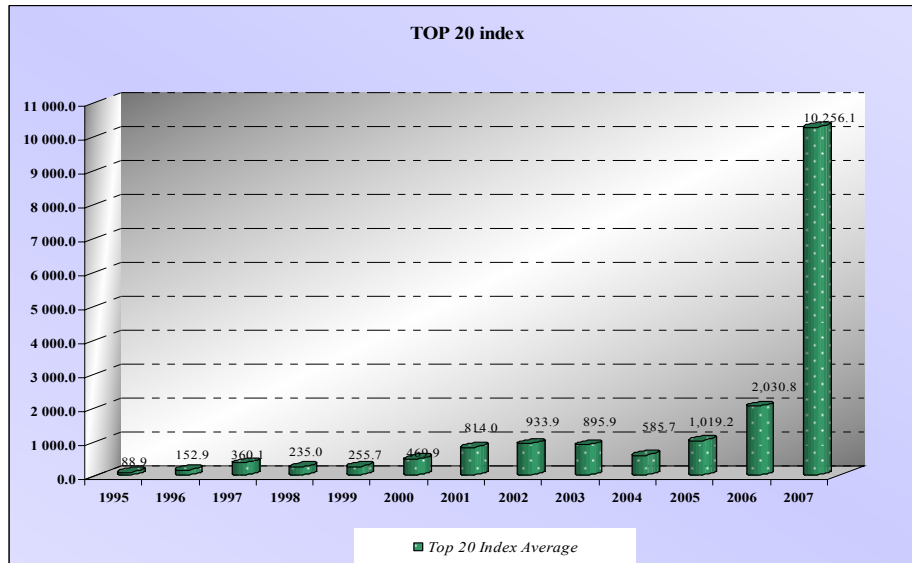


During the year of 2007, there were 253 trading days and 116.1 million shares and 542.8 million bonds of 307 companies were traded and the total trading value totaled 102.6 billion MNT.

62.1 billion tugrug share tradings account for 60.7 percent, and 40.5 billion tugrug bond tradings account for 39.9 percent of the total trading value.

The total trading value of securities rose by 49.5 billion MNT which is 4.9 times higher than the previous year and the total trading value of bond rose by 35 billion MNT which is 7.5 times higher than 2006.

4. Top 20 Price Index Dynamic

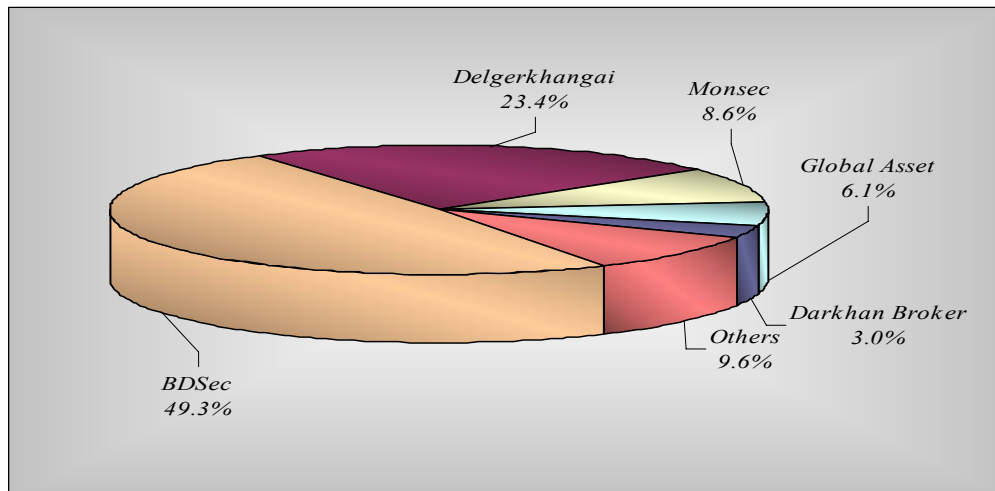


Since the end of 1999, Top 20 index has been calculated based on the portfolio of 20 securities selected using various indicators in order to illustrate the change in the securities market.

Because the general outlook of a market development is largely determined by the increase and decrease of the index, the regular calculation of the index and implementing regulatory measurements are critical.

As of Dec 31, 2006, the top 20 index was 2030.8 points and as of Dec 29, 2007 it jumped to 10256.1 points. The peak reached 13676.9 points during the reporting year which indicates that the index rose by 5.1 times than the previous year.

5. Market Shares of Broker and Dealer Companies



According to an estimation that calculates the percentage shares of the B&D companies of the market based on their overall transaction, 90 percent of the total transaction handled by 5 large B&D companies and the remaining 31 B&D companies each handled only 0.3 percent of the total transaction.

This indicates that the management of B&D companies as well as their staff competency and financial capacities are low which may lead to incompetiveness among the B&D companies.

Therefore, it is necessary to promote merging of B&D companies as well as strengthening their governance and management by a way of imposing stricter terms and conditions for the B&D companies.

F. The Further Implementation of the Policy Measures

Given the fact that the development of capital market is one of the pathways to economic growth, we need to constantly learn from international best practices, make practical evaluations and draw conclusions on current situations, and establish our future outlook in order to regain our strength in the marketplace. The following measures must be taken in order to solve many issues we face on continual basis.

- With the purposes of strengthening the legal environment of the capital market, it is necessary to make amendments to the Company Law, Securities Market Law, Law on Investment fund, Law on Trust, and finalize the drafts for submission and further approval
- With the purposes of developing the capital market and developing and implementing state integrated policy, it is necessary to submit FRC developed

“Capital Market Development Program 2008-2011” to the parliament for passage.

- Develop regulations on IPO in line with roles and responsibilities of the securities market participants recognizing that IPO’s involve major risks such as financial, economical, as well as social risks
- raise the business conduct requirements for the securities market participants, promote high standards of integrity as well as strengthening the disciplinary arrangements along with improving capital adequacy standards for Broker, Dealer companies
- Promote Brokerage and Dealer services in rural areas and ensure that citizens in rural areas are given access to market facilities through the establishment and implementation of service standards
- Privatize MSE and enhance the organizational structure of the Securities Clearing House and Central Depository in its appropriate form that is consistent with international standards which promotes positive impact on the market development
- Strengthening the listing requirements in compliance with international standards and protect investors from the risks of share price decrease by revising listing standards and delisting unqualified securities
- in order to provide investors with full disclosure of material information, create possibilities of conduct risk assessment, and improve supervision of market participants, it is necessary to establish integrated database by solving both hardware and software issues
- By the means of monitoring the trading activities on the MSE as well as effectively implementing the regulatory system, there should be an effective mechanism that addresses price manipulation, insider trading, misuse of client assets and any other fraudulent and deceptive practices.

2. INSURANCE MARKET

Main objectives in 2007 were to develop insurance related rules, regulations and instructions within the scope of the “Law on Insurance” and “Law on Insurance Intermediaries”, to build fundamentals prior to introducing life insurance and compulsory insurance system, to improve the state supervision on the insurance market, and to study and introduce new mechanisms to protect insureds.

A. Promoting Public Confidence on the Financial Market

Although overall insurance legal environment is considered to be formed comparably well, not all the rules, regulations, and instructions which should be passed

with regard to the “Law on Insurance” and “Law on Insurance Intermediaries” are in place. By passing and enforcing 22 rules, regulations and instructions such as “Instruction on Content and Form of Additional Financial Statements of Insurers”, “Instruction on Defining Insurance Related Parties”, “Regulation on Reinsurance Plan Requirements for the Insurants and its Supervision”, the market met the international standards on operation of professional market participants and their financial reporting, endorsed methodology to exercise state supervision system, established fundamentals for life insurance and upgraded supervision system for reinsurance. Furthermore, adoptions of “List of Voluntary Life Insurance”, “Requirements for the Entities to Conduct Life Insurance Business and List of Application Documents for Licensing” are considered as a start of legal environment for life insurance.

By considering precondition of increase in new insurance products and its penetration in the market, the FRC drafted the “Law on Drivers’ Compulsory Liability Insurance” and participated actively to draft the “Law on Savings Insurance” in order to develop legal environment as quick as possible.

Studies and researches have been held on legislation of asset based mortgage loans’ insurance, with relevant organizations.

Translation of 4th International Accounting Standards, the chapter “Insurance Policy” which was adopted by National Standardization and Measurement Council, has been recorded as a start of introducing international standards in the Mongolian market.

Some pressing issues have been solved to a certain extent such as to develop industry infrastructure, to provide professional participants with specialized staff and to prepare auditors specialized on insurance auditing. 15 companies were licensed to run 220 types of insurance activities by aggregate number. The licenses of companies such as “Capital Daatgal”, “Chin Uils Daatgal”, “Mongoliin Undesnii Daatgal”, and “Erel Daatgal” are revoked in 2007 due to their failure to comply with requirements of Law on Insurance and to establish appropriate reserve fund levels.

Following results of the inspections made on “Gan Zam Daatgal” and “Ard Daatgal” companies, their licenses were suspended and were reinstated after flaws were remedied.

Insufficient access of insurance intermediaries and agents nationwide which had negative influence to the market was detected and measures were taken accordingly to resolve the situation. Two companies which passed the inspection and met other qualifications are licensed out of four applications to conduct activities on market as

insurance intermediaries. And 286 individuals, who attended insurance agents' training and passed the examination, are licensed as insurance agents.

Granting the power to the Commission to license the insurance auditors, by new provision in the Law on Insurance, has been considered as an important regulation in terms of protecting insureds' rights and 18 auditors were licensed in 2007.

International tender for "Project on Upgrade and Enhancement of Insurance Regulation" through Technical Assistance from the European Bank for Reconstruction and Development (EBRD) has been processed and concluded.

By introducing new calculation method which calculates and distributes total premium consistently and concurrently through reporting period, regulations such as concrete calculation on insurance companies' financial statements and profitability, registration on premiums and earned premium, and calculation on reserve fund have been enforced in line with international standards.

B. Promoting Public Financial Education

Unless nature, special characteristics of insurance market, importance of involving insurance is not acknowledged by the public, our citizen have to bear the concern in their every actions about all financial risks, capital and psychological loss may occur to their entire life, and presumably, it will lead to negative influences in market development.

Therefore, first steps have been taken in response to the urgent need to form developed mechanisms to ensure quality information dissemination system in order to promote transparency, fairness, fastness, public focus, and informative and advisory functions of insurance market.

First of all, technical specifications to develop information system of insurance market were accomplished with participation of project team TA #4737MON implemented jointly by the FRC and Asian Development Bank. And in this way, the basis for insurance sector database system was established.

The FRC disseminated the news and information about its approved policy, actions, rules and instructions which are intended to improve insurance market regulation in order to ensure transparency as well as the information about licensed insurers, auditors charged for auditing professional insurance participants through mass media and its website. In necessary cases, as a response to requests, the information was provided through official letters.

Two live broadcasting on television were organized about insurance market challenges, and publication titled “For Insurants Attention” was published in order to improve insurants’ education and knowledge on insurance market.

Recognizing importance of staff proficiency and capacity building of professional participants and regulatory body on financial market development, several trainings were conducted specially on the market such as

- two trainings for insurance agents;
- two trainings for insurance company accountants;
- a training for life insurance regulation and on actuary with Korean Financial Supervisory Services;
- a training on life insurance regulation and its supervision with cooperation of Indian Insurance Regulation and Development Authority and Mongolian “National Life” LLC;
- 3 trainings which covered three provinces and licensed agents who shall involve herdsmen in index based livestock insurance with the team of “Index based Livestock Insurance Project”;
- Licensing training for actuaries which is conducted in cooperation with Association of Mongolian Insurers and with funding of Luxembourg Government.

C. Protecting the Legal Rights of Financial Market Participants

Insurants started to realize protecting the rights of financial market participants is one of the main functions of the FRC, and in relation with this, number of applications and complains to the FRC with regard to abuses of rights are increasing. In 2007, 28 complaints were received, investigated and solved according to legal provisions, and 247 official letters and requests were received and responded in the legally prescribed timeframe.

Some transportation and insurance companies were collecting compulsory insurance fee by automatically adding to ticket fee which was a common practice while the liability insurance of passengers and drivers belong to a voluntary type insurance. Such malpractices inconsistent to the relevant laws caused for frustration among public. The companies involved in this activity were imposed with relevant sanctions.

Advisory services related to insurance market legal system and market regulation have been provided by the FRC upon every request from individuals and entities.

D. Fighting Against Financial Fraud and Misconduct

In scope of re-licensing insurance companies, all the insurance companies were examined through the schedule to verify whether they are operating in compliance with laws, rules, regulations and instructions passed by the FRC.

Following are widespread violations and breaches of the companies:

- Granting agent fee to the individuals without licenses;
- Misplacing reserve funds, and using reserve fund assets for other investments which abuses the Commission requirements;
- No applications made to the State Registration Authority inform of changes in companies' charters which violates legal provision;
- Insuring voluntary insurance products through compulsion by utilizing regulatory bodies which are authorized to regulate relevant businesses which abuses provisions of Law on Insurance;
- People often get frustrated because of bureaucratic actions of insurance companies in the process of indemnities, where benefiting from blur and indefinite wordings and definitions on insurance policy.

The 20 million MNT which was imposed from the insurance companies found guilty according to the examination, was collected to the state budget. Orders are given by the state inspectors to the companies in order to cease and to rectify the flaws and the implementations were controlled by the FRC. Starting "Breaches List of Insurance Companies" which enrolls every violation and breaches of the companies is recognized as introducing effective practice to the supervision.

Carrying out financial analyses to the financial institutions through off-site supervision brings advantages for the provision to determine policy making, to become facility to conduct risk management and as well as the basis of database statistics.

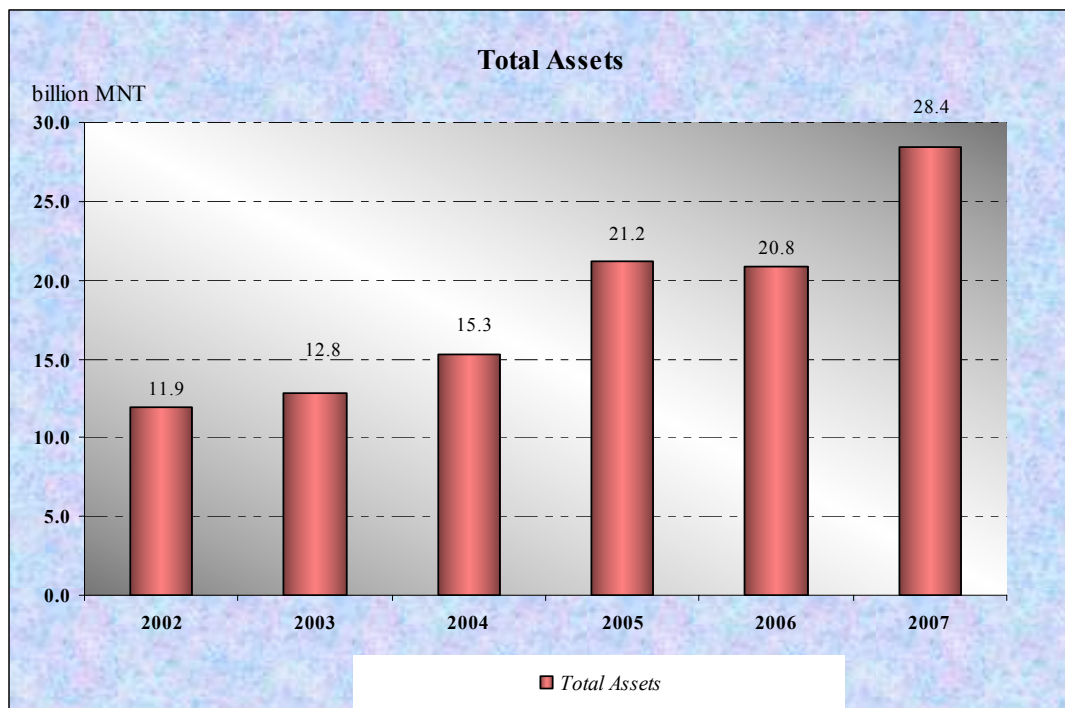
The remote and permanent supervision, analyze and compilation of financial statements on 15 insurance companies are quarterly has been undertaken. Basically, all the licensed companies operating on insurance market are qualified the prudential ratio on solvency with regard to the policy regulated from the FRC to protect domestic insurance market from financial risks and to stabilize the activities.

Insurers' solvency improved since the insurance market reserve fund volume increased and reached 17.8 billion MNT as a result of enforcing "Regulation on Building Insurance Reserve Fund, its Distribution and Control" which was passed in order to increase the risk fund amount, the main prudential indicator for insurers.

E. The Current Situation of the Market

During the reporting year, insurance industry as a whole recorded total profit of 633.5 million MNT, increased the reserve fund by 5.6 billion MNT (45.9%) to 17.8 billion MNT, and made reinsurance agreements worth 4.5 billion MNT.

1. Total Assets

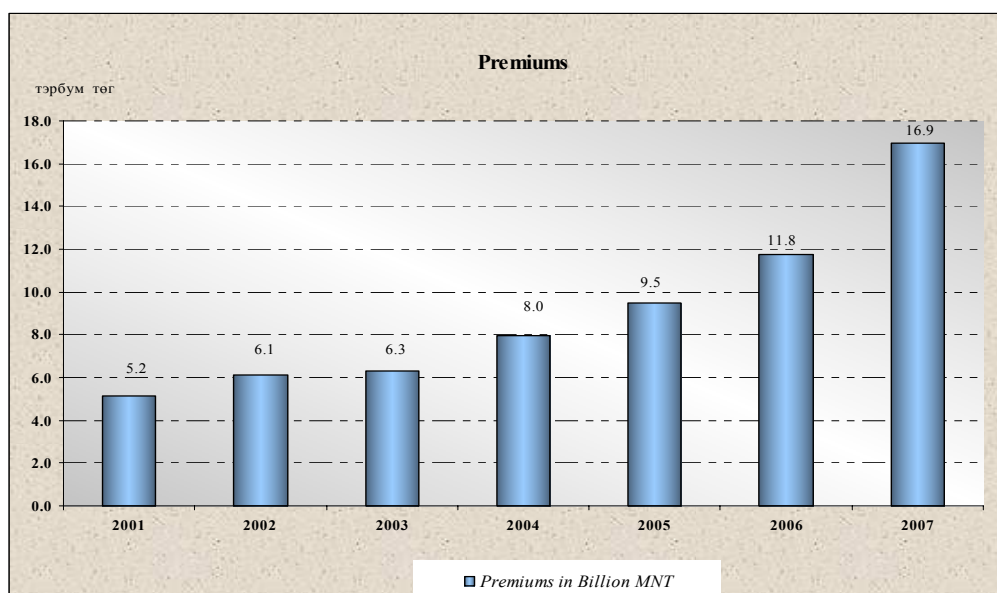


Total assets of insurance companies reached 28.4 billion MNT which gives a rise of 7.6 billion MNT or 36.5% increase compared to 2006.

No significant change has been recorded in assets structure. 80% of total assets are composed by current assets which 67.6% is taken by cash and cash equivalents, 12.0% by short term investments, 9.4% by accounts receivable, and 11.0% by other current assets.

If we look at insurance market performance, accumulated loss of 303.4 million MNT in 2007 is lower by accumulated loss of 594.2 million MNT in 2006, which is 2.9 times of decrease. This shows us positive results of introducing new method of reserve fund establishment which was started from second half of 2007.

2. Premium Income



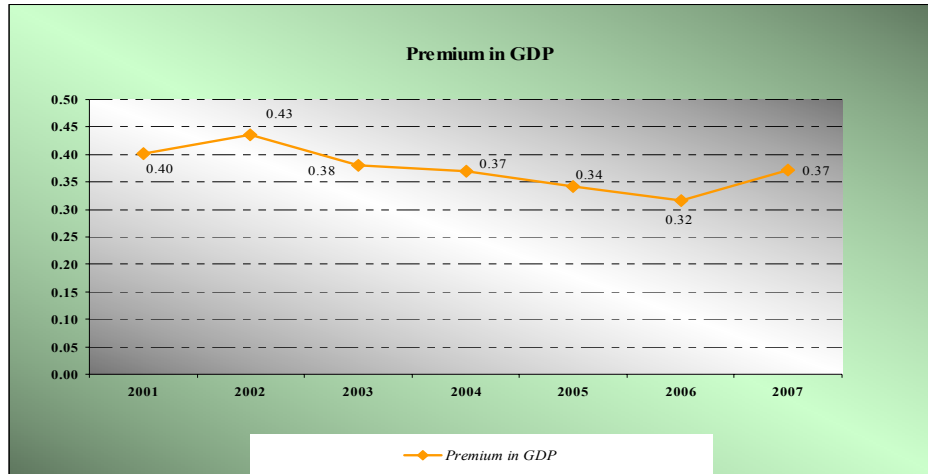
While insurance premium has been steadily increasing with average amount of 1.9 billion MNT within last few years, sharp increase was observed in 2007, whereas growth equaled 5.1 billion MNT or 43.2%. This increase is resulted by introduction of new insurance products to the market and the improved public awareness about advantages of insurance services in order to prevent potential risks which can be proved by the fact that 84.8% of increase accounts to premiums collected from asset and liability insurance products.

Comparison of premiums by insurances type, in 2006 and 2007

(MNT in million)

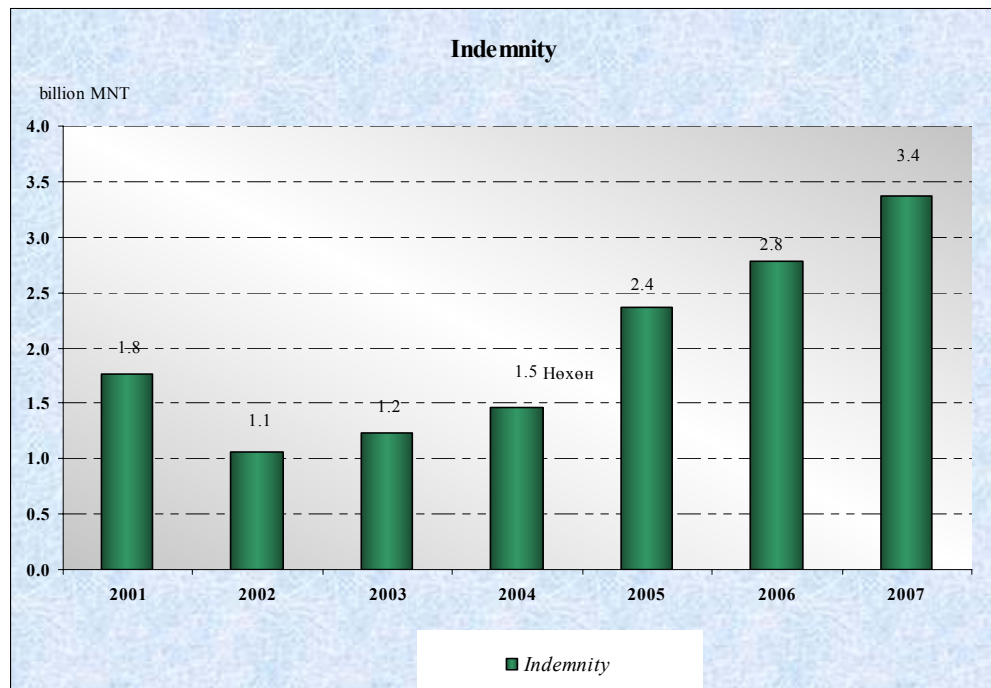
Insurance subclass	2006	2007	Growth	
			MNT in ml.	Percent
1. Interest, and Health Insurance	1 048.4	1 495.0	446.6	42.6
2. Property Insurance	8 051.4	10 534.7	2 483.3	30.8
3. Liability Insurance	2 679.3	4 566.4	1 887.1	70.4
4. Financial Insurance		333.0	333.0	
Total	11 779.1	16 929.1	5 150.0	143.7

3. Total Premiums as Percentage of GDP



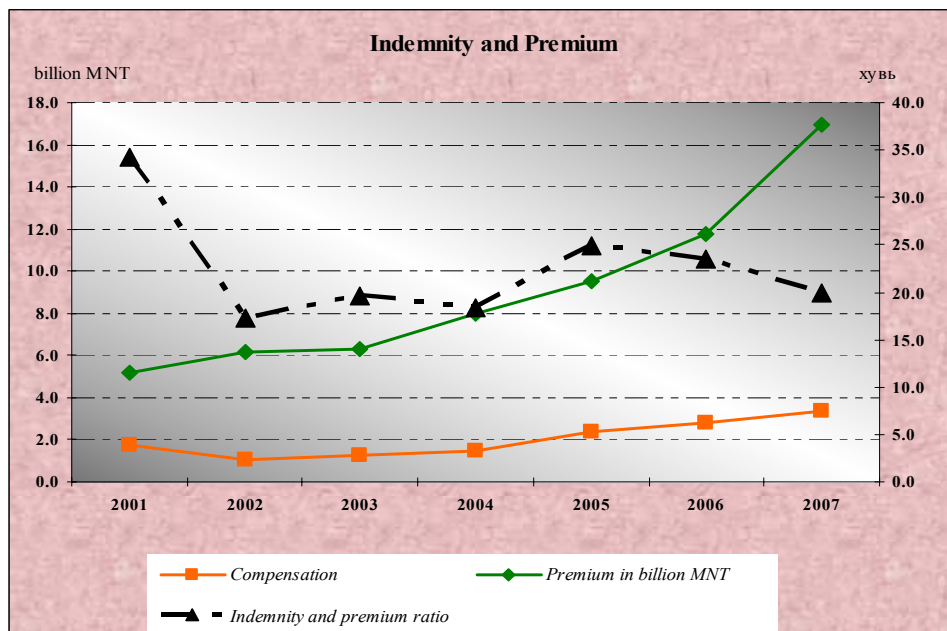
Downward trend of insurance premiums as percentage of GDP observed during last few years, changed in 2007, when 5.2 billion MNT or 0.05 percent increase is recorded. This indicator equals about 10% in developed countries. Therefore 0.4 percent in Mongolia shows us that our insurance market can develop further; there is a necessity to carry out measures to improve public knowledge, and to introduce new types of life and compulsory liability insurances.

4. Indemnity



During the reporting period indemnity level reached 3.4 billion MNT, which constitutes 21.6% increase compared to 2006 level. Increase of indemnity in 2007 was mainly influenced by 37.3% rise in property indemnity and 35.3% rise in liability insurance.

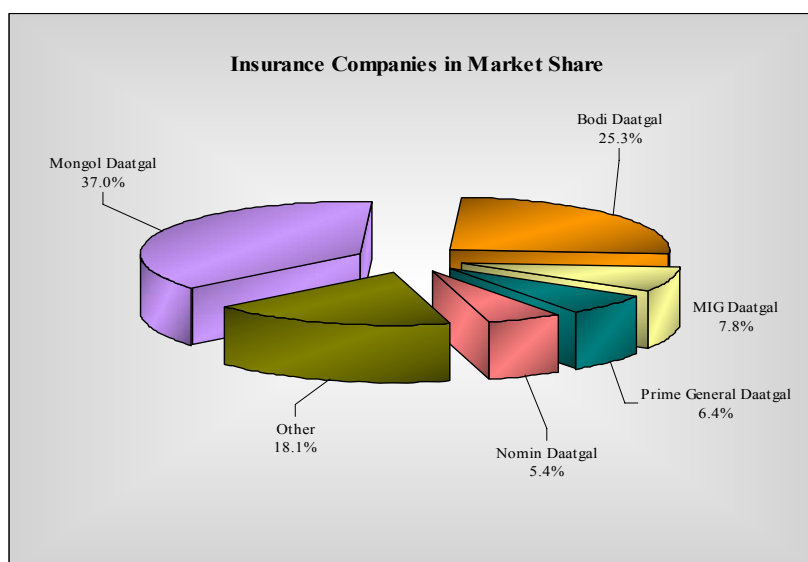
5. Loss Ratio



We see the change dynamics of insurance premium and indemnities for last 7 years, annual increase acceleration of the premiums was almost 5 times higher than the collected indemnities. This trend sharply increases in last 2 years, and may cause decrease of the public trust to insurance and result in negative effects to the insurance market development.

There were a practice in Mongolia, where the calculating the one of the main indicators of insurance sector, the loss ratio, by dividing total indemnity to premium. According to this calculation this ratio was 19.9% in 2007. But it is revealed that, the Mongolian regulation to determine differs from the international practice which calculates it by comparing total indemnities to income accounted premiums. After rectified calculation in 2007, it is now indicating 48.57% which is close to developing markets average of 50%. /loss ratio – shows that how many MNT is compensated back to the insurants from every 100 MNT of premium/

6. Market Shares of Insurance Companies



The market shares of insurance companies based on premiums collection, five companies shown on the above chart occupy 81.9% of whole market. In other words, the remaining 10 companies take 1.8% in average which reveals that market urgently needs competitive environment and companies with high solvency potentials and proper management.

F. The Further Implementation of the Policy Measures

Specific attention should be paid to the following challenges on insurance market and should be solved in the nearest future.

- Considering nascent stage of the insurance market development, it is necessary to introduce new long term and life insurance products as well as compulsory liability insurance products for the persons such as notaries, attorneys, doctors, food manufacturers, and the persons who work with substances which may endanger the environment, and also it is important to approve rules, regulations and instructions in relation with new products and services, and to ensure compliance of legislations;
- It is necessary to implement a policy that increases Mongolian insurance market competitiveness through' financial capability of insurance companies and enhancing the governance and management competence, instead of increasing the number of insurance companies, in order to integrate and expand smaller companies through the regulation of increasing the minimum capital requirements for equity and reserve using funds, to invest in other financial markets. In order to find success in these areas, the Law on Insurance should be amended in relevant provisions;

- Observing several initiatives to establish foreign invested insurance companies or the attempts to purchase local companies with foreign investment, it is urgently needed to form and adopt relevant legal provision to protect domestic insurance market by studying and applying international and regional practices;
- By building legal system that foreign companies which operating on Mongolian territory to be insured with local insurance companies, in order to eliminate unlicensed foreign insurance companies operating on Mongolian market through insurance dealers and intermediaries;
- Develop and approve relevant legislations in connection with establishing national reinsurance company by analyzing the fact that large volumes of funds are is flowing out to the foreign reinsurance companies.
- In terms of providing fair and fast insurance market information system, build database equipped with modern software consistent with current market demands, and develop and carry out financial reporting in line with international standards.

3. NON-BANK FINANCIAL INSTITUTIONS

It is a crucial task to reform the Non-bank financial institutions (NBFI) accounting standard, and to create an integrated information database system. The main objectives were to create a condition to utilize the risk management supervision, to refine the Commission policy based on clarifying and determining the capacity of market.

A. Promoting Public Confidence on the Financial Market

To improve the legal framework for the Non-bank financial institutions activities, we are welcoming recommendations, complaints from the NBFIs Association and professional participants. A task force has been established to make amendment on the Non-bank financial institution activities Law. In this framework, we are aiming to learn from the practices and experiences of similar regulatory bodies and intend to develop amendments to the law.

In order to improve the Non-bank financial institutions off-site supervision and build a capacity and to make it in line with the international standards temporary regulation on currency exchange points and off-site supervision guideline being developed. This year following six guidelines and instructions have been endorsed by the Commission and came into force: a guideline for NBFI record registering, a guideline on monitoring NBFI records, a sample instruction on accounting records and financial reporting of NBFI.

There were 109 NBFIs licensed from the Bank of Mongolia, this year FRC re-licensed them, 10 Limited Liability Companies requested to operate in the NBFIs sector, 17 NBFIs are requested to expand its activities through changes in: paid in capital amount and structure, 7 NBFIs applied to open a branch office, 9 NBFIs applied for change of title.

With the aim of further developing the regulatory policy and to pursue the implementation, we have contacted with the each one of the 86 NBFIs directors which are operating in Ulaanbaatar City and discussed about the regulatory policy decision, NBFIs challenges-difficulties and further development issues

A policy has been focused to support and increase the current asset of NBFIs. In this framework 7 NBFIs are qualified for loans from the “Sustainable livelihood” project which was financed by the World Bank and part of the project was directed towards development of the Microfinance sector.

In collaboration with the Asian Development Bank, “Capacity Building for Financial Sector Reforms” project team had developed an Information Technology database program Blue-Print for the Commission it was the first step toward to build an integrated network system for the NBFIs.

B. Promoting Public Financial Education

In order to make information related to the Non-bank financial institutions activities more transparent for the public and also with the intention of implementing the regulation, the Commission distributed the information by public media Commission’s regulatory policy action information, regulations which are effective, licensed institutions, institutions licenses of which were suspended or revoked were publicly distributed by public media and official website.

Improving and enhancing the financial education for the financial institutions executives and specialists, is an essential factor in this sector’s development, and in sustainable and risk free operation of the sector. 67 NBFIs executives and accountants participated in the training in 2007. The following trainings were organized for the Non-bank financial institutions: financial institutions lending service, market risk management, Non-bank financial institutions prudential ratios, requirement and condition for the licensing of NBFIs and foreign countries practices on anti-money laundering. During the trainings common violations, which were spotted during inspection were openly discussed.

C. Protecting the Legal Rights of Financial Market Participants

Protecting and assuring the legal rights of the customers shall boost the public confidence in the market, leading to further expansion of the market. Even though NBFIs utilize their own assets, to provide a lending service for the public, and they take the risk on their own, trust services, factoring services, and money transfer services present certain risks for the customers. Thus, financial institutions activities shall be transparent for the public. It is necessary to provide timely information for the public in order to protect the customer's legal rights.

Following to the requirement imposed by the Commission NBFIs create a bulletin media board, and disclose their financial reports through public media and some NBFIs already created web-site for their customers.

During the reporting period FRC has inspected and responded to over 450 letters and complaints related with NBFIs.

We aim to modify and make amendment to the laws and regulations which are conflicting with interests of the market participants as FRC is the State regulatory body that is responsible for the market regulation. We conduct regular review on present laws and regulations.

D. Fighting Against Financial Frauds and Misconduct

In accordance with the Commission integrated supervision plan, 46 Non-bank financial institutions were inspected inline with the special guideline. During course of the supervision we have identified a number violation of both regulation and law on the Non-bank financial institutions and other relevant legislative acts. Following are the common violations we have found:

- Legal entities engaging in some activities of the Non-bank financial institutions without the Commission's authorization.
- Non-bank financial institutions reflecting in financial statements changes in the amount of the structure of the capital of capital without prior notification to FRC.
- Not conforming with the accounting standards, financial statements weren't consistent, errors on the balance sheet.
- Opening a branch office /representative office/ without the Commission's permission.
- Breaching of the institutional charter, due to the failure operate internal audit unit and lending committees in a proper manner.

- Not regularly reporting the changes of the company charter and change of the state registration certificate.

While we were conducting inspection of Non-bank financial institutions 6.03 million MNT administrative fines were imposed for the NBFIs. In order to reduce violations of this sort we have given out recommendations and advices as well as State Inspectors prompt corrective action official letters sent out. Course of the inspection these is an indication shows that violations have been reduced significantly since we have conducted the above mentioned actions.

In the reporting year, we have received the financial statement every quarter, conducted prudential ratio analysis and given out detailed assignments and recommendations.

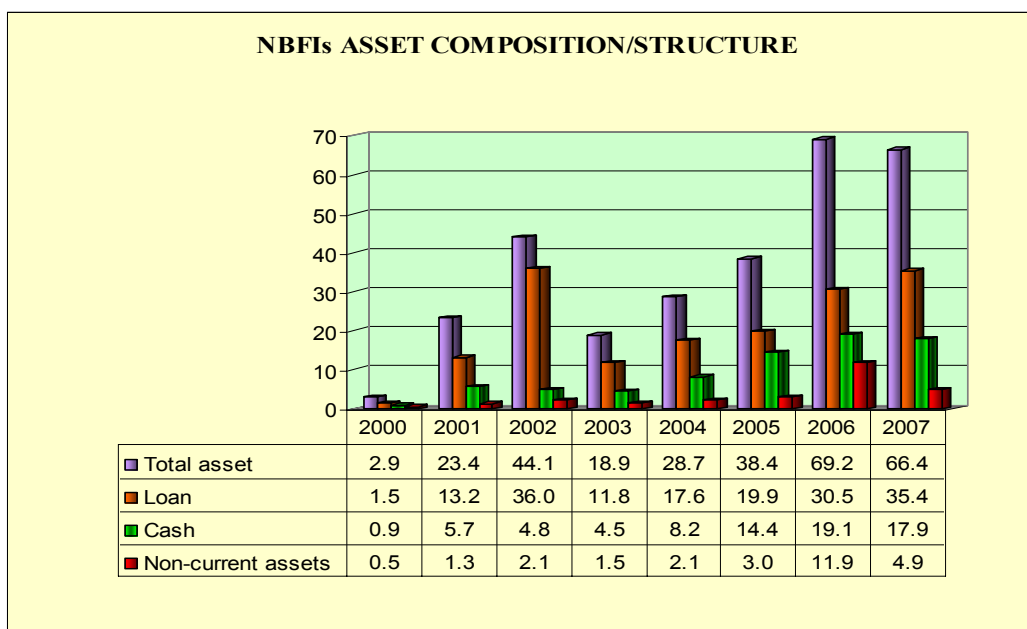
Consolidation and analysis of financial statements is a main way to implement the Off-Site supervision. Furthermore, it's important to gather statistical information identify the scope of the service and defining the accessibility of the service shall play great role for further development trend. In course of the Off-Site supervision, licenses of 14 NBFIs have been suspended and 12 licenses were revoked, which have breached Non-bank financial institutions laws and regulations.

E. The Current Situation of the Market

Currently, there are 137 licensed Non-bank financial institutions in the market. Out of 137 Non-bank financial institutions 112 of them operate in Ulaanbaatar City, 25 Non-bank financial institutions operate in rural area. 14 NBFIs were supported with full or partial foreign investment from Japan, UK, China, Korea and Italy.

There are 43 branch offices of the NBFIs, 433 shareholders, and 647 employees sector wide. Moreover, NBFIs provided financial service to in aggregate number 72.900 customers.

1. Total assets

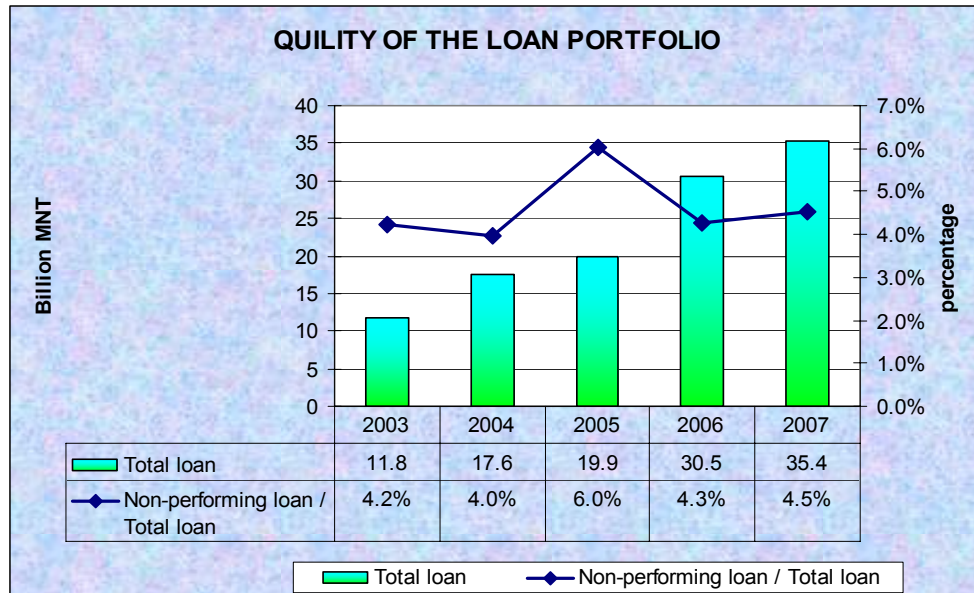


NBFIs total assets has reached 66.4 billion MNT, it takes 2.0 percent of banking sector total assets and equals to 1.5 percent Mongolian Gross Domestic Product.

As a result of increasing the minimum capital requirement of the NBFIs in 2006 total assets grew by 80 percent, but in 2007 NBFIs failed to meet minimum capital requirements, and their activities were terminated. Therefore, total assets decreased by 4 percent down to 66.4 billion MNT. Nevertheless, number of legal entities who want to engage in the NBFIs activities has increased sharply.

In average 57.6 of total assets are composed by lending, 26.2 percent by cash, 9.3 percent by non-current assets.

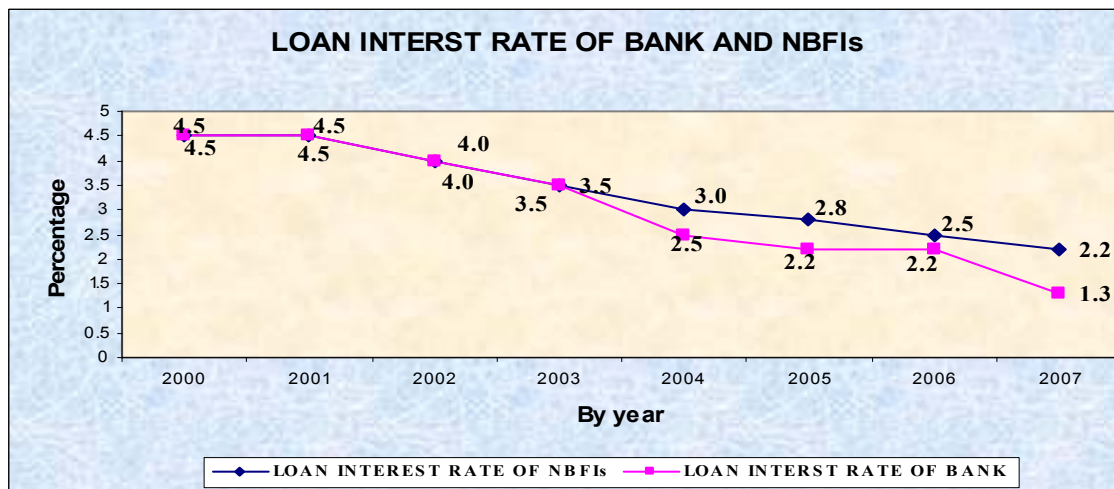
2. Loan portfolio quality



In total lending volume of non-performing loan has decreased from 6 percent to 4.3 percent in 2005 through 2006, but in 2007 it has increased by 0.2 percent, 4.5 percent and non performing loan outstanding increased by 23 percent or 288 million MNT.

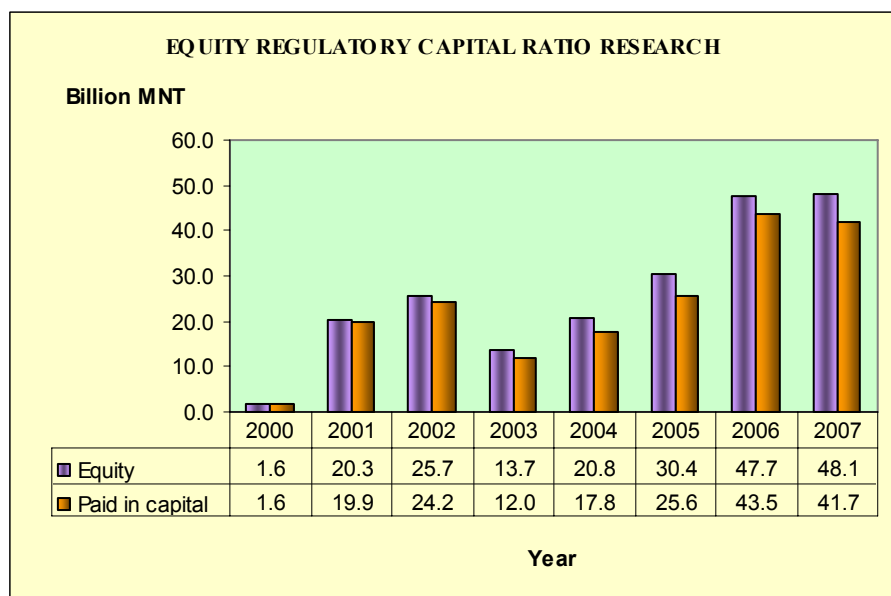
NBFIs have created risk fund worth 1.3 billion MNT which equals to 81 percent of the non performing loans.

3. Loan interest rate



In the recent years, due to banking competition increased among financial institutions, loan interest rate has been decreasing substantially. In 2007, NBFIs monthly average interest rate turned into 2.2 percent, which show 2 times decreased compared to 2000-2001 level.

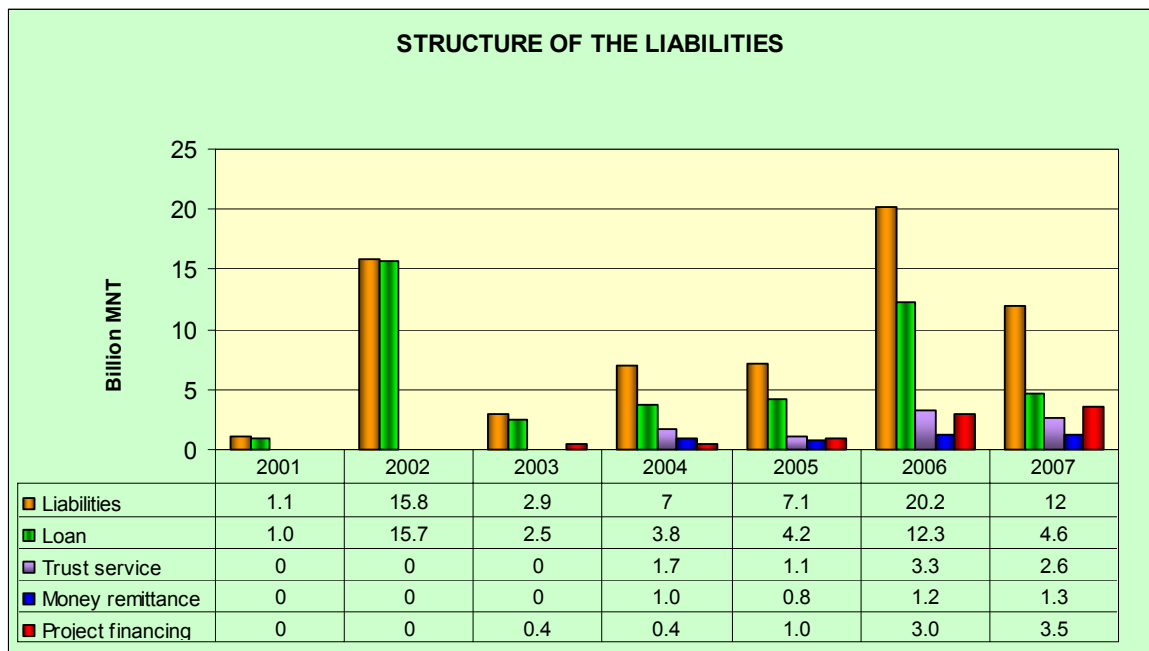
4. Equity and minimum capital requirement



Total quality of the NBFIs has reached to 48.1 billion MNT which equals to 12.8 percent of the banking sector equity.

In relation to increasing the minimum capital requirement of the NBFIs, equity increased by 56.9 percent in 2006. But in 2007 the FRC has made to decision to cancel activities, 36 NBFIs activities, still if we compare with the last year it has increased by 0.84 percent. Paid in capital decreased by 4.14 percent. 86.7 percent of equity is composed by paid in capital.

5. Liabilities



Non-bank financial institutions activities were based on the bank loans, starting from 2004 NBFIs have introduced new services like financial trust service and money remittance, also NBFIs have increased its funding by participating in bulk loan projects which were implemented by international cooperation agencies and donor institutions.

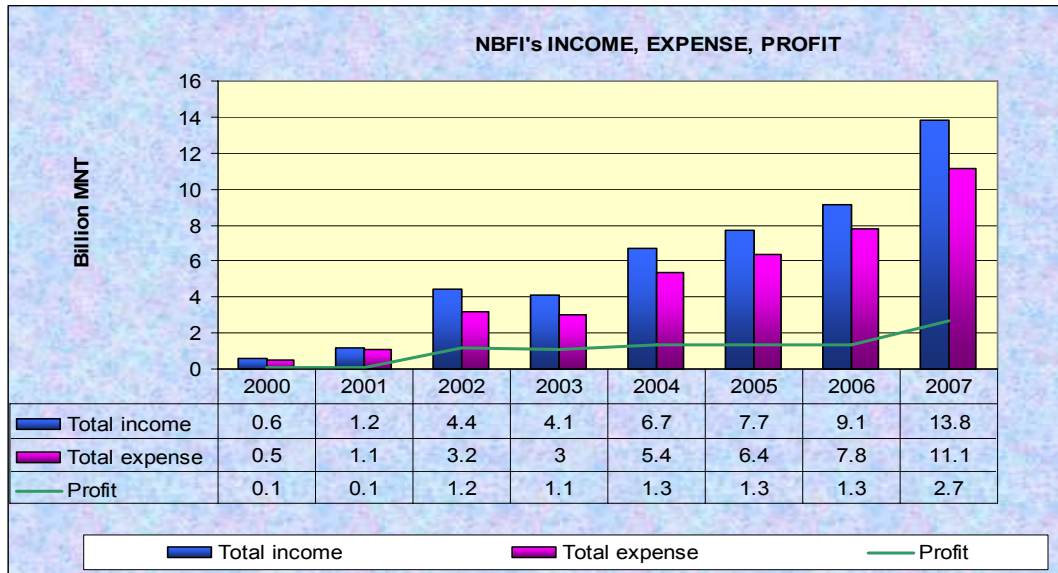
In 2007 total liabilities of the NBFIs was decreased by 41 percent or 7.8 billion MNT which was caused by the NBFIs had to reimburse its bank loans at interest rate by 0.5-2.0 percent.

NBFIs financial trust service resources do not differ from the deposit service, thus in order to prevent from potential risk and protect the stability of the financial sector, it is essential to create appropriate regulatory legal environment.

6. Profitability

NBFI' industry average return on asset is 4.6 percent; average return on equity is 6.1 percent, which is compared with banking sector indicator return on asset nearly 2 times higher, return on equity is relatively lower. The reason for low return on equity and can be explained by the fact that NBFIs are not able to fully utilize financial leverage, on the other hand cost of financing operation costs are high.

In the past years, NBFIs lending activities has expanded therefore interest rate return sustainably increased, land just in 2007 it increased by 52 percent or 4.7 billion MNT reliability 13.8 billion MNT. But total expenditure has increased by 42 percent and it has reached 11.1 billion MNT.



F. The Further Implementation of the Policy Measures

Although Non-bank financial institutions are the one of the main component of financial sector, the legal environment of this sector is not well developed; staff is inexperienced and have limited knowledge regarding the financial management. Since there are inadequate assets, it becomes difficult to attract enough costumers in the sector. Moreover, there is lack of motivation to compete with each other in the market. Thus, following policy measures need to taken immediately:

- Define mid-term strategies for the microfinance market and gain knowledge from foreign country experiences.
- Pass a range of necessary laws and regulations related with Non-bank financial institutions activities, formulate a regulation on the activities of NBFIs and ensure enforcement.
- In the framework of improving the legal environment of this sector, support the new services, products, an amendment should be made to the current laws related with Non-bank financial institutions.
- By improving the financial reporting standard it is necessary to introduce a risk management system.
- Strengthen the quality of the off-site supervision and accounting standards
- Support the capacity and quality of the NBFIs activities by promoting, NBFIs merge, to become larger.
- Promote an appropriate Corporate Governance for the NBFIs
- In the framework of the Government liaison or international institutions project, increase the loan accessibility for the NBFIs

- Create an integrated information database network for the sector.

4. SAVINGS AND CREDIT COOPERATIVES

The objective of the year 2007 was to regain public trust confidence in the sector. We just get over SCC related social crisis, and it is an essential task to improve legal environment of this sector, intensify the regulation and supervision, and to strengthen licensing requirement.

A. Promoting Public Confidence on the Financial Market

Savings and Credit Cooperatives is a financial activity thus it should be regulated by an independent Law on Savings and Credit Cooperatives rather than a general law on Cooperatives. The SCC law draft has been submitted to Parliament of Mongolia. Savings and Credit Cooperatives further development path will be defined clear after passage of this draft law.

In order to intensify the SCCs activities of the supervision, and to improve the financial capacity of the SCCs following regulations were amended to comply with “Savings and Credit Cooperatives activities prudential ratio regulation”, “SCCs financial solvency regulation” “On-Site supervision regulation”.

In the reporting year, 129 Savings and Credit Cooperatives have been licensed and 1 SCCs failed to meet the Commission’s requirement thus its license was suspended.

The attention mainly has been directed to lowering savings interest rate and to sustain financial stability. Regarding for the market regulation SCCs savings interest rate has been averaged to in line with banks and Non-bank financial institutions.

In order to implement the provisions of the “Saving and Credit Cooperatives Law, which was passed by Parliament of Mongolia June 2007 in this framework 468 Savings and Credit Cooperatives did not submit its request for the Commission. / Ulaanbaatar city -309, local 159/ and preparation work has been completed to withdraw its licenses.

B. Promoting Public Financial Education

Lack of public knowledge regarding exercise of joint control over financial institutions, and its implementation also lack of information had played significant role

for the crisis of the Savings and Credit Cooperatives, therefore this year we aimed to achieve timely distribute of information to public.

The Commission's policy implementation on the Savings and Credit cooperatives activities; supervision result, information regarding licensing of SCCs have been reported regularly on following media : "Zuunii news", "Daily news", "Morning news", "C-1" TV Mongolian National Television and SBN.

The Commission organized a Capital Market Development open fair, during the fair we have distributed hand outs and brochures relating with SCC regulation and ownerships right for deposit holders.

Improving and enhancing the financial market participant's education shall play important role its market stabilization process, especially of the SCCs directors and executive employees; therefore we have conducted following trainings and seminars:

In collaboration with the Asian and Mongolian Savings and Credit Cooperatives organized the 3 days trainings "Savings and Credit Cooperatives Management Instruments" for the employees at FRC and SCC, which gave overview of , up coming challenges, further directions "Savings and Credit Cooperatives development history", it also has strengthen the international cooperation.

In collaboration with the XAC bank we have conducted following trainings in Zavkhan, Arkhangai, Dund-Gobi, and Orkhon, Dornogobi provinces for the Savings and Credit Cooperatives which have a franchise contract with the XAC bank: "Loan risk assessment", "Legal environment for conducting Savings and Credit Cooperatives activities", 180 participants participated in the training, We concluded that citizen have received good information regarding the "Savings and Credit Cooperatives characteristics", special features of its the activities, members rights for the cooperatives, internal democracy, "financial capacity", about how to improve discipline.

Besides training and seminars the Commission has given numerous valuable recommendations and advices for the Savings and Credit cooperatives management and members how to improve internal supervision, and reporting. We concluded it has significant assistant for the Savings and Credit Cooperatives activities.

In the reporting year, Savings and Credit Cooperatives Department specialists have given professional legal advices to 336 legal entities, /aggregate number/ 600 citizens.

C. Protecting the Legal Rights of Financial Market Participants

In order to protect the interest of the Savings and Credit Cooperatives deposit holders from potential illegal activities we collaborated with the relevant institutions and paid special attention towards prevention. With the aim of restoring market confidence citizens, and in order to regaining trust, attention was paid to reducing the bureaucracy and improving efficiency of public authorities.

187 complaints from deposit holders who were not able to get their money back from the Savings and Credit Cooperatives was reviewed in, 26 complaints with potential criminal implication were transferred to the State Investigation Department.

The Commission has paid constant attention to 6 Savings and credit cooperatives which were in financial difficulties and cause damages for its members. In order to clarify the problems the Commission has ordered following assignments:

In course of the operational supervision and during process of reviewing licensing, complaint also we have double checked distribution of financial statement for deposit holders. Result of the requirement Savings and Credit Cooperatives starting to get into habit of operating relevant laws and regulation on the advertisement board, distributing the Commission's brochures, and to introduce Commission's inspection report for its members.

D. Fighting Against Financial Frauds and Misconduct

There is an indication shows that Savings and cooperatives' management operates in the framework of the Law, the deposit holders starting to strengthen its internal supervision. There is positive improvement and changes in the sector, but Savings and Credit Cooperatives crisis not over yet. The Commission continues to strengthen the supervision and had taken action towards enforcing and satisfying the license requirement condition.

In the reporting year, accordance of the Commission's consolidated supervision schedule for the Savings and Credit Cooperatives in 2007 we have conducted 8 inspections over 64 Savings and Credit Cooperatives, and based on public information, public information and complaints we have also conducted a supervision over 15 Savings and credit cooperatives which weren't included in the schedule.

Results of the inspection following violations were common:

- Cooperative's governance not well defined therefore, governors, supervisory board, loan committee did not comply with the relevant laws, executive directors did not have work contract

Internal supervision mechanism not formed or lack of activity, members meeting not organized accordance of the law, accurate information not provided regarding the members, not following accounting standards, attracting funds from non-member depositors, lending to non-members, and supervision over loan repayment not sufficient.

- Failed to meet the capital adequacy requirement, not submitting data and reports to the Commission, and make error on the report, lack of culture on the contacting with the State regulatory institutions,

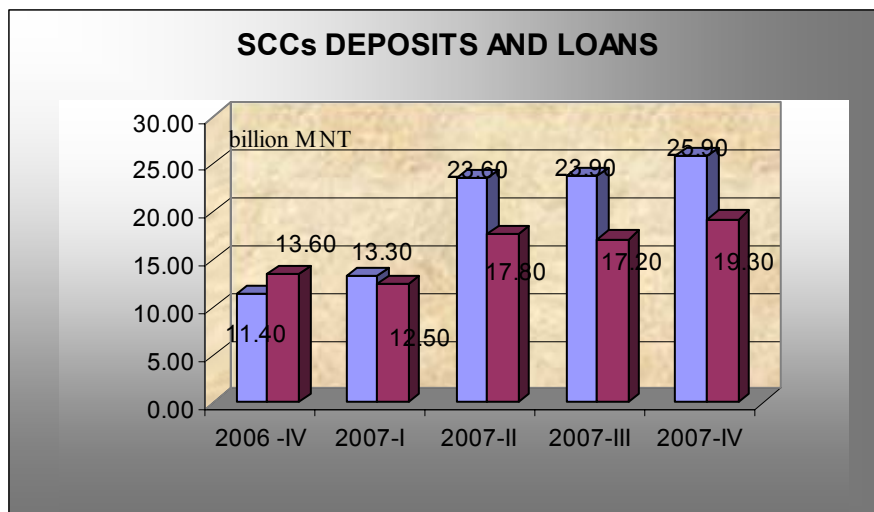
Based on the supervision, 5 cooperatives which were violated the laws and regulation were fined by 460000 MNT, 24 cooperatives have received prompt corrective action official letter which were assigned to improve its activities, paid constant close attention over the its implementation, these cooperatives which have caused a damages of the consumers interest, 5 cooperatives which were not giving back the costumers savings accordance of the contract period and it was considered as criminal case therefore it has transferred to the State Investigation department for further investigation.

Savings and Credit Cooperatives financial report, prudential ratio report, have been received quarterly and analyzed. In order to prevent from the future possible risk, we conduced research and given out numerous advices and recommendations.

E. The Current Situation of the Market

At the end of 2007, 100 out all licensed Savings and Credit Cooperatives operated Ulaanbaatar city and 81 in local region. 21 percent or 38 SCCs are under the XAC bank franchise service, and operate in the local region.

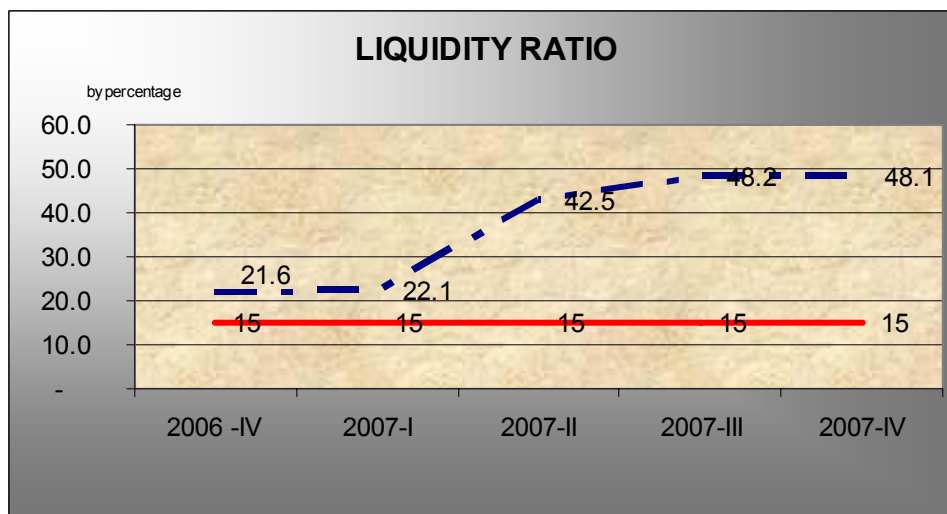
1. Deposit and loan



At the end of 2007, deposit savings amount to 25.9 billion MNT, which is 2.3 times higher than compared to previous year, outstanding loans 19.3 billion MNT which constitutes 18.4 percent increase, compared to 2006.

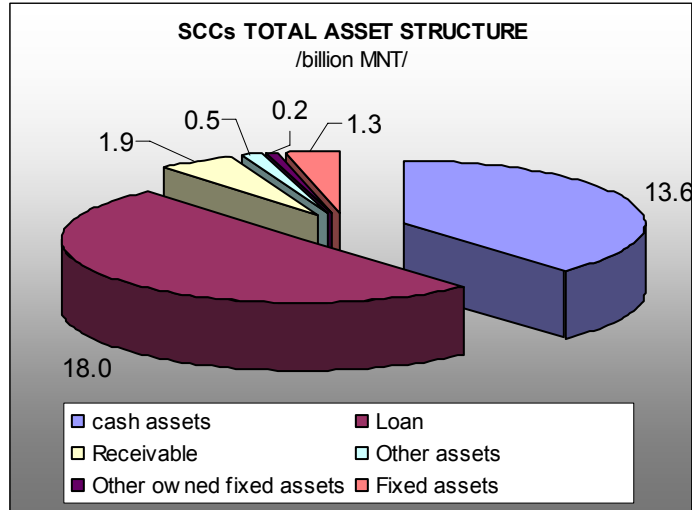
74.5 percent of the deposits were utilized for lending 25.5 percent placed as cash in hand or in other institutions.

2. Savings and credit cooperatives liquidity ratio capacity



The benchmark of liquidity ratio of cooperatives /liquid assets divided by short term loans from others/ is above 15 percent. Thus, the performance indicates that it is higher than prudential ratio requirement by 33.1 percent which shows that repayment capacity has increased.

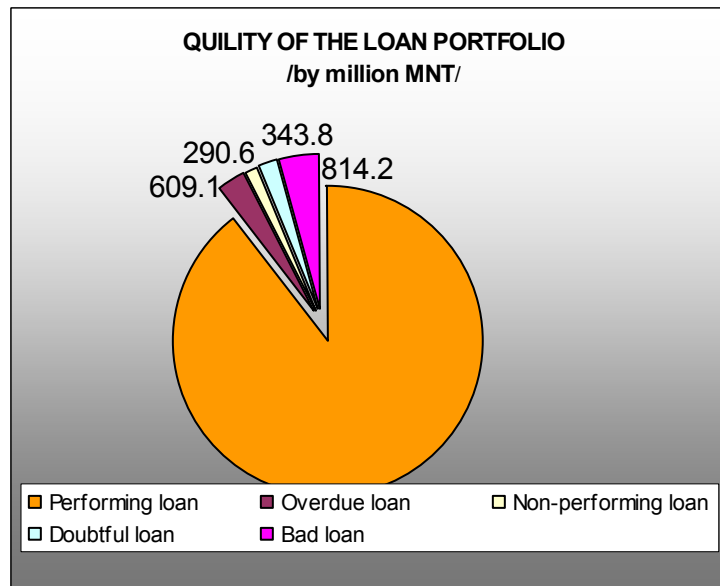
3. Savings and credit cooperatives assets structure



SCCs total assets have reached 35 billion MNT, at the end of 2007, stating 44.5 percent increase compared to 2006. 38 percent of total assets were composed by in cash 51.4 percent by loans, 5.4 percent by receivable or 0.7 percent by other assets, and 3.7 percent fixed assets.

It indicates that, asset generating revenue has increased by 61.2 percent to 18 billion MNT, reaching 85 percent of this good profit trend. In the reporting year, Savings and Credit Cooperatives are running at a loss 1.85 billions MNT and 1.9 billion MNT of accumulated profit, so SCC whole, system SCC has made profit over 50 million MNT.

4. Quality of the savings and credit cooperatives loans

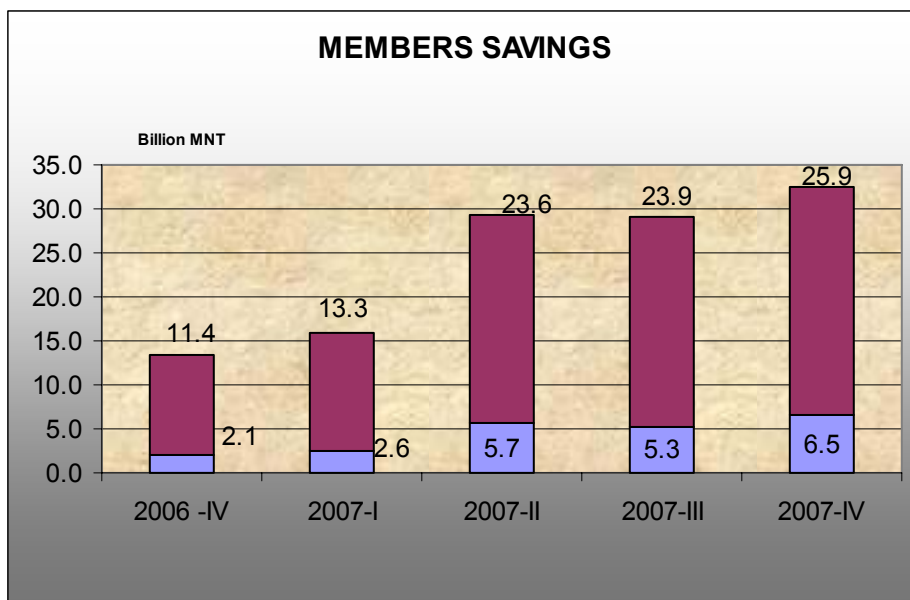


Total lending of the SCCs is 19.3 billion MNT, compared to previous year it has increased by 5.7 billion MNT, but total loans non-performing loans increased by 1.3 percent and reached 2.1 billion MNT. 1.2 billion MNT risk reserve fund has been created for the SCC loan portfolio.

5. Savings and credit cooperatives liabilities and shared capital

At the end of 2006, Savings and credit cooperatives liabilities, shared capital ratio was 18.4 percent, but in the reporting year it has reached to 25 percent. This indicates that cooperatives tend to raise funds from members deposits. Once again, it shows that possibility of financial risk higher in the sector.

Members total deposit amount accounts for 74 percent and the prudential ratio norm is 70 percent.



6. Future policy implementation

Contribution of microfinance institutions in the financial market is increasing, and accessibility of microfinance loans are broadening. For that reason, we ought to define SCC development tendencies and to create a legal environment which best suits the current situation of the market.

First of all, the FRC needs to implement the following specific tasks as a priority.

- Learn and study from international best practices, develop a local model.
- Create central database for the Savings and credit cooperate, and start data consolidation.

- Expand activities of the microfinance service in rural areas and provide policy support.
- Create a mechanism to involve SCCs in the insurance market service
- Savings and Credit Cooperatives accounting standard shall be improved in line with international standard, accurate financial reporting information.

THREE. FINANCIAL PERFORMANCE

Financial operations of the FRC were focused to spend budget resources as prescribed to run steady operation of the Commission Office, to expand international relations, to upgrade facilities and working environment, to improve staff social welfare, and to disseminate public about its operation.

The State Great Hural (Parliament) of Mongolia endorsed budget of the FRC at 541.4 million MNT of which 381.4 million MNT was planned to be funded from state budget, 160.0 million MNT to be generated from its operational revenue. In addition, 30 million MNT was granted from the Mongolian Development fund to improve housing conditions of the FRC staff.

Income

The FRC received 357.9 million MNT from the State Budget, raised 151.6 million MNT to the State Budget from its operations. In addition total income of 486.0 million MNT was made from its main activities while carrying out the functions, of which 96.8% of income was formed from regulatory fee, and the rest 3.2% were from other resources.

Expenditure

351.1 million MNT was spent to salary and social security expenditures, while 170.3 million MNT was spent for the products and services out of allocated 521.4 million MNT budget. The FRC regularly and timely reported Commission's 13.9 million MNT budget expenditure to the State Fund, were saved.

Savings from expenditure lines such as transportations, fuel, overseas and domestic business trips, trainings and internships, disseminations and advertisements, and the fee and commission charge 0.4 - 4.4 million MNT was transferred to cover overspent budget lines.

Here, some expenditure which are exceeded:

- Stationery expenditure was exceeded with around 1 million MNT which was caused by increased costs related to integration of the regulatory bodies' accounting and financial reports, following off-site supervision feedback;
- Post and telecommunication cost surpassed by 1.9 million MNT which caused by the transfer and installation of the cables and etc. as a result to change the office twice.
- Regarding the implementation of the decision from the State Great Hural (Parliament) to increase the number of employees, the expenditure of purchasing and installing furniture, technical and internet devices were surpassed by 2.6 million MNT than initially planned.

There were no payables and receivables recorded in its operation in 2007.

Assets

Total assets of the FRC is increased by 162.1 million MNT

- Following the decision of the Government of Mongolia and State Property Committee, the Government House 4 building annex was transferred to the FRC's use, and in relation with this, private investment 52.6 million MNT which was previously put in to this building annex was reimbursed back to the investors by the FRC and the asset is recorded to Commission Offices' balance sheet;
- The FRC purchased "Land Cruiser 105" for 56.8 million MNT in order to enhance access of the FRC services in rural area; and,
- Purchased facilities and technical devices worth 32.1 million MNT, furniture and other movable property for 20.6 million MNT

According to the decision of the General Manager and Head of Office based on "Law on Civil Service" and "Internal Rule for Operation of the Commission Office", 30 million MNT which was allocated from Mongolian Development Fund was spent to improve housing condition of employees.

/attached "Financial Statements of the FRC in 2007"/

The Commission in 2008

- By consolidating and analyzing the accomplishments in the scope of "Capital Market Development Year", it can be said that although tasks that planned were not fully accomplished, it is considered that good development trend has been determined, and first steps has been taken towards the reform. In order to proceed this practice to dedicate "the current year" to implement something beneficial that were stated in Commission Strategic Plan, the FRC announced 2008 as "Micro Finance Market Development Year". In relation with this, according to

the plan some actions are planned to be particularly taken on non bank financial institutions market, savings and credit cooperatives and insurance market, and some tangible conclusions are expected from these actions.

- Will consider high significance and shows best endeavor to carrying out issues and duties which are stated in Main Guideline for socio-economic development of Mongolia, Government Action Plan, and a Performance Agreement signed between General Budget Administrator, the Chairman of the Commission and the General Manager (and the Head of Office) in their designated time frame.
- Direct legal and other regulatory actions to improve financial market professional participants' ethics, responsibility, and discipline by strengthening the requirements, and develop and secure compliance of the risk management methodology for the State remote supervision system.
- Improve efficiency of the organization of the Commission Office, reduce enhance working condition, build capacity of professional human resource, seek for opportunities to standardize operations, and start to build "Financial Education and Information Center" of the Commission.

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