Journal of Financial Crises

Volume 3 | Issue 2

2021

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Recommended Citation
Fulmer, Sean (2021) "Mongolian Asset Recovery Agency," *Journal of Financial Crises*: Vol. 3 : Iss. 2, 320-329.
Available at: https://elischolar.library.yale.edu/journal-of-financial-crises/vol3/iss2/16

Mongolian Asset Recovery Agency[1]

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Yale Program on Financial Stability Case Study
June 23, 2021

Abstract

Mongolia's transition away from the monobank system in the 1990s did not occur smoothly, with inherited, non-performing loans from the monobank period causing significant instability and insolvency in the banking sector. These inherited portfolios, in conjunction with risky lending by the newly formed banking sector, led to the insolvency of People's Bank (also known as Ardyn Bank), and Insurance Bank, which together held approximately 35% of total assets in the banking system. From 1996 to 1997, the Mongolian government, with the technical and financial support of the World Bank and the Asian Development Bank, formed the Mongolian Asset Recovery Agency (MARA) to remove nonperforming loans from the banking sector as well as to liquidate the People's and Insurance Banks. MARA attempted to achieve this through the purchase of nonperforming loans in exchange for interest-bearing government bonds. MARA's stated goal was to recover 90% of the nonperforming loans, as well as to create a more normalized financial culture of fulfilling contractual debt obligations. Initially, MARA intended to be functional for a three-year period, but further insolvency crises required MARA to stay open longer than three years. By 2000, MARA had recovered only 14% of the initial $35 million in assets that it seized in 1997 from the two liquidated banks that sparked the need for MARA.

Keywords: Mongolia, asset management companies, asset purchase programs, MARA, nonperforming loans, broad-based asset management

[1] This case study is part of the Yale Program on Financial Stability (YPFS) selection of New Bagehot Project modules considering broad-based asset management company programs.

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Mongolian Asset Recovery Agency (MARA)

At a Glance

In 1991, Mongolia dissolved its pure monobank system, dividing the state-owned bank into six different enterprises including the central bank (Enoch, Gulde, and Hardy 2002). The five major commercial banks that emerged from the monobank system inherited a portfolio of nonperforming loans that had been made to state-owned enterprises when Mongolia had a central economy, which accounted for about 20% of total loans. Beyond the inherited loans, more than half of the new loans made after the transition away from the monobank system were considered "problem loans," as banks continued to loan to loss-making businesses in the hopes of recovering some funds and capitalized interest on nonperforming loans in order to disguise their losses. By the mid-1990s, the five commercial banks in Mongolia accounted for 90% of total banking sector assets (Asian Development Bank 1996). Some of the smaller, minor banks failed and required takeovers by the larger banks in 1994. However, these failures likely did not solely cause the deterioration of the Mongolian banking system, since the small banks made up such an insignificant portion of the system (Enoch, Gulde, and Hardy 2002).

Summary of Key Terms	
Purpose: To hold the nonperforming assets of banks, to attempt to recover as much of them as possible and to "set an example of financial discipline and the enforcement of loan contracts" (Enoch, Gulde, and Hardy 2002).	
Launch dates	Announcement: December 1996 First transfer: January 1997
Wind-down dates	Unknown
Size and type of NPL problem	42.2% of total bank loans A mix of inherited monobank loans and new problem loans
Program size	Not specified at outset
Eligible institutions	Two liquidated commercial banks Closed bank
Usage	Initial plan transferred about $35 million in assets to MARA
Outcomes	About 14% of the initial debt in 1997 was recovered by 2000
Ownership structure	Government agency, then a government department, and finally a state-owned enterprise
Notable features	Mongolian authorities provided MARA with expedited access to the courts

Of the five major banks, only one of them, T&D Bank, managed to reach the liquidity ratio requirement established by the Bank of Mongolia in June of 1996. Of the remaining commercial banks in 1996, the Asian Development Bank (ADB) determined that the financial stability of People's Bank, also known as Ardyn Bank, and Insurance Bank was most in question, as they were insolvent and in blatant violation of prudential regulations. About 57% of loans made by People's Bank were nonperforming, and Insurance Bank maintained just enough reserves for loan losses of less than 4% of its noninherited loan portfolio. The ADB determined that substituting interest-bearing government securities for the inherited nonperforming loans would not fix People's Bank and Insurance Bank, since they faced larger problems than a simple restructuring could handle (Asian Development Bank 1996).

To restore confidence and stability to the banking system, the government of Mongolia, in accordance with advice from the World Bank and the ADB, decided to assume responsibility for the nonperforming loans, while liquidating People's Bank and Insurance Bank. These institutions would not be recapitalized and instead would enter receivership in December 1996, with three separate new institutions emerging from receivership (Asian Development Bank 1996). These institutions were Savings Bank, which handled secure household deposits; Reconstruction Bank, which provided banking services to former business customers and other entities in the failed banks, and the Mongolian Asset Recovery Agency (MARA), which would purchase nonperforming loans from the receiver of the two liquidated banks in return for restructuring bonds. In order for MARA to purchase the nonperforming assets and capitalize the new banks, the government utilized funds from a $35 million Financial Sector Program Loan (FSPL) from the ADB to replace the assets with government securities. The receiver would then transfer the bonds to either the Savings Bank or the Reconstruction Bank. The World Bank stated that the "FSPL will finance the recapitalization of the banking sector" (World Bank 1997).

The Mongolian government established MARA as a government agency under the auspices of the Ministry of Finance, rather than as an incorporated public enterprise to project governmental authority (Enoch, Gulde, and Hardy 2002). The government initially intended for MARA to exist for three years and recover 90% of the nonperforming assets transferred to them within that time period (World Bank 1997). Despite this stated optimism, other analysis of the program did not expect MARA to recover much from the nonperforming assets since many of the borrowing enterprises no longer existed (Enoch, Gulde, and Hardy 2002).

Of the $35 million in liquidated assets seized by MARA in 1997, the World Bank estimated that MARA recovered about 14% of it after three years (World Bank 2002). However, an IMF analysis of MARA concluded that the overall recovery rate was closer to 17% (Enoch, Gulde, and Hardy 2002).

Summary Evaluation

There has not been much evaluation of MARA, but a 2000 report from the World Bank indicates that MARA's "ability to recover nonperforming assets is hampered by its insufficient authority, lack of funding, low salaries, and lengthy court delays" (World Bank 2000).

Mongolian Asset Recovery Agency: Mongolia Context	
GDP (SAAR, Nominal GDP in LCU converted to USD)	$1.346 billion in 1996 $1.181 billion in 1997
GDP per capita (SAAR, Nominal GDP in LCU converted to USD)	$580.91 in 1996 $505.59 in 1997
Sovereign credit rating (5-year senior debt)	Data not available for 1996 Data not available for 1997
Size of banking system	Data not available for 1996 Data not available for 1997
Size of banking system as a percentage of GDP	Data not available for 1996 Data not available for 1997
Size of banking system as a percentage of financial system	Data not available for 1996 Data not available for 1997
5-bank concentration of banking system	90% of total banking assets in 1996
Foreign involvement in banking system	Data not available for 1996 Data not available for 1997
Government ownership of banking system	Data not available for 1996 Data not available for 1997
Existence of deposit insurance	No deposit insurance system established in Mongolia at this time
Sources: Bloomberg; World Bank Global Financial Development Database; World Bank Deposit Insurance Dataset; Asian Development Bank 1996.	

Key Design Decisions

1. Part of a package: Mongolia established MARA along with two other institutions, Savings Bank and Reconstruction Bank, to stabilize the banking system after the liquidation of two banks that accounted for almost half of the system.

Following the liquidation of People's and Insurance Banks, the government created three institutions: MARA (for nonperforming assets), Savings Bank (which could only invest in safe assets and hold household deposits), and Reconstruction Bank (which could only provide banking services to businesses with deposits in the failed banks). The government issued government bonds to Savings Bank and Reconstruction Bank to replace the bad assets and contribute to their initial capital. The Asian Development Bank (ADB) provided a $35 million Financial Sector Program Loan (FSPL) to capitalize the new banks (World Bank 1997).

2. Legal authority: The Speaker's Decree No. 104 of December 11, 1996, liquidated the People's and Insurance Banks, while the Ministry of Finance and Economy (MOFE) Order No. 17 on January 11, 1997, established MARA.

The government decrees and orders establishing MARA do not appear to be available digitally. The government developed the plan for the creation and activities of MARA in conjunction with the Asian Development Bank (Asian Development Bank 1996). Additionally, the Law of Mongolia on Banking, passed in 1996, established the process through which receivership would occur.[3] The law allowed the Bank of Mongolia to pursue receivership if the appointment of a conservator had failed to regulate the behavior of the bank or if the bank had become insolvent (Parliament of Mongolia 1996). The law required the receiver to arrange for the assets of the bank to be assumed by others, while ensuring that depositors received first priority among creditors (Parliament of Mongolia 1996).

3. Special powers: Mongolian authorities provided MARA with expedited access to the courts.

MARA technically received "expedited access to the courts, having its cases heard by judges who are specialists in this field of law" (World Bank 1997). However, the courts and individual judges did not typically understand the legitimacy of MARA to claim nonperforming assets on behalf of the Ministry of Finance. Judges also had a weak understanding of these transactions in general, since the two-tier banking system had existed for only seven years since the breakup of the monobank system (Bold Magvan, email message to author, March 14, 2021).[4]

[3] Unofficial English translation of this law by Lehman Law can be found at http://lehmanlaw.mn/wp-content/uploads/2016/04/Banking1996.pdf.
[4] Bold Magvan was the Deputy Governor of the Bank of Mongolia from 1996-2000.

4. Mandate: MARA's mandate was to minimize losses and utilize the Mongolian legal system to pursue delinquent borrowers in order to normalize contractual obligations.

While MARA initially set out with a defined goal of recovering 90% of assets transferred to it in the first three years, this was not the sole mandate of MARA (World Bank 1997). According to an IMF Research Paper, the goal of MARA was "not only to minimize the cost of the bank restructuring operation, but also to set an example of financial discipline and the enforcement of loan contracts." MARA attempted to rebuild confidence in the banking sector through the litigation of defaulting borrowers through the legal system of Mongolia (Enoch, Gulde, and Hardy 2002). The agency also attempted to actively restructure delinquent enterprises, but achieved little success due to the limited capacity of MARA and the politicization of its activities.

5. Ownership structure: MARA initially began as a government agency, but later became a department within the Ministry of Finance and Economy and then a state-owned enterprise.

Initially, officials had proposed to make MARA an incorporated public enterprise because that structure would allow the asset management agency to maintain a nonpolitical categorization. Additionally, MARA hired staff from the liquidated banks with performance-based contracts, which would assimilate easier into a public enterprise. However, Mongolian authorities created MARA as a government agency, since they desired MARA to carry governmental standing in order to provide stability to the banking sector (Enoch, Gulde, and Hardy 2002).

In 2000, MARA transitioned into the "Asset Recovery Department" within the Ministry of Finance (KDI and KOICA 2004). In 2002, Government Resolution 109 transformed MARA from a government agency into a state-owned enterprise (Minister of Finance and Economy 2002).

6. Governance/administration: MARA functioned under the Ministry of Finance and Economy.

There is no further publicly available information on the internal organizational structure of MARA, nor annual reports or audits.

7. Size: There did not appear to be a set cap on the size of MARA.

The government initially provided 21 billion Mongolian tugriks ($29.4 million) in government bonds to MARA at its creation to cover the nonperforming assets of the failed banks (World Bank 1997).

8. Funding sources: MARA acquired assets from the receiver of the two liquidated banks in return for interest-bearing government bonds using funds from the ADB.

The ADB provided a $35 million FSPL to Mongolia to finance the banking sector restructuring (World Bank 1997). The receiver sold all of the assets of the liquidated banks to MARA in return for interest-bearing government restructuring bonds, which MARA financed with the FSPL funds. The receiver then transfered the deposits of the liquidating banks, as well as the restructuring bonds, to the Savings and Restructuring Banks. Finally, MARA sold "liquid and fixed assets and performing loans" to the other two successor institutions against cash and bonds (Asian Development Bank 1996).[5]

The restructuring bonds were issued with a maturity of one month, with government assurances that they would be rolled over continuously. The interest rate on the bonds was slightly higher than the interest rate set by the Bank of Mongolia, which hovered around 4% for 1997. The bonds were nonnegotiable and available only to banks (Enoch, Gulde, and Hardy 2002).

9. Eligible institutions: MARA purchased assets from liquidated banks that the government was in the process of restructuring.

While MARA was created as a direct response to the insolvency and liquidation of the People's and Insurance Banks, its activities were not limited to just those institutions. MARA later took on the following failed banks: Reconstruction Bank (which was created alongside MARA), HOTSH Bank and Central Asia Bank (KDI and KOICA 2004).[6] It is unclear if MARA followed a set criteria for eligible institutions, whether private or public.

10. Eligible Assets: MARA assumed all of the non-performing assets of the two failed banks.

MARA did not seem to place a restriction on which assets could be obtained. About 70% of the non-performing assets assumed by MARA in 1997 were small to medium sized loans to individuals. The other 30% of assets were defaulted loans to enterprises for large investment projects, which the World Bank cites as requiring "extensive loan workout" (World Bank 1997).

11. Acquisition mechanics: The People's and Insurance Banks were forcibly liquidated and their assets seized by the government.

While the two failed banks were closed without warning; there is no documentation for how the directed and inherited loans in the nonliquidated commercial banks were taken

[5] Some references state that the government assumed responsibility for all of the inherited and directed loans in the banking system, including those in institutions not being liquidated (World Bank 1997). However, it is not clear if those loans were placed into MARA or simple assumed by the government.
[6] It is not clear if Mongolia considered the bankruptcies of these banks to be the result of the same crisis that necessitated the creation of MARA.

over by MARA.[7] However, an IMF research paper states that the government accepted responsibility for these loans and acquiesced to swapping bonds for the directed and inherited loans, which amounted to about $11 million by the end of 1996 (Enoch, Gulde, and Hardy 2002).

12. Acquisition pricing: It is uncertain how MARA and the Mongolian government priced the non-performing assets.

There is no information available on specific pricing strategies used to assess and assume the nonperforming assets.

13. Recovery and disposal: MARA planned to utilize several strategies to recover loans, which the agency intended to establish financial discipline and not simply minimize losses.

The stated goal of MARA was to maximize recovery of the nonperforming loans received from the failed banks. This goal included providing financial discipline and normalizing loan contract enforcement within the Mongolian financial system, rather than simply minimizing losses. MARA could utilize the following techniques for recovering loans: "netting loans against deposits, renegotiating loans, seizing collateral, and initiating bankruptcy proceedings" (Enoch, Gulde, and Hardy 2002). MARA never implemented its ability to initiate bankruptcy proceedings.

According to a World Bank report from 1997, MARA intended to create a "Bulk Sales Program," in which moderate-size loans would be packaged together and sold to individual investors rather than commercial banks at a significant discount. About 70% of the nonperforming assets assumed by MARA in 1997 were from small to medium-size loans to individuals, which made the Bulk Sales Program more attractive than individual sales. After the completion of the Bulk Sales Program, MARA intended to seek to delegate the remainder of the loan recovery efforts to commercial banks, through the creation of a secondary market created by the government (World Bank 1997). This secondary market was never created, and it is unclear if the Bulk Sales program ever materialized.

As a state-owned enterprise in 2002, MARA was allowed to sell recovered assets at a discount, through an auction process (World Bank 2005).

14. Timeframe: MARA initially had a definite timeframe of three years, but further banking failures necessitated an extension.

An initial report on the Mongolian banking sector restructuring stated that MARA had a three-year lifespan when created, with the hopes of transitioning debt recovery duties to commercial banks (World Bank 1997). However, the creation of MARA did not result in a

[7] The closing of the failed banks required 900 agents to simultaneously enter 100 branches at the close of business on Friday, December 13, 1996, to prevent any destruction of records. On Monday, the branches of the People's Bank reopened as the Savings Bank, while Insurance Bank became the Reconstruction Bank (Enoch, Gulde, and Hardy 2002).

fully healthy and stable banking system, as other banks began to fail. This development was expected at the time, since the Mongolian government did not have the funds available to liquidate all of the insolvent banks at once. This included the Reconstruction Bank, which was intended to facilitate enterprise deposits originally in the People's and Insurance Banks (KDI and KOICA 2004). As a result of this, MARA existed in its various forms until at least 2005 (World Bank 2005).

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