THE BANK OF MONGOLIA

ANNUAL REPORT 2021

FOREWORD

In 2021, Mongolia's economic activity and financial sector has recovered and successfully overcome major challenges. In spite of the COVID-19 pandemic, the economy contracted 5.3 percent in 2020, however, in 2021, it has expanded by 1.2 percent. The main reason for this economic recovery, lower interest rates and increased lending can be explained by the implementation of fiscal and monetary policy measures through the banking sector. The banking sector loan growth increased by 21.3 percent, the average interest rate on new togrog loans reached 14.3 percent, which is a 2% decrease compared to the previous year's. Despite the delays in coal exports due to the border constraints induced by the COVID-19 pandemic, the togrog's exchange rate remained stable throughout the year, and international reserves remained relatively stable at adequate levels.

The reform of the banking sector continues successfully, and the amendments to the Banking Law were approved on January 28, 2021 by the parliament. As a result, changes have been made for banks to become publicly traded companies, to create a balance of ownership, management and control by diversifying the banks' ownership structure, to clarify the order of pay-outs in the event of bank liquidations, and to improve the definition of systemically important banks in the banking system. Following the regulations approved by the Bank of Mongolia and the Financial Regulatory Commission, banks submitted their plans to become public companies by preparing their initial public offerings (IPOs), and commenced to successfully launch their IPOs within 2021.

In addition, the legal environment of the financial sector, technological infrastructure, payment, supervision and regulatory tools have been improved, and a step-by-step plan to return to normalcy to terminate temporary pandemic regulations. The Bank of Mongolia has received the "Best Innovation" award at the "Bloomberg TV Mongolia Awards 2021" for successfully transferring the national payment "₮" card to EMV technology. The successful transfer of the "₮" card to international standard EMV chip technology has improved privacy and security, reduced the risk of duplicating ₮ card information, and is an important step in the introduction of advanced mobile payment solutions. The process of making payments and transactions has become easier and faster with the introduction of the ₮ card with EMV chip. For example, citizens can make payments with their card from a distance and without a PIN code within a certain range, moreover, payments such as public transportation, parking, and road bills quickly. As a result, a favorable environment for new payment services has been created for commercial banks and Fintech companies.

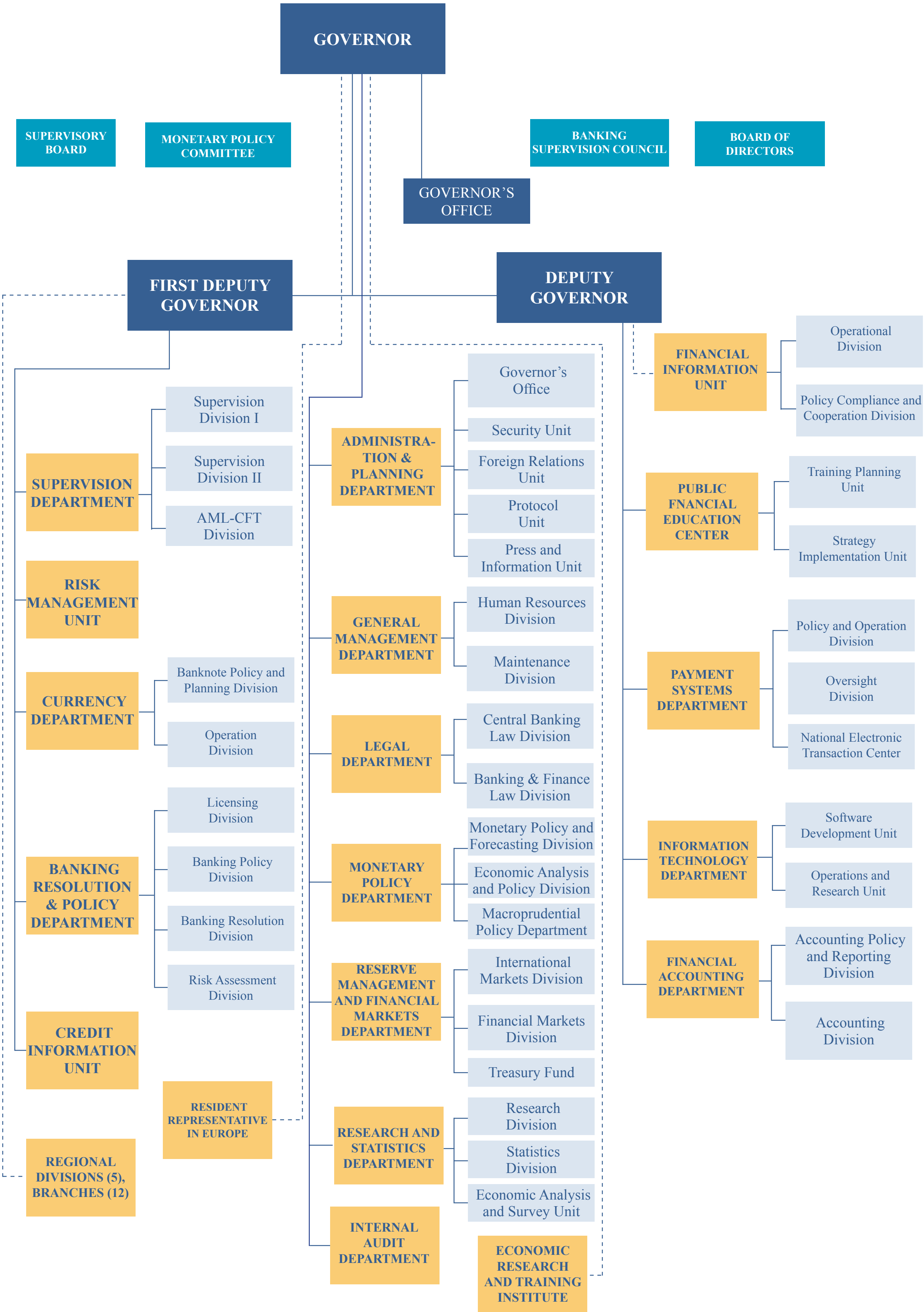
The Bank of Mongolia is pursuing counter-cyclical policy that is fully in accordance with the country's situation in order to maintain a strong economic recovery and successfully continue the ongoing reforms in the banking sector. The central bank will develop policy adjustments based on research and analysis, communicate its decisions and rationale in an open and transparent manner, and continue to contribute to improving public financial literacy.

We are confident that together we can turn challenges into opportunities, sustainably recover our economy, and successfully continue to pursue banking reforms.

May Mongolia flourish and prosper.

GOVERNOR LKHAGVASUREN B.

ORGANIZATIONAL STRUCTURE OF THE BANK OF MONGOLIA



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MACROECONOMIC OVERVIEW OF MONGOLIA

1

1.1 REAL SECTOR

Gross domestic product

Gross Domestic Product (GDP)[1] increased by 1.4%[2] compared to the previous year. The change in GDP can be explained by the following contributions. Investment contributed 18.3%, government consumption contributed 1%, and household consumption contributed-4.5% (Figure 1.1).

Due to the COVID-19 pandemic, "Zero-Covid" policy measures including border closure implemented by the Chinese government resulted in goods and services exports decreasing by 14.5% and hence the net exports to fell by 13.4%.

Figure 1.1: GDP growth, expenditure approach

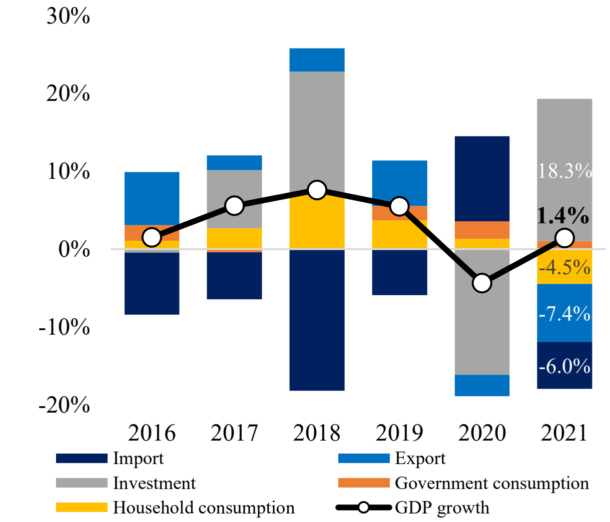
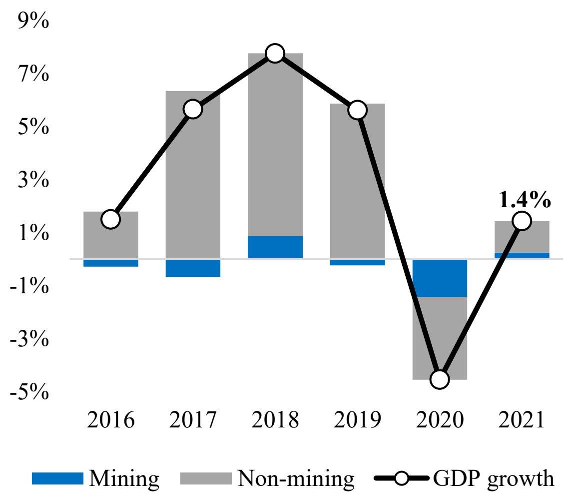


Figure 1.2: GDP growth, production approach



Source: The National Statistics Office of Mongolia

The non-mining sector production, which declined by 3.1% in the previous year, increased by 4.3% in 2021, which made up 1.2% of the total GDP growth. The mining sector accounted for the remaining 0.2% of total output growth (Figure 1.2). Regarding the non-mining sector, transportation and warehousing sector fell by 16.7% resulting in 0.8% decrease in GDP growth, construction sector fell by 32.7% resulting in 1.3% decrease in GDP growth. Moreover, the fact that annual production of food and export from livestock could not reach last year's output, resulted in 5.5% decrease in agricultural sector, hence resulting in GDP growth to fall by 0.8% (Figure 1.3).

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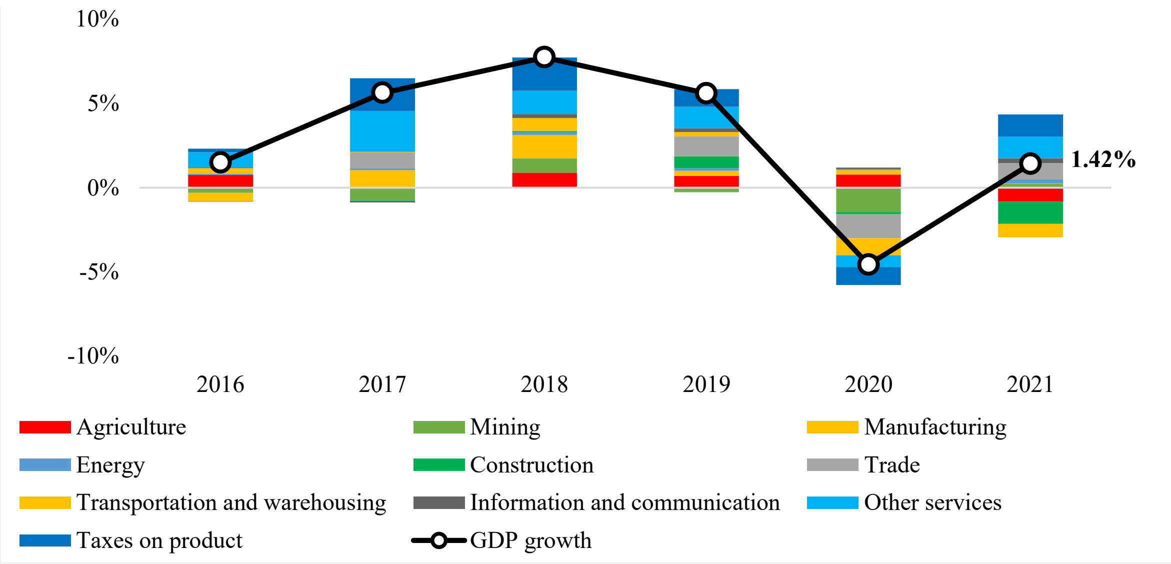
1 Calculated at the base price of 2015

2 GDP growth measured by production approach.

Figure 1.3: GDP growth by production sectors



Source: The National Statistics Office of Mongolia

The construction sector, which showed a continuous declinefor the past 6 quarters, still had a 32.7% decrease in 2021, resulting in 1.3% of GDP growth slowdown. The energy sector increased by 9.4% and manufacturing sector by 0.3%, which contributed the GDP growth by 0.2% and 0.3%, respectively (Figure 1.4).

Figure 1.4: The growth of agriculture and manufacturing

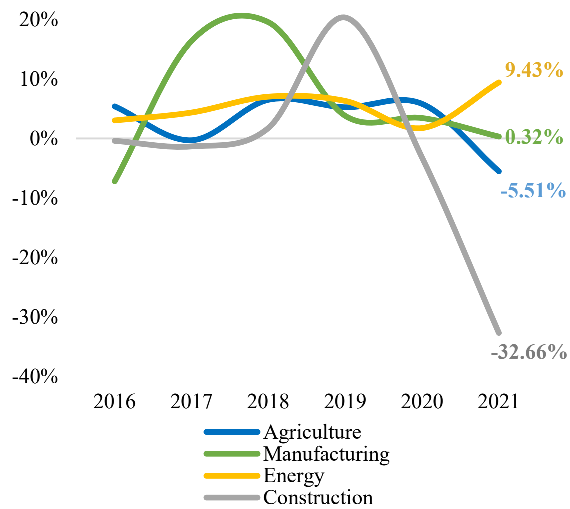
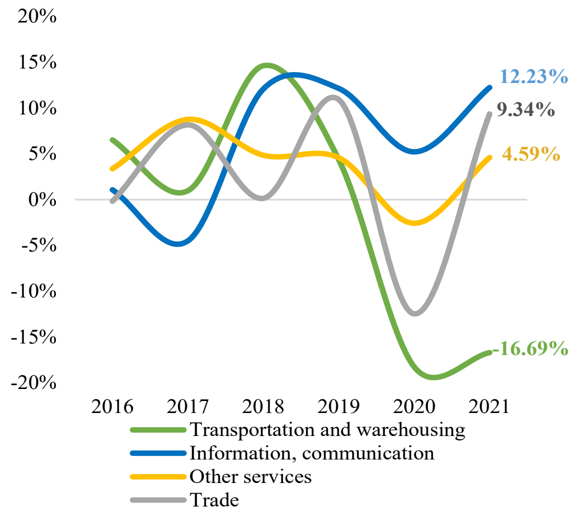


Figure 1.5: The growth of service sector



Source: The National Statistics Office of Mongolia

Inflation

It was stated in the "Monetary Policy Guidelines for 2021" to stabilize inflation around 6 percent within interval of +/-2 percentage points, between the period from 2021 to 2023. Though nationwide consumer price inflation remained low in the 1st quarter, it started to reach the target level in the 2nd and 3rd quarters of 2021, surpassing the target in the 4th quarter to reach 13.4 percent by the end of the year.

The global economy recovered significantly in 2021 after slow down due to the “COVID-19” pandemic in the previous year, creating excess demand over supply, which in turn pushed up inflation. In addition, inflationary pressure of imported products intensified due to production disruptions associated with prolonged transportation and logistics delay, and higher commodity prices. As for domestic prices, a number of factors including elevated costs of transportation and production, outbreak of infectious animal diseases, and increases in vegetable prices earlier than its seasonal trend contributed to higher inflation (Figure 1.6).

Amid the ongoing pandemic, the set of macro stabilization policy measures that aimed to alleviate the financial burden on households and to support consumption has been stimulating domestic demand. Therefore, gradual recovery of economic activities in 2021 had the effect of driving demand-driven inflation to some extent.

Figure 1.6: Monthly and annual inflation

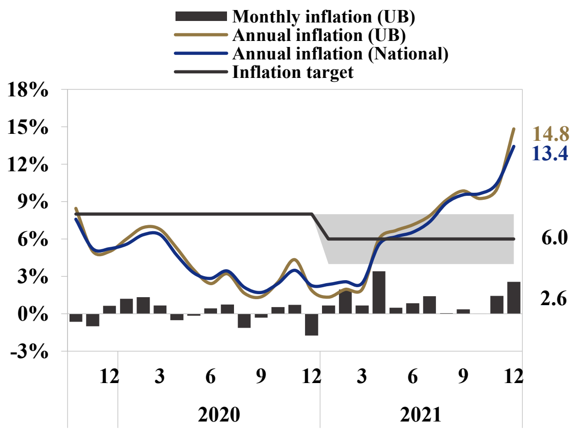


Table 1.1: Inflation contribution by products

Product	Basket weight	Annual growth	Contribution to annual inflation
Meat	**0.10**	**24.3%**	**2.4%**
Gasoline	**0.06**	**48.3%**	**2.2%**
Vegetable	0.02	44.4%	1.0%
Firewood	0.01	39.0%	1.0%
Catering service	0.04	22.6%	1.0%
Dairy products	0.04	19.9%	0.8%
Refined coal	**0.02**	**100.0%**	**0.7%**
Total	0.29		9.1%

Products that have a greater impact on inflation[3] (Table 1.1):

- **Non-meat domestic food price** inflation accounted for 2.3 percentage points of the inflation. Firstly, when vegetables’ import supply was disrupted in October due to border issues, domestic vegetable prices increased earlier than its trend and remained at a high level. Secondly, the impact of the pandemic and rising gasoline prices have been leading to higher production cost and prices of domestic food.
- **Domestic meat price** normally decreases throughout fourth quarter according to its seasonal pattern. However, it grew against it in the 4th quarter of 2021, contributing to annual inflation by 2.2 percentage points. Outbreak of contagious animal diseases in October caused negative shock to meat supply that may have caused higher meat price.
- **Imported food price** contributed 1.8 percentage points to annual inflation. This could be explained by several events. Firstly, “Zamiin-Uud” border had been closed since October, which caused supply shortage for imported perishable goods. Secondly, owing to such border issues and rising gasoline prices, transportation cost increased sharply. Lastly, international food price has been steadily rising and led to higher imported food prices in the 4th quarter.
- **Gasoline price** contributed 2.2 percentage points to annual inflation. Despite nominal exchange rate remaining stable, domestic gasoline price surged by around MNT 850 on average this year in line with sharp growth of global oil prices.
- **Refined coal** contributed 1.7 percentage points to annual inflation. This was due to 1) the price of firewood increased by 39 percent annually 2) Despite being sold at a subsidized price with 50 percent discount, **refined coal price** contributed to year-end inflation by 0.7 percentage points, owing to the base period during which prices were down by 75 percent.

[3] Annual inflation of Ulaanbaatar

Employment

In 2021 the key indicators of the labor market have decreased and the labor market remains weak compared to the pre-pandemic levels. For instance, the labor force decreased by 1.4% and reached 2,104.7 thousand people. The economically active population rose by 0.8%, which increased the number to 1,226.5 thousand people, while economically inactive population declined by 4.4%, which made the inactive population 878.2 thousand people. Since the number of economically active population rose and the inactive population has shown a decline, the labor force participation rate has increased by 1.3% and reached 58.3% (Figure 1.7). The number of unemployed people has surged this year, which caused the unemployment level to reach 8.1% after rising by 0.5% since last year (Figure 1.8).

Figure 1.7: Labor force participation rate

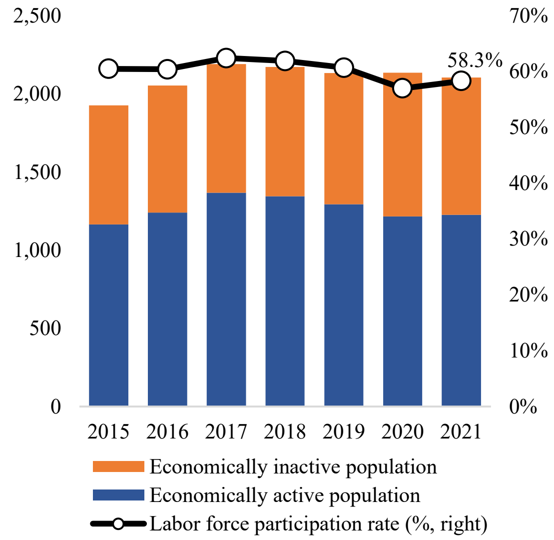
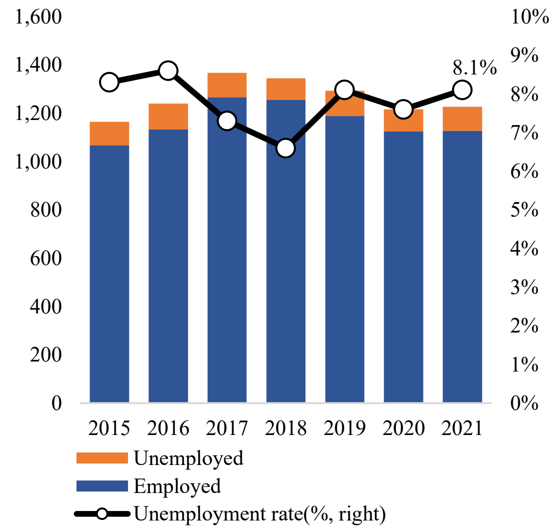


Figure 1.8: Unemployment rate

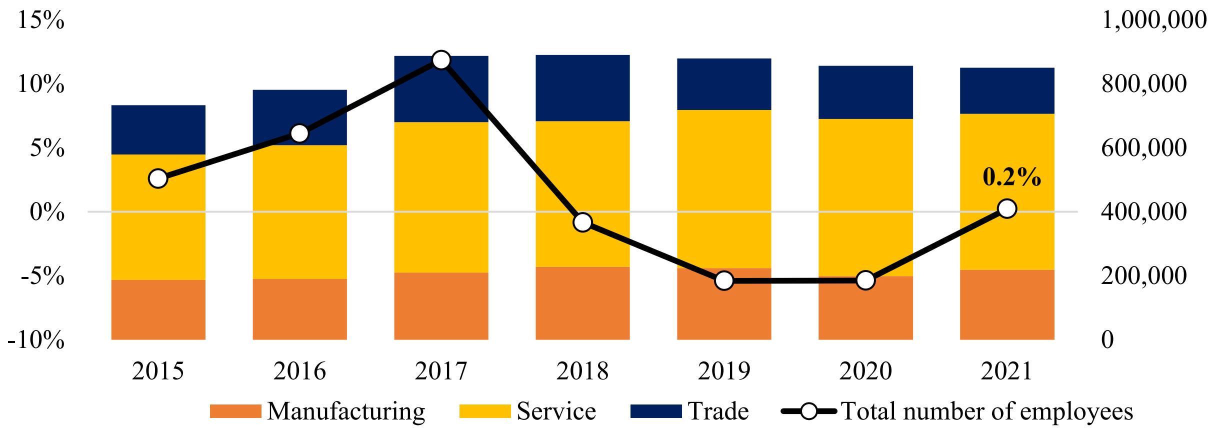


Source: The National Statistics Office of Mongolia

In 2021, the total number of employed workers by major economic sectors can be broken down into the following: 487.1 thousand (43.2% of the total labor force) in the service sectors, 277.8 thousand (24.7% of the total labor force) in the agricultural sector, 218.7 thousand (19.4% of the total labor force) in the manufacturing sector, and 143.5 thousand (12.7% of the total labor force) in the trade sector (Figure 1.9).

Employment rate increased by 0.2% compared to the previous year, which is mostly affected by the increase in number of employees in the agricultural and manufacturing sectors. Meanwhile the number of workers in the trade and service sectors slowed down.

Figure 1.9: Employment, by economic sectors



Source: The National Statistics Office of Mongolia

1.2 EXTERNAL SECTOR

Balance of Payments

According to the preliminary report of 2021, the current and capital account reported a 1,832 million USD deficit, the financial account reported a 1,835 million USD surplus, and the balance of payments deficit reached 222 million USD. Statistical errors and omissions are 224 million USD.

Figure 1.10: Balance of Payment

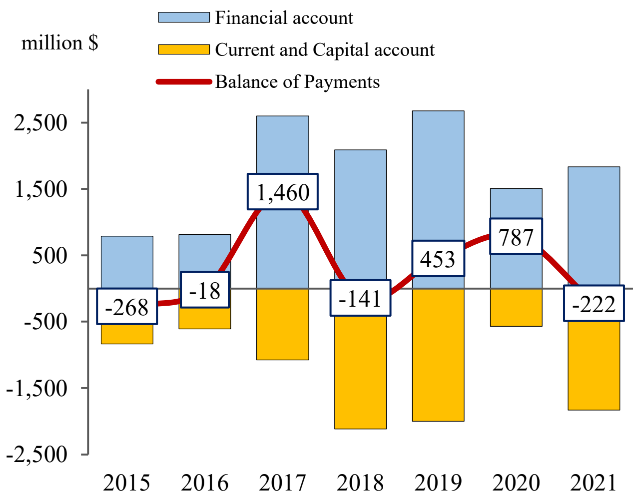
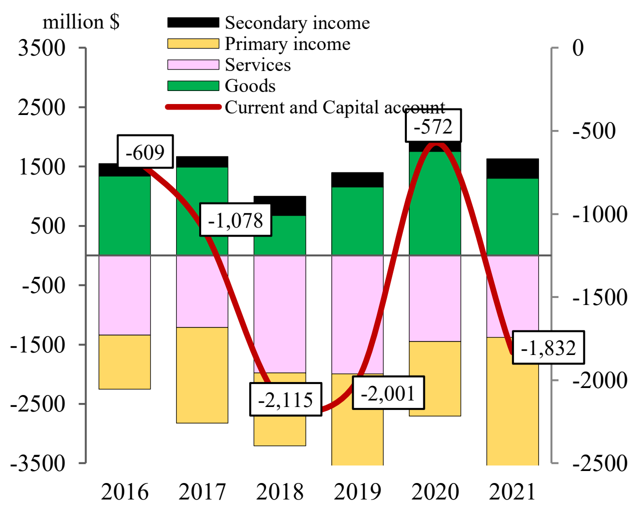


Figure 1.11: Current and Capital account composition



Source: The Bank of Mongolia

In 2021, the current and capital account deficit was 1,832 million USD, an increase of 220% or 1,261 million USD from the previous year. This deterioration is mainly due to an increase in the primary income account deficit.

Figure 1.12: Financial account composition

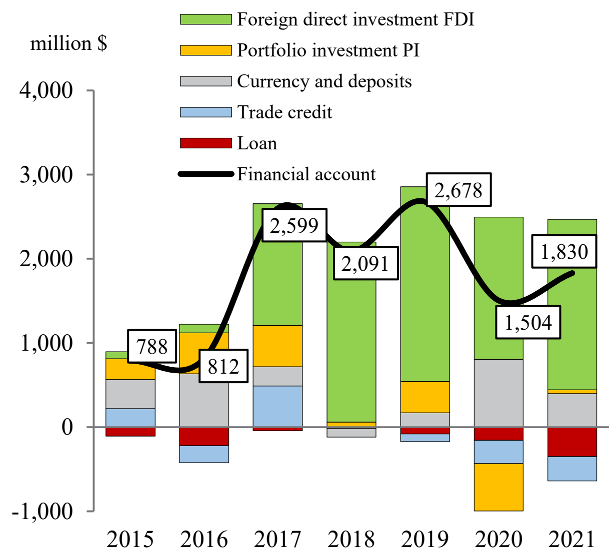
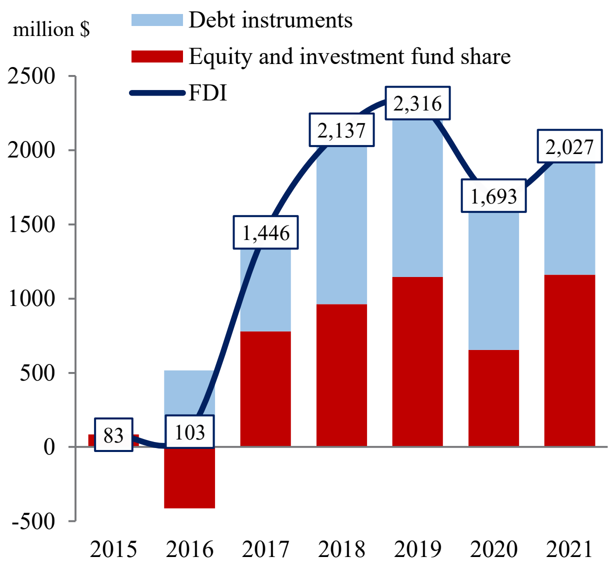


Figure 1.13: FDI composition



Source: The Bank of Mongolia

In 2021, the financial account surplus increased by 22 percent, or 331 million USD from the previous year and reached 1,835 million USD. According to the interpretation of the 6th edition of the Balance of Payments Manual, Mongolia issued net borrowing in the reporting year.

Trade in goods

Mongolia's trade balance recorded a surplus of 2,398 million USD in 2021, for the 8th consecutive year. Trade balance increased by 5 percent or 121 million USD from the previous year and reached 2,398 million USD. In particular, import increased by 29 percent or 1,550 million USD and export increased by 22 percent or 1,671 million USD from the previous year. Consequently, trade turnover increased by 25 percent or 3,221 million USD year on year.

Table 1.2: Foreign trade performance (million USD)

Category	2015	2016	2017	2018	2019	2020	2021	Change (21'/20')	
								Value	%
Turnover	**8,467**	**8,274**	**10,538**	**12,887**	**13,747**	**12,875**	**16,096**	**3,221**	**25%**
Export	4,669	4,916	6,201	7,012	7,620	7,576	9,247	1,671	22%
Import	3,798	3,358	4,337	5,875	6,128	5,299	6,849	1,550	29%
Balance	**872**	**1,558**	**1,863**	**1,137**	**1,492**	**2,277**	**2,398**	**121**	**5%**

Source: Mongolian Custom general administration

Export: In 2021, the exports of copper concentrate increased by 1,122 million USD, coal by 640 million USD, iron ore by 313 million USD, crude oil by 123 million USD resulting in the increase of mining exports by 21 percent or 1,469 million USD.

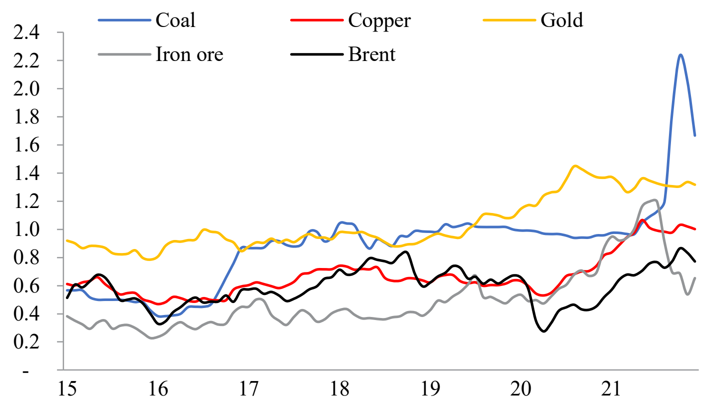
Compared to the previous year, export of manufactered goods increased by 56 percent or 130 million USD and animal products increased by 27 percent or 80 million USD.

Main export mineral prices in international markets remained high throughout 2021. The global economy recovered rapidly at the end of 2020, as the increased industrial activity resulted in rapid increase in demand for minerals, but the supply did not recover as much as demand, this resulted in high prices throughout the year of 2021.

Gold price: Gold price averaged 1,800 USD per ounce in 2021, up 1.6 percent from the previous year. This was mainly due to (i) the prevalence of COVID-19 variants, resulting in high uncertainty, and (ii) disruptions in the global supply chain, rising commodity prices, and increased demand resulted in high inflation of global economies.

Copper price: Refined copper prices on the London Metal Exchange averaged 9,291 USD per tonne in 2021, up 50% from the previous year.

Figure 1.14: Commodity price index in global markets (2011/1=1.0)



Source: Bloomberg

Copper prices soared due to: (i) as global economy recovered rapidly, demand for copper soared (ii) copper reserves at major metal exchanges fell to historic lows. (iii) a strike in Chile, a major copper supplier, and a supply cut off by locals in Peru's main transportation route to copper deposit.

Coking coal price: The price of coking coal on the Chinese Dalian Stock Exchange reached an average of 221 USD per tonne in 2021, up 69 percent from the previous year. Coal prices increased due to (i) China's ban on Australian coal imports continued, and coal imports from Mongolia were delayed throughout 2021 due to the pandemic. (ii) due to energy crisis in China, thermal coal was replaced by coking coal. (iii) China's domestic coal mines had high environmental control measures in place throughout 2021. (iv) some coking coal mines in China were temporarily shut down due to zero COVID-19 policy.

Iron ore price: Iron ore prices reached 156 USD per tonne in 2021, up 50 percent from the previous year. Iron ore prices increased due to: (i) due to high price and demand for steel in the world market, demand for iron increased; and ii) China's easing of its fiscal and monetary policy stance at the end of 2021, resulting in mineral demand to increase, and demand for iron to increase.

Crude oil price: Brent crude has averaged 70 USD per barrel in 2021, up 64 percent from the previous year. On the supply side, fearing that demand would not recover due to the pandemic, OPEC only gradually increased production throughout 2021, but did not reach pre-pandemic levels.

On the demand side, demand remained high when the Omicron variant spread as countries around the world did not take the same drastic measures as before.

In addition, in the last few months of the year, due to the geopolitical tensions between Russia and Ukraine uncertainty increased, resulting in the oil price to increase.

Table 1.3: Export of goods (million USD)

Category	2015	2016	2017	2018	2019	2020	2021	Change (21'/20')	
								Value	%
Mining products	**4,092**	**4,236**	**5,519**	**6,200**	**6,751**	**7,039**	**8,509**	**1,469**	**21%**
Copper ores and concentrates	2,280	1,608	1,613	2,012	1,796	1,778	2,900	1,122	63%
thousand tonne	*1,478*	*1,562*	*1,447*	*1,437*	*1,404*	*1,395*	*1,283*	*-113*	*-8%*
Coal	555	972	2,256	2,786	3,074	2,124	2,764	640	30%
thousand tonne	*14,426*	*25,714*	*32,990*	*35,758*	*36,467*	*28,587*	*15,708*	*-12,879*	*-45%*
Iron ores and concentrates	227	250	310	342	576	640	952	313	49%
thousand tonne	*5,065*	*6,085*	*6,258*	*7,449*	*8,449*	*8,202*	*7,106*	*-1,096*	*-13%*
Non-monetary gold	421	758	595	144	418	1,788	1,005	-783	-44%
Kg	*11,343*	*19,169*	*14,548*	*3,432*	*9,069*	*30,491*	*17,250*	*-13,241*	*-43%*
Other	609	648	744	914	886	710	888	178	25%
Non-mining products	**578**	**680**	**680**	**812**	**869**	**537**	**738**	**201**	**37%**
Total	**4,669**	**4,916**	**6,199**	**7,012**	**7,620**	**7,576**	**9,247**	**1,671**	**22%**

Source: Mongolian Customs and, Bank of Mongolia

In 2021, the export increase of 22 percent or 1,671 million USD was mainly due to price changes. More precisely, in 2021 the export increased by 68 percent due to price changes and decreased by 46 percent due to quantity changes. This is as Mongolia's export quantity decreased, but as commodity prices increased on world markets the total exports increased.

Import: In 2021, import expenditures increased by 29 percent or 1,550 million USD from the previous year. These can be explained by the following:

- Imports of consumer goods increased from the previous year by 642 million USD, of which food and medicine imports increased by 402 million USD.
- Imports of capital goods increased by 21 percent or 470 million USD. This increase is largely due to imports of machinery, equipment and parts, and building materials, each contributing to the increase by 25% and 21% respectively.
- While, import of petroleum products increased by 315 million USD is mainly due to petroleum price increase in the international market.

Table 1.4: Import of goods (million USD)

Category	2015	2016	2017	2018	2019	2020	2021	Change (21'/20')	
								Value	%
Consumer goods	**1,101**	**1,159**	**1,285**	**1,643**	**1,631**	**1,542**	**2,184**	**642**	**42%**
Non-durables	643	652	733	864	859	878	1,315	437	50%
Durables	459	507	553	779	772	664	869	205	31%
Capital goods	**1,447**	**1,155**	**1,702**	**2,396**	**2,661**	**2,290**	**2,760**	**470**	**21%**
Machinery, equipment, supplies and vehicles	757	687	1,077	1,512	1,801	1,419	1,771	352	25%
Construction materials	473	283	441	648	654	599	727	127	21%
Other capital goods	218	185	183	236	206	272	262	-10	-4%

Intermediate goods and industrial materials	**512**	**508**	**552**	**717**	**665**	**634**	**762**	**127**	**20%**
Petroleum products	**708**	**531**	**791**	**1,112**	**1,166**	**817**	**1,132**	**315**	**39%**
Diesel	377	255	428	577	669	432	590	158	36%
thousand tonne	*655*	*548*	*805*	*849*	*1,080*	*1,027*	*989*	*-38*	*-4%*
Gasoline A92-95	228	165	244	251	289	222	353	131	59%
thousand tonne	*361*	*332*	*354*	*352*	*476*	*529*	*514*	*-15*	*-3%*
Gasoline A80	46	26	33	45	38	23	38	15	65%
thousand tonne	*73*	*53*	*57*	*65*	*65*	*57*	*59*	*2*	*3%*
Other petroleum products	57	85	87	240	169	140	151	11	8%
thousand tonne	*58*	*124*	*153*	*292*	*223*	*250*	*202*	*-47*	*-19%*
Other	**29**	**6**	**7**	**7**	**5**	**15**	**11**	**-4**	**-27%**
Total	**3,798**	**3,358**	**4,337**	**5,875**	**6,128**	**5,299**	**6,849**	**1,550**	**29%**

Source: Mongolian Customs and, Bank of Mongolia

Trade in services

In 2021, a deficit in services accounts decreased by 5% from the previous year, reaching 1,380 million USD.

The following factors contributed to the service account deficit: transport service deficit decreased by 111%, amounting to 24 million USD. Construction services deficit decreased by 30%, amounting to 68 million USD.

Figure 1.15: Service exports (USD million)

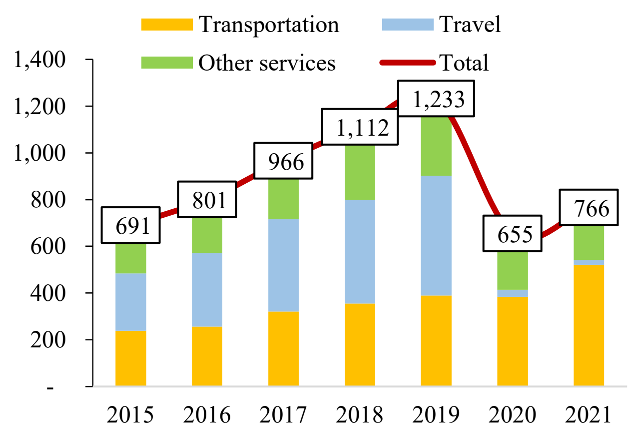
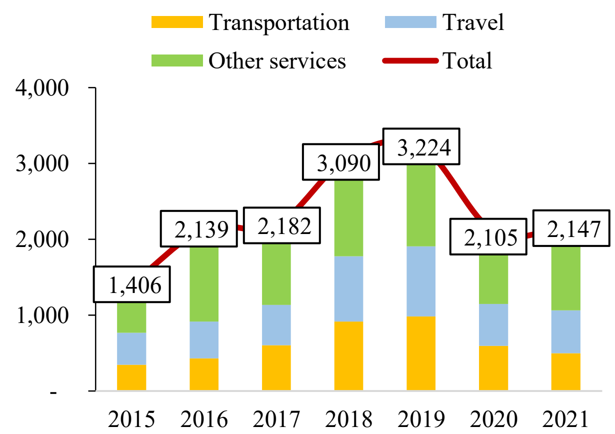


Figure 1.16: Service imports (USD million)



Source: Bank of Mongolia

Table 1.5: Foreign trade in services (USD million)

Service account	2015	2016	2017	2018	2019	2020	2021	Change (21'/20')	
								Value	%
1. Transportation	-106	-176	-284	-561	-594	-212	24	236	-111%
2. Travel	-176	-166	-137	-415	-412	-521	-545	-24	5%
3. Construction services	-81	-137	-218	-165	-107	-97	-68	29	-30%
4. Insurance services	-24	-15	-20	-21	-23	-21	-24	-2	12%
5. Financial services	-52	-205	-24	-121	-207	-145	-148	-3	2%

6. Royalties and license services	-13	-23	-15	-15	-25	-23	-30	-7	30%
7. Communication, computer and information services	-72	-69	-48	-64	-55	-70	-99	-29	41%
8. Other business services	-174	-529	-435	-590	-546	-343	-486	-143	42%
9. Other services	-18	-18	-35	-27	-23	-18	-4	14	-79%
Total services	**- 715**	**- 1,338**	**- 1,216**	**- 1,978**	**- 1,992**	**- 1,450**	**- 1,380**	**70**	**-5%**

Source: Bank of Mongolia

International investment position

Mongolia’s net international investment position reached -39,017 million USD 2021 preliminary, which is a 5 percent or 1,699 million USD increase year on year. Mongolia’s total investment abroad or net foreign assets stood at 8,238 million USD, of which 53 percent was in foreign exchange reserves, 32 percent in other investment; 10 percent in direct investment and the remaining 5 percent in portfolio investment.

While total investment in Mongolia or net foreign liabilities stood at 47,255 million USD, of which 55 percent was in direct investment liabilities, 35 percent in other investment, and the remaining 10 percent in portfolio investment.

Out of total foreign direct investment in Mongolia, 53 percent or 13,953 million USD was made in the form of shareholders’ investment in share capital, while 47 percent or 12,273 million USD were stock of loans from parent companies, so-called “inter-company lending”.

Table 1.6: Mongolia’s international investment position (USD million)

A. Foreign assets	**8,238**	**A. Foreign assets**	**47,255**
1. Direct investment abroad	824	1. Foreign direct investment in Mongolia	26,226
2. Portfolio investment	417	2. Portfolio investment	4,539
3. Financial derivatives	11	3. Financial derivatives	0
4. Other investment	2,619	4. Other investment	16,489
5. Reserve assets	4,366		
		C. POSITION	**-39,017**

Source: Bank of Mongolia

The annual growth rate of international investment short position was due to the following:

- The short positions in foreign direct investment increased by 1,892 USD.
- While, the short position in portfolio investment and other investments decreased by 179 and 167 million USD respectively. Foreign exchange-reserves decreased by 160 million USD.

Table 1.7: Changes in IIP (USD million)

Indicators	2015	2016	2017	2018	2019	2020	2021	Change (21'/20')	
								Amt	%
Foreign direct investment	-20,257	-15,822	-17,525	-19,690	-21,891	-23,510	-25,402	-1,892	8%
Portfolio investment	-2,844	-3,351	-4,668	-4,589	-5,146	-4,301	-4,122	179	-4%
Financial derivatives	-51	-15	0	-1	9	4	11	8	214%

Other investment	-6,800	-11,458	-12,846	-12,891	-13,144	-14,037	-13,870	167	-1%
Reserve assets	1,323	1,296	3,008	3,542	4,341	4,526	4,366	-160	-4%
Total position	**- 28,629**	**- 29,350**	**- 32,031**	**- 33,630**	**- 35,831**	**- 37,318**	**- 39,017**	**1,699**	**5%**

Source: Ministry of Finance

External debt

At the end of 2021, Mongolia's outstanding external debt totaled 33,190 million USD, which is an increase of 3 percent or 829 million USD compared to the previous year. Change in external debt stock can be mainly explained by the following factors:

Government external debt decreased by 2 percent or 171 million USD due to decreased concessional borrowing by the government from foreign organizations and financial institutions.

Central Bank's external debt increased by 15 percent or 341 million USD due to the allocation of the IMF SDRs, as well as gold financing.

Increased external debt in the private sector was mainly due to an increase in intercompany loans. The intercompany debt increased by 8 percent or 867 million USD due to the increase in intercompany lending from the parent company. However, the external debt of other sectors decreased by 2 percent or 208 million USD.

Table 1.8: Mongolia's Gross External Debt (USD million)

Indicators	2015	2016	2017	2018	2019	2020	2021	Change (21'/20')	
								Amt	***%***
TOTAL EXTERNAL DEBT	**22,718**	**23,459**	**24,260**	**28,715**	**30,702**	**32,362**	**33,190**	**829**	**3%**
Government	3,760	4,073	4,786	7,184	7,806	8,654	8,483	-171	-2%
Government external debt/GDP (%)	*31%*	*41%*	*66%*	*59%*	*57%*	*66%*	*56%*	*-0.1*	*-15%*
Central bank	1,960	2,084	1,758	2,030	1,985	2,221	2,562	341	15%
Deposit-taking corporations (Other than Central bank)	2,129	2,182	2,216	2,230	2,138	1,651	1,651	0.4	0.02%
Short-term	407	444	465	764	610	594	408	-185	-31%
Long-term	1,721	1,738	1,751	1,466	1,528	1,057	1,243	186	18%
Other sector	3,749	3,787	8,304	8,042	8,407	8,430	8,222	-208	-2%
Short-term	326	343	518	609	562	683	400	-284	-42%
Long-term	3,423	3,444	7,786	7,433	7,845	7,747	7,822	75	1%
Intercompany lending	11,121	11,333	7,196	9,228	10,366	11,406	12,273	867	8%

Source: Ministry of Finance, Bank of Mongolia

The share of Government external debt portion in GDP maintained between 29-41 percent during the 2013-2016 period. However, in 2017 the share portion increased to 66 percent. In the years, 2018 and 2019, the share portion had decreased to 59 percent and 57 percent, respectively. In 2020, the share portion returned to 66 percent.

However, in 2021, due to increased GDP levels and the decreased foreign debt levels, the share portion decreased to 56 percent (according to international standard, the Development Bank of Mongolia's external debt is classified as other sectors).

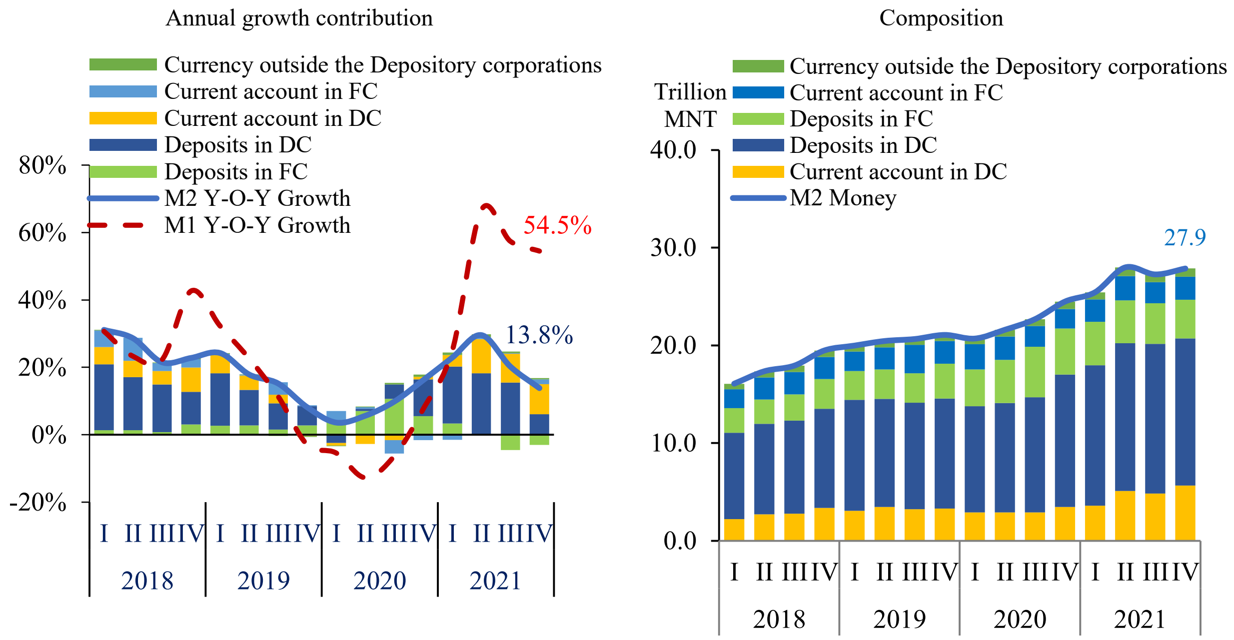
1.3 MONETARY AND FINANCIAL SECTOR

Money and Credit indicators

The average annual growth rate of M2[4] money supply during 2020 was 16.2 percent, and the first half of 2021 was 25.4 percent, peaking at 32.1 percent in April and declining to 13.8 percent, totaling to MNT 27.9 trillion by the end of the year. On the liabilities side, M2 annual growth can be broken down into the following: 9.0 percentage points by current accounts in domestic currency, 6.1 percentage points by deposits in domestic currency, 1.4 percentage points by current accounts in foreign currency, 0.4 percentage points by currency outside of depository corporations, and -3.0 percentage points by deposits in foreign currency.

The growth of annual M1 money supply, consisting of the most highly liquid assets, was driven by an increase of MNT 2,200.8 billion in current accounts and MNT 94.0 billion in currency outside of depository corporations, contributing a total of 9.4 percentage points to the M2 money supply growth. The growth of other deposits[5] contributed 4.4 percentage points to the increase in M2 money supply growth. This growth can be explained by the following: deposits in domestic currency increased by MNT 1,438.9 billion, current accounts in foreign currencies increased by MNT 347.5 billion, and deposits in foreign currencies decreased by MNT 743.5 billion.

Figure 1.17: Money supply, by contribution and composition (Liabilities):



Source: Bank of Mongolia

If we consider the 13.8 percent annual growth of money supply during the first half of 2021 from the assets side, claims on private sector and individuals contributed 17.6 percentage points, net credit to the government accounted for 4.4 percentage points, and net foreign assets contributed -8.2 percentage points. In other words, the share of money supply in net domestic assets outweighed share of money supply in net foreign assets. Higher new loan issuance of depository corporations[6] resulted in an increase in claims on private sector and individuals, whereas the increase in net credit to the government is the result of a decrease in social security's deposits in the banks.

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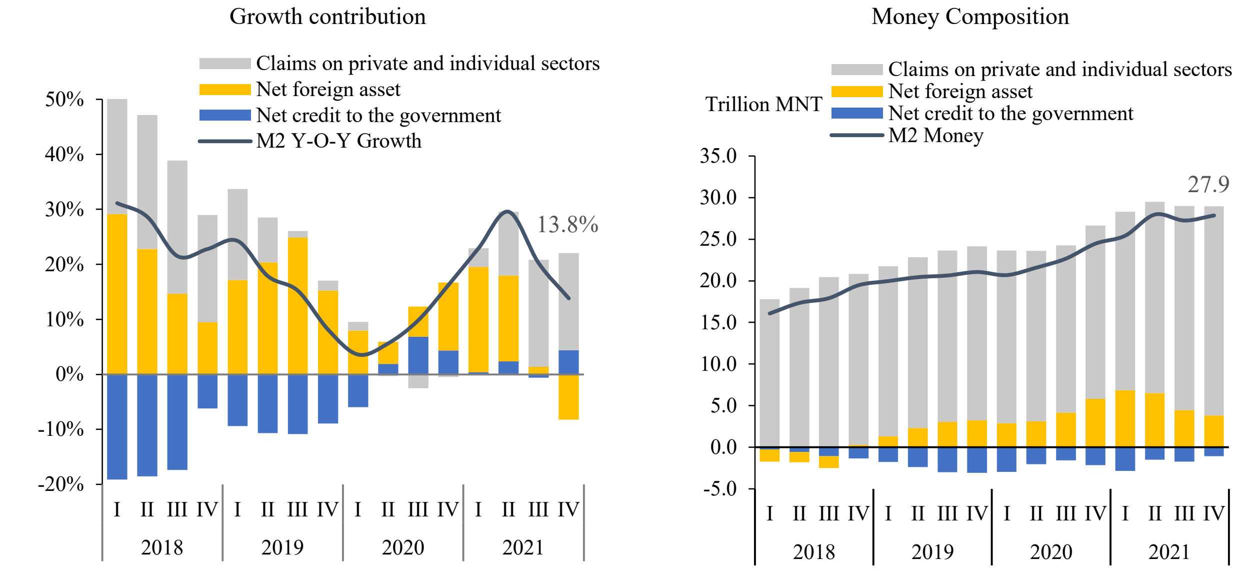
[4] M2 Money=M1+other deposits

[5] Other deposits consist of deposits in domestic and foreign currencies, and current accounts in foreign currency.

[6] Depository corporations consist of banks and credit and savings unions.

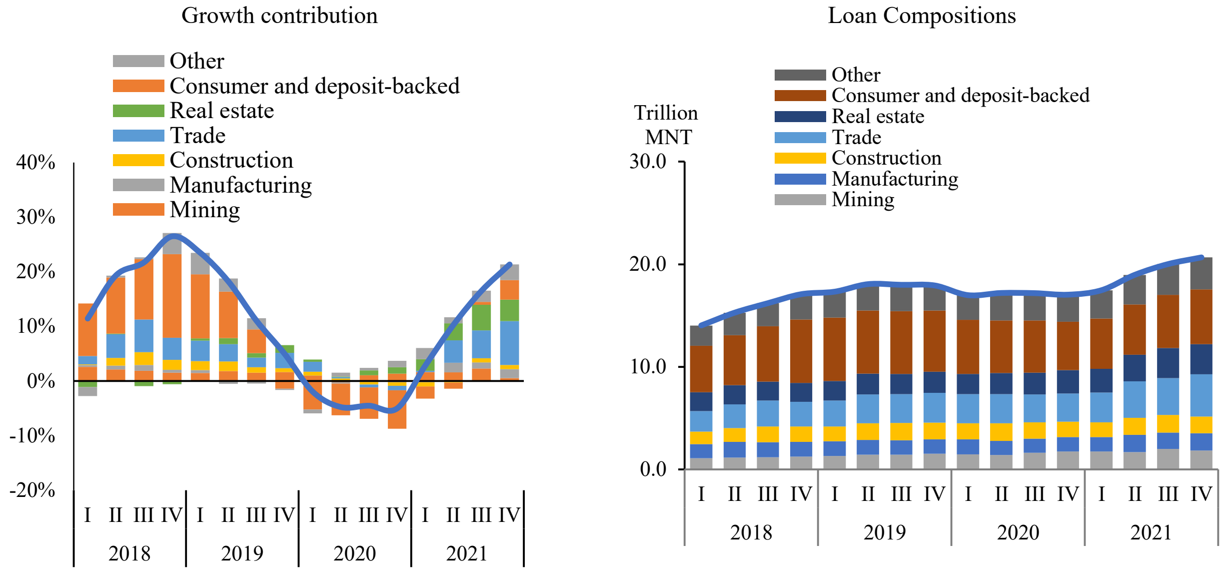
Figure 1.18: Money supply, by contribution and composition (Assets):



Source: Bank of Mongolia

Annual credit growth declined by 5.0 percent in 2020 and increased from the end of the first quarter of 2021. As a result, by the end of 2021, annual credit growth increased by 21.3 percent, reaching a total of MNT 20.7 trillion. Consumer[7] and deposit-backed loans declined in the first half of 2021 but increased by 3.6 percent by the end of the year. Compared to the same period the previous year, the growth of loans issued to the trade, real estate, manufacturing, and mining sectors were recorded at 8.1 percent, 3.9 percent, 1.6 percent, and 0.5 percent, respectively.

Figure 1.19: Banks outstanding loan growth, by economic sectors



Source: Bank of Mongolia

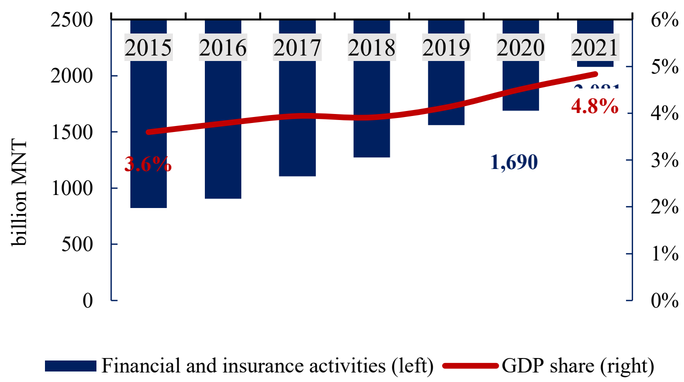
7 Consumer loans = Salary + Pension + Credit card + Herder's + others

Banks total outstanding loan growth can be mainly explained by changes in the following economic sectors: consumer and deposit-backed loans increased by 1.9 percentage points accounting for 25.7%, trade sector loans decreased by 3.8 percentage points accounting for 19.9%, and real estate loans decreased by 0.9 percentage points accounting for 14.3% of total outstanding loan growth respectively.

Financial sector

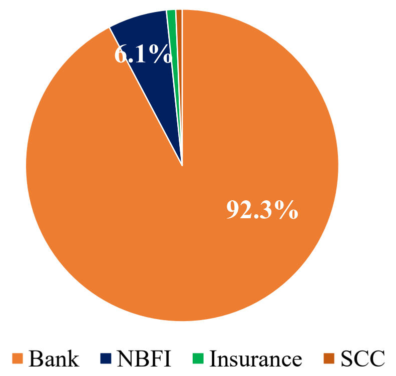
As of the end of 2021, there are 11 commercial banks, 534 non-bank financial institutions, 209 savings and credit cooperatives, 17 insurance companies, 57 insurance intermediary companies and 25 insurance loss-adjuster companies operating in the Mongolian financial sector. Even though the scope of activities in the non-bank financial sector has increased year by year, the banking sector accounts for more than 90 percent of total financial system.

Figure 1.20: GDP share of financial and insurance activities



Source: NSO, FRC

Figure 1.21: Total assets of Financial sector, by share of institutions (as of 2021)



Source: FRC

Total assets of Non-bank Financial Institutions (NBFIs) increased by 35.0% year-on-year and reached MNT 2.7 trillion by the end of 2021. The loan portfolio increased by 51.6% or MNT 685.1 billion year-on-year, explaining 34.1% of the total assets increase. 90.5% of total outstanding loans were performing, 2.5% classified as past-due and 7.0% as non-performing loans. Compared to previous year's indicators, the share of non-performing loans to total loans declined by 3.3 percentage points and the share of past-due loans decreased by 2.4 percentage points.

Total assets of Savings and Credit Cooperatives (SCCs) increased by 13.8% year-on-year, reaching MNT 291.2 billion, while total outstanding loans increased by 27.4% year-on-year, reaching MNT 213.4 billion. By the end of 2021, 3.5% of SCCs loans were classified as non-performing.

A total of 17 insurance companies, including 15 non-life, 1 life, and 1 reinsurance, conducted operations in 2021. Total assets of insurance companies increased by 11.3% year-on-year and reached MNT 425.4 billion by the end of 2021. Although core indicators of the insurance sector have been growing in recent years, the insurance market depth (insurance premiums to GDP), a key measure of the sector's development, remains low compared to international levels. By the end of 2021, the insurance premiums to GDP ratio was 0.58%, showing 0.03 percentage point increase from the previous year. Total premium income of the insurance sector reached MNT 247.5 billion, most of which were from non-life insurance. From the total premiums, 28.3% or MNT 69.9 billion were spent on insurance claims. Compared to the end of 2020, return on assets and return on equity increased by 0.4 percentage points and 1.0 percentage points, respectively.

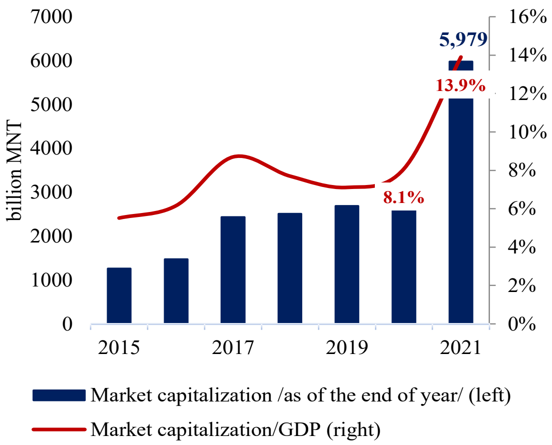
In 2021, a total of MNT 1.4 trillion worth of securities was traded in the stock market, of which 74.1% were corporate bonds, 21.6% were corporate stocks and the remaining 4.0% were investment funds. Mongolia's stock market capitalization reached MNT 6.0 trillion, increasing by 97.5% or MNT 2.9 trillion from the previous year.

Table 1.9: Non-bank financial sector as of 2021, in billions of MNT

Indicators	NBFI	SCC	Insurance
Assets	2,709.9	291.1	425.4
Liabilities	910.8	227.3	225.9
Equity	1,589.1	63.9	199.5
Debt balances	2,012.2	213.4	-
Non-performing loans	140.2	7.4	-
Profit for the reporting year	210.0	10.7	25.2
Insurance premium incomes	-	-	247.5
Payments for insurance claims	-	-	69.9

Source: FRC

Figure 1.22: Market capitalization



Source: FRC, NSO

Banking sector

As of this reporting year, there were 11 banks in the sector, employing a total of 15,958 workers across 1393 branches. Deposit accounts and number of debtors reached a total of 3.0 million and 946.4 thousand, respectively.

The banking sector's total assets increased by MNT 4.5 trillion, or 12.5 percent, to MNT 40.8 trillion in 2021, compared to the previous year. This is 12.8 percentage points growth from the last year, when annual asset growth was -0.3 percent. Credit growth accounts for the bulk of the annual growth of the asset.

At the end of 2021, the total outstanding loans in the banking sector reached MNT 20.9 trillion, comprising 47.2 percent of total assets. The total outstanding loans in the banking sector increased by 22.0 percent or MNT 3.8 trillion compared to the previous year, mainly due to employment support loans, repo-financed loans, and mortgage loans provided under the Economic Stimulus Program.

Figure 1.23: Total outstanding loan (in trln. MNT) and loan growth (yoy)

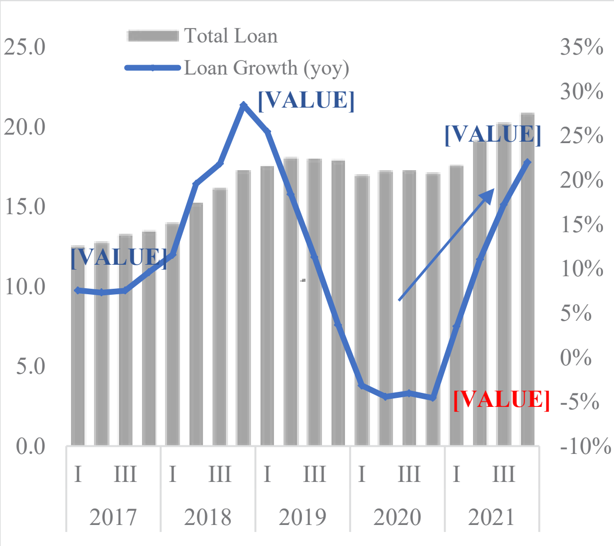
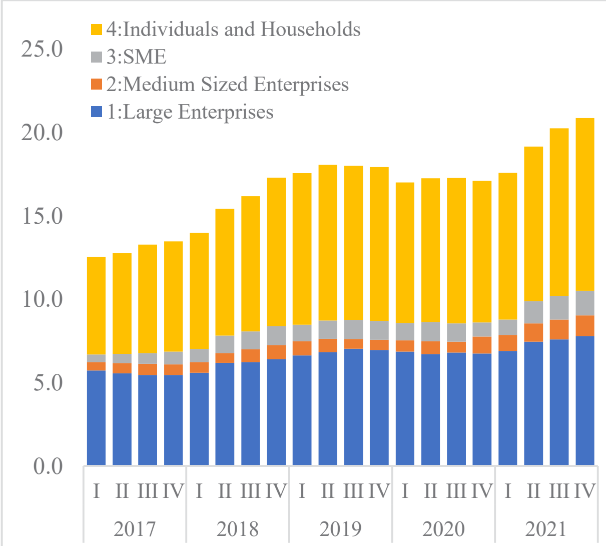


Figure 1.24: Total outstanding Loan by borrower type (in trln. MNT)



In the reporting year, loans to all sectors of the economy grew, with trade and consumer loans accounting for 62.4 percent of total loans.

The ratio of non-performing loans to total loans in the banking system was 9.1 percent, and the percentage of special mention loans was 6.6 percent, at the end of 2021. Compared to the previous year, non-performing loans grew by 3.9 percent or MNT 70.8 billion. Non-performing loans of corporates increased by 5.8 percent or MNT 77.1 billion, while non-performing loans of individuals decreased by 1.3 percent or MNT 6.3 billion.

Figure 1.25: Non-performing loan ratio by borrower type

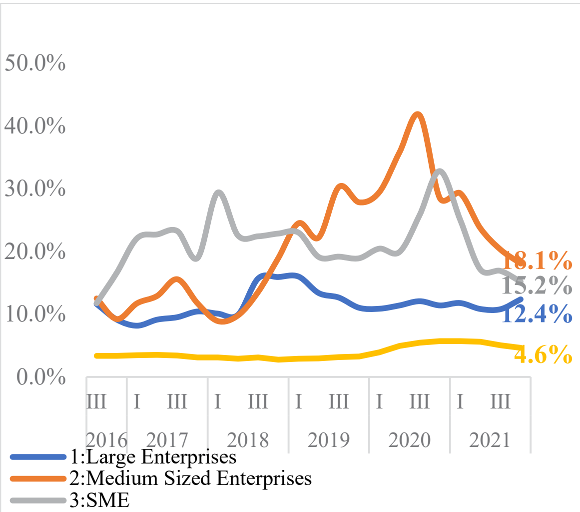
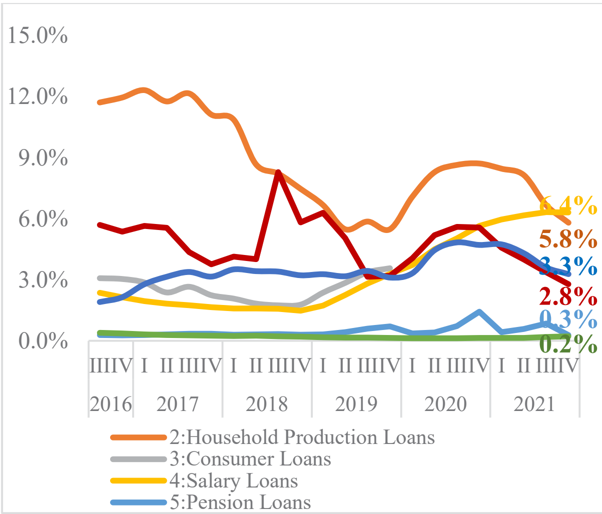


Figure 1.26: Non-performing loan ratio of Individual loans by borrower type



Source: The Bank of Mongolia

Among the main economic sectors, non-performing loans in mining, manufacturing, and construction accounted for 23.3, 17.8, and 17.1 percent, respectively, and were higher than the banking sector average, while the ratio of non-performing loans in the trade sector was the lowest at 2.9 percent.

At the end of 2021, the banking sector liabilities reached MNT 36.9 trillion, representing 12.4 percent growth from the previous year. Most of the annual growth of liabilities was contributed by growth of the current account balance.

Figure 1.27: Liabilities (in bln.MNT)

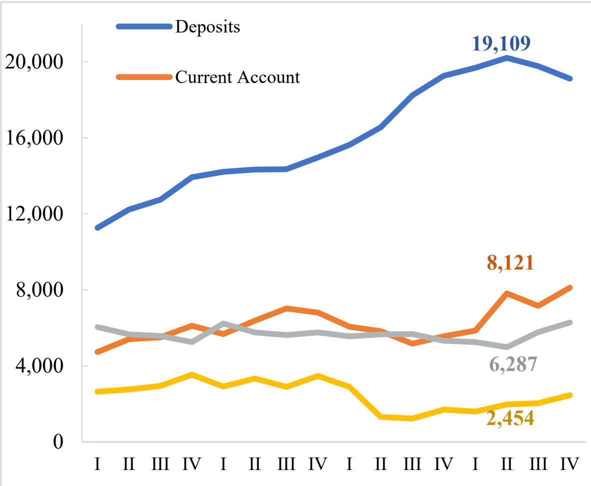
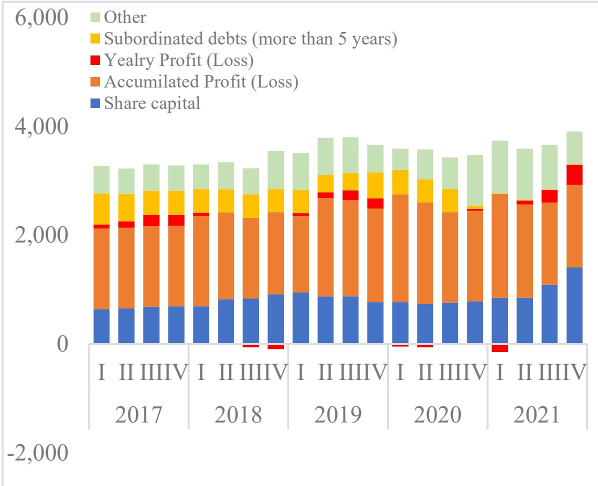


Figure 1.28: Bank capital composition (in bln.MNT)



Source: The Bank of Mongolia

In comparison to the end of the last year, the current account balance increased by 46.0 percent or MNT 2.6 trillion, while deposits decreased by 0.8 percent or MNT 147.9 billion. In terms of composition of total liabilities, current and deposit account accounted for 74% of total liabilities, by decreasing two percentage points from the previous year.

The increase in current and deposit account may have been driven by the factors that households temporarily delayed non-food expenditures due to the nationwide lockdown and government decided to exempt every household's utility bills (electricity, water, and waste) for the pandemic period. In addition, deferrals on mortgage loans and interest payments may have an accumulated effect on the current and deposit account of individuals who had planned to repay their loans.

Figure 1.29: Net Profit or Loss

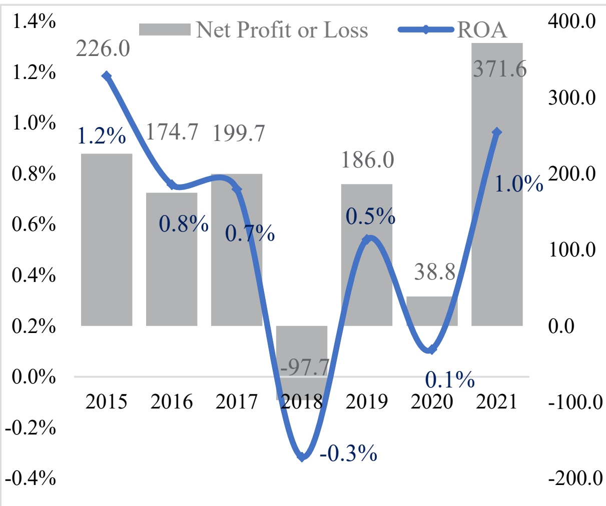
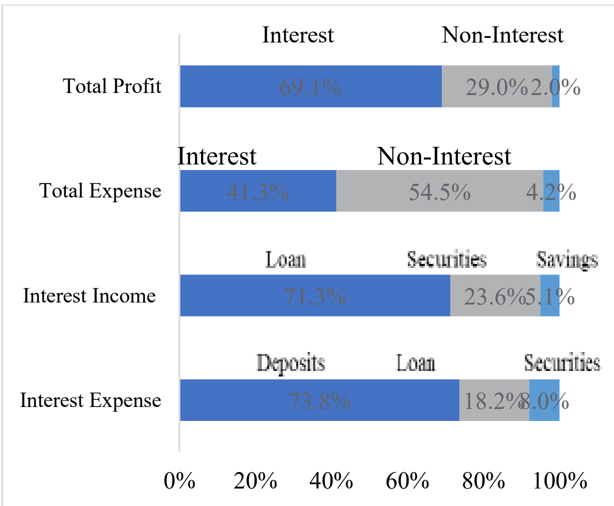


Figure 1.30: Composition of revenue and cost



In 2021, the banking sector's total income reached MNT 4.7 trillion, with interest income accounting for 69.1 percent and non-interest income accounting for 29.0 percent. As for the total interest income, its 71.3 percent was loan interest income, 23.6 percent was securities interest income, and the remaining 5.1 percent was interest income paid on current account and deposits. Meanwhile, total expenses reached MNT 4.3 trillion in 2021, of which 41.3 percent and 54.5 percent were interest expenses and non-interest expenses, respectively. Of total interest expenses, interest expenses on current and deposit accounts accounted for 73.8 percent, while loan and securities interest accounted for 18.2 percent and other interest accounted for 8.0 percent.

The banking sector's profit stood at MNT 371.6 billion in the reporting year, with a return on assets of 1.0 percent and a return on equity of 9.6 percent, while the banking sector profit were MNT 38.8 billion in 2020. In the reporting year, the banking sector's Tier 1 capital to risk-weighted assets ratio was 14.5 percent, the total equity and risk-weighted assets ratio was 14.5 percent, and the liquidity ratio was 41.6 percent.

As a result of the measures to reduce the economic impact of coronavirus infection (Covid-19) banking sector's total assets and profitability increased, and the bank's prudential ratios improved.

The Impact of the Covid-19 Pandemic on the Banking Sector

In accordance with other countries' experiences and banking-related legislation, the Bank of Mongolia has taken the necessary steps to mitigate the impact of the Covid-19 pandemic on the banking and financial sector.

The pandemic affected MNT 5.13 trillion loans of 175,604 borrowers as of December 31, 2021, with 77 percent (139,519 borrowers) loans totaling MNT 3.94 trillion being restructured. The number of loans affected by Covid-19 and restructured loans increased rapidly in 2020 but has been relatively stabilized since the beginning of 2021.

Figure 1.31: Loans affected by Covid-19 and restructured loans

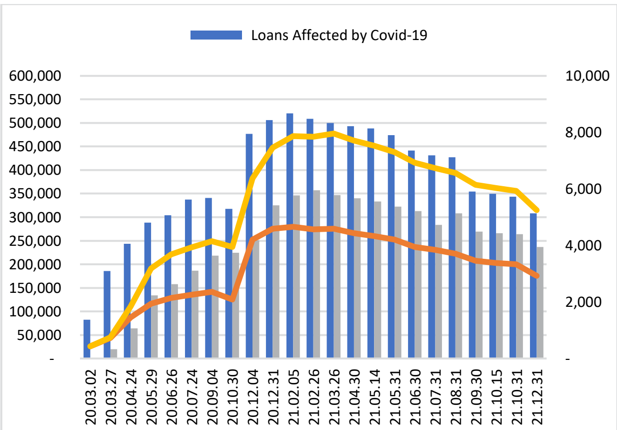
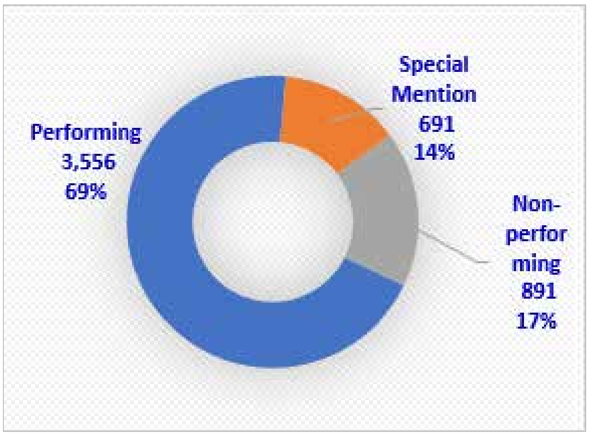


Figure 1.32: Quality of Loans affected by Covid-19



Source: The Bank of Mongolia

In accordance with the recommendations of the Banking Supervision Committee at the Bank of Mongolia dated June 29, 2021, the temporary regulation on "Asset classification, provisioning and its disbursements" for banks was partially extended until April 1, 2022, according to a predetermined schedule.

This gives banks the opportunity to restructure borrower's loan and banks were allowed to maintain the classification of defaulted loans and the borrower's credit history. Going forward, the Bank of Mongolia decided to gradually phase out the forbearance measures by the end of March 2022 in the way that changing the overdue days for downgrading the classification of loan quality (90 days) to 75 days from August 2021, 60 days from October 2021, 45 days from December 2021, 30 days from February 2022, and 15 days from April 2022. In addition, the temporary reliefs for prudential requirements of liquidity ratio and export LC's were rescinded.

Partial extension of temporary relief measures in the above-mentioned banking regulations and prudential requirements will help to maintain banking sector stability, reduce systemic risks, and ensure solvency. As a result, MNT 6.75 trillion was repaid from 213,701 borrowers affected by the Covid-19 pandemic, of which MNT 4.73 trillion was from the 107,558 borrowers whose loans restructured.

Table 1.10: Loans affected by Covid-19 (in bln MNT)

№	Loan Type	Total Loan	Loans affected by Covid-19	Share of total loans	Restructured amount	Restructured loan/ loans affected by Covid	Employment loans	Share of affected loans	Repo financing loans	Share of affected loans
	Total Loan	**20,240**	**5,138**	**25%**	**3,945**	**77%**	**1,795**	**35%**	**633**	**12%**
1	Corporate Loans	10,207	2,672	26%	1,901	71%	1214	45%	479	18%
2	Individual Loans	7,768	1,608	21%	1,318	82%	580	36%	154	10%
3	Mortgage Loans	2,265	859	38%	726	85%	-	-	-	-
4	*Mortgage MIK*	*2986*	*2487*	*83%*	*2381*	*96%*	-	-	-	-

Source: The Bank of Mongolia

The Covid-19 pandemic has affected 25 percent of total loans, resulting in 77 percent of them being restructured. Moreover, employment support loans account for 35 percent of the loans affected by Covid-19, while repo financing loans account for 12 percent.

Table 1.11: Loans affected by Covid-19 by economic sector (in bln MNT)

№	Loan Type	Total Loan	Loans affected by Covid-19	Share of total loans	Restructured amount	Restructured loan/ loans affected by Covid	Employment loans	Share of affected loans	Repo financing loans	Share of affected loans
	Total Loan	**20,240**	**5,138**	**25%**	**3,945**	**77%**	**1,795**	**35%**	**633**	**12%**
1	Mining	2,196	526	24%	405	77%	15	2.86%	5	0.91%
2	Manufacturing	1,465	332	23%	187	56%	162	49%	89	27%
3	Trade	3,967	705	18%	500	71%	1013	144%	236	34%
4	Construction	1,680	462	27%	328	71%	149	32%	40	9%
5	Real Estate	2,897	1001	35%	812	81%	7	0.72%	15	1.47%
6	Other	8,035	2112	26%	1,712	81%	448	21%	248	12%

Source: The Bank of Mongolia

The Covid-19 pandemic has affected 24 percent of mining loans, 23 percent of manufacturing loans, 18 percent of trade loans, 27 percent of construction loans, 35 percent of real estate loans, and 26 percent of retail loans.

Table 1.12: Economic sector that needs to pay attention in which most of loans affected by Covid-19 (in bln MNT)

№	Loan Type	Total Loan	Loans affected by Covid-19	Share of total loans	Restructured amount	Restructured loan/ loans affected by Covid	Employment loans	Share of affected loans	Repo financing loans	Share of affected loans
1	Manufacturing	1,465	332	23%	187	56%	162	49%	89	27%
2	Electricity, gas	75	17	22%	12	70%	15	90%	4	21%
3	Water Supply, Waste Management	25	3	12%	2	55%	5	148%	2	71%
4	Construction	1,680	462	27%	328	71%	149	32%	40	9%
5	Transportation and storage	627	180	29%	145	81%	30	17%	31	17%
6	Public administration	1	0	24%	0	75%	0	99%	0	0%
7	Other	5,178	1224	24%	980	80%	213	17%	95	8%

Source: The Bank of Mongolia

The repayment of loans restructured and affected by Covid-19 are shown below.

Table 1.13: Changes in loans affected by Covid-19 and restructured loans (December 31, 2020-December 31, 2020) (in bln MNT)

№	By type	2021.01.01	2021.12.31	Total Changes		Contribution to changes: Decreased by repayment		Contribution to changes: Newly issued	
		Amount	Amount	Amount	%	Amount	%	Amount	%
1	Loans Affected by Covid-19	8,435	5,138	-3,297	-39.08	-5,170	-61%	1,874	22%
2	Restructured Loans	5,415	3,945	-1,470	-27.15%	-3,454	-64%	1,984	37%

Source: The Bank of Mongolia

Going forward, the Bank of Mongolia will be making necessary adjustments on the phasing-out plan depending on the pandemic and economic circumstances. This is consistent with the aim of maintaining banking sector stability, reducing systemic risks, ensuring solvency, preserving capital conservation buffer and allocation of assets, and avoiding risk accumulation and solvency pressures.

1.4. GENERAL GOVERNMENT BUDGET

Government budget

In 2021, total budget structural revenue and grants totaled MNT 12,689 billion when total budget expenditure and net lending were MNT 15,598 billion, according to preliminary estimates. The government's budget deficit was MNT 2,909 billion, or 6.8% of GDP.

Table 1.14: Consolidated budget

₮, trillion	2020 Actual	2021 Amendment	2021 Preliminary	2021/2020 %, y-on-y
Total revenue	**10.4**	**13.7**	**14.3**	**37.5**
Fund revenue	1.0	1.7	1.6	60.0
Structural revenue	**9.4**	**12.1**	**12.7**	**35.1**
Tax revenue	8.5	10.6	11.3	32.9
Non-tax revenue	0.9	1.4	1.4	55.6
Total expenditure and net lending	**14.0**	**15.7**	**15.6**	**11.4**
Primary expenditure	13.0	14.8	14.8	13.8

Interest payment	1.0	1.0	0.8	-20.0
Budget balance	**-3.6**	**-2.0**	**-1.3**	**-**
% of GDP	-9.4	-4.8	-3.0	-
Structural balance	**-4.5**	**-3.7**	**-2.9**	**-**
% of GDP	-12.0	-8.8	-6.6	-
Primary balance	**-3.5**	**-2.7**	**-2.1**	**-**
% of GDP	-9.4	-6.5	-4.7	-

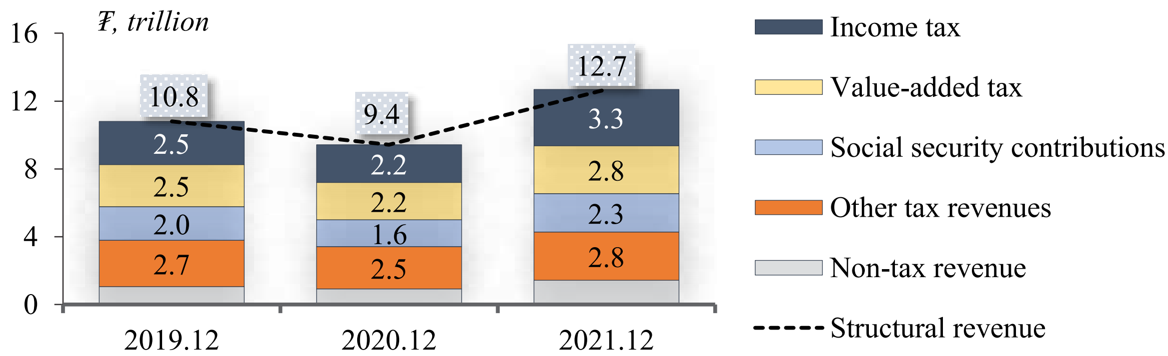
Source: Ministry of Finance

Budget revenue

In 2021, total structural revenue was MNT 12.7 trillion, up 35% year on year (27 percent, excluding Oyu Tolgoi's one-time tax revenue). Budget revenues increased for the most components from the previous year (Figure 1.32). The changes in revenue components are as follows:

- Corporate income tax revenue: + MNT 820 billion (58.8%[8]), of which MNT 600 billion is related to one-time tax revenue from Oyu Tolgoi;
- Social security contributions: + MNT 670 billion (42.3%), of which social security discounts during the pandemic decreased by about MNT 500 billion in 2021 compared to the previous year;
- Value-added tax revenue: + MNT 630 billion (28.7%);
- Personal income tax revenue: + MNT 280 billion (32.7%);
- Customs duty on imported goods: + MNT 200 billion (27.3%).

Figure 1.33: Budget revenue



Source: Ministry of Finance

Budget expenditure and net lending

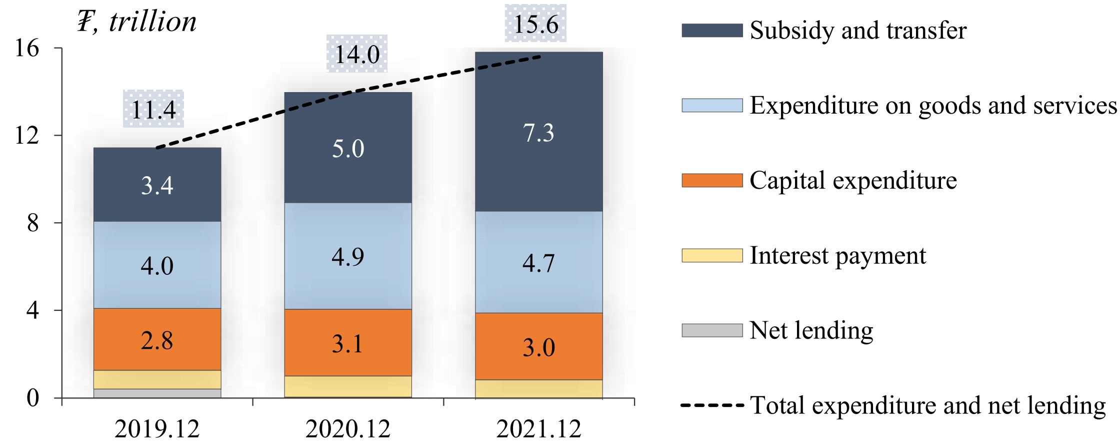
Subsidies and transfers expenditure increased by approximately 50% in 2021, according to preliminary estimates, while other expenditures stayed at 2020 levels (Figure 1.33). During the pandemic, the government implemented measures to support households' income, such as one-time allowances for all citizens, as well as increases in child allowances and welfare pensions. As a result, subsidies and transfers accounted for 47 percent[9] of total budget expenditures. Subsidies and transfer expenses have grown in comparison to the previous year in the following sub-components:

8 CIT revenue reached MNT 2.2 trillion in 2021, a surge of 58.8 percent year on year. CIT revenue growth is reduced to 15.8 percent, after excluding collection of tax revenue with disputes.

9 The average is 32 percent between 2010 and 2020.

- One-off allowance[10]: + MNT 1.0 trillion;
- Child allowance: + MNT 330 billion (32.8%);
- Pension: + MNT 120 billion (7.4%);
- Welfare pension: + MNT 20 billion (13.1%).

Figure 1.34: Budget expenditure and net lending



Source: Ministry of Finance

Sources for financing budget deficit and amortization

In 2021, a total of MNT 7.0 trillion was required to cover the government financing needs. Out of which, MNT 2.9 trillion was drawn from government's current account and deposits held at the Central bank; MNT 4.1[11] trillion was issued through "Century" bonds and foreign loans; while MNT 729 billion was financed by the Fiscal Stability Fund.

Table 1.15: Financing gap and sources of budget deficit

₮, trillion	2020	2021/2020	Change
	Actual	Preliminary	
Financing sources of budget deficit	**4.5**	**2.9**	**-1.6**
Government current account and deposits	2.1	2.2	0.0
Government bond	**-0.2**	**-0.6**	**-0.3**
Newly issued bonds	1.7	2.8	1.1
Principal payments	-2.0	-3.4	-1.4
Government loans	**2.5**	**0.6**	**-1.9**
New loans	3.2	1.3	-1.8
Principal payments	-0.7	-0.7	0.0
Stabilization Fund	0.1	0.7	0.6
Privatization of property	0.0	0.0	0.0

Source: Ministry of Finance

[10] One-off allowance amounting to MNT 300,000 per individual was issued by the government to every citizen, in accordance with implementing national state of emergency measures.

[11] A total of MNT 2.8 trillion debt was re-financed through "Century" project. In particular, Chinggis bond amounting to USD 660 million and Gerege bond amounting to USD 340 million were re-financed.

MONETARY POLICY IMPLEMENTATION

2

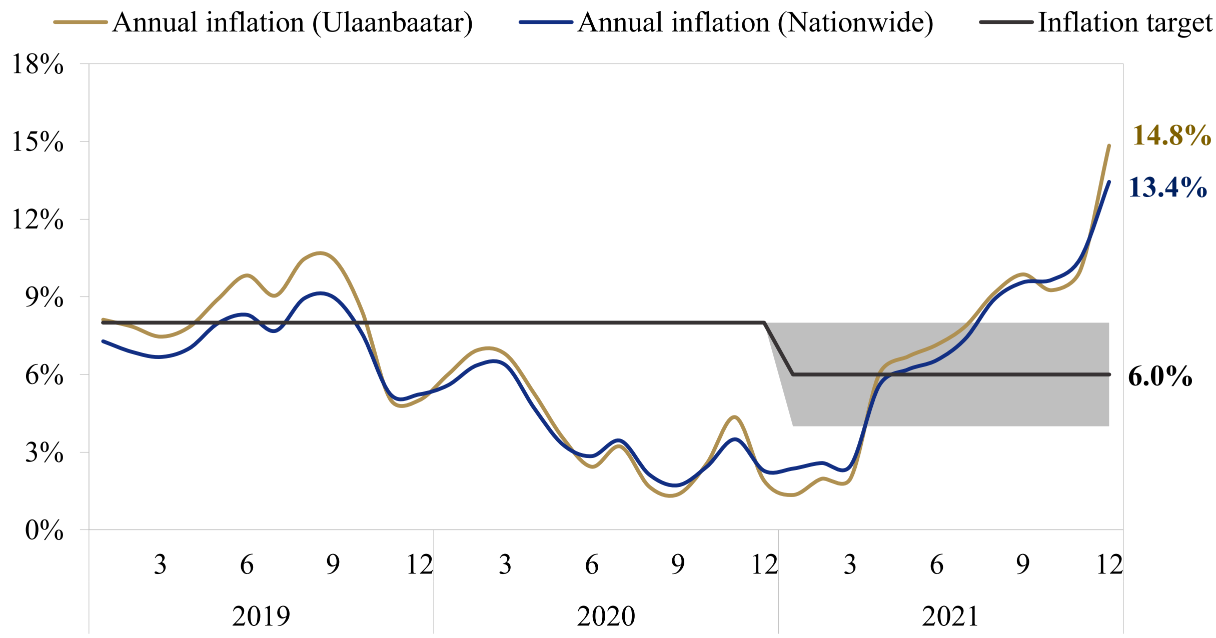
2.1 MONETARY POLICY OBJECTIVE, ACTIONS, AND RESULTS

Using market-based monetary policy instruments, inflation, measured by the consumer price index shall be stabilized around 6% with an interval of ±2 percentage points during 2021-2023.

Inflation measured by the Consumer Price Index (CPI) in December 2021 was 13.4 percent per annum nationwide and 14.8 percent in Ulaanbaatar, which was higher than the target level (6 percent (+/- 2)). Specifically, supply-driven inflation has accounted for most of the inflation in the second half of 2021 due to border constraints, the spread of infectious animal diseases, and rising transportation costs. Despite the gradual easing of the quarantine measures, economic activity and demand-driven inflation were relatively low.

The supply-driven factors, having a significant impact on inflation, can be explained as following in detail: 1) the spread of highly contagious animal diseases, which negatively affected meat prices and supply; 2) higher import prices due to the supply chain disruptions and border restrictions; 3) domestic fuel prices have risen as the world oil price increased; 4) the prices of some goods and services have increased due to the second-round effect of rising fuel and import prices; 5) a discount of refined fuel price decreased from the previous year, and wood price hiked up. It is uncertain how long the rise in global prices and transportation cost, which has increased due to the delays and congestion in international transport and logistics, will continue.

Figure 2.1: Annual inflation



Source: NSO

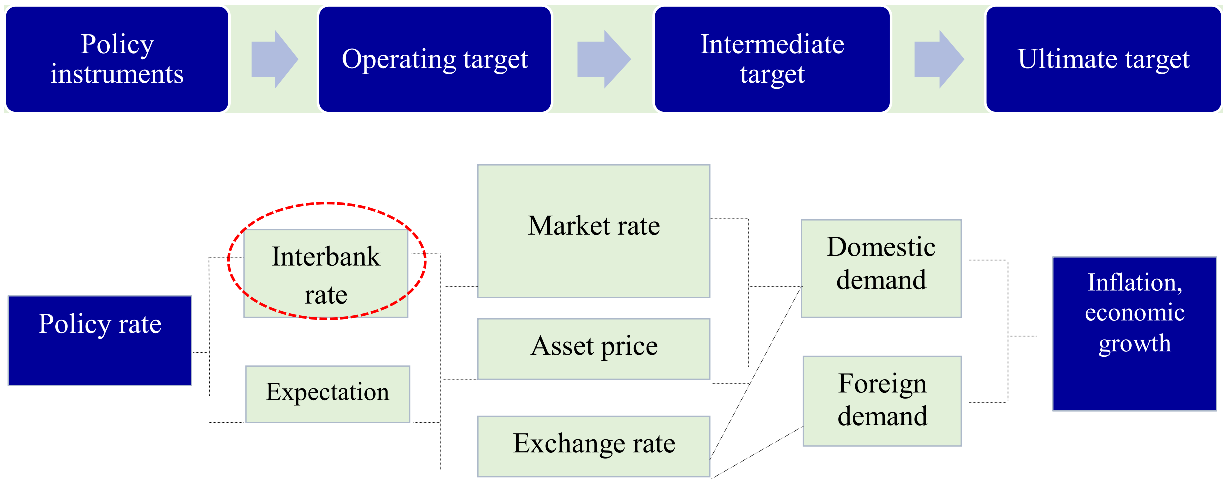
In the first half of the reporting year, monetary policy was aimed to alleviate financial difficulties and pressures of the Covid-19 pandemic within the economy and to support economic recovery without compromising inflation targets in the medium term. Although prices for some goods and services increased due to supply-side factors, inflation was around the target range in the first half of the year. As of June 2021, annual inflation was 6.6 percent nationwide and 7.1 percent in Ulaanbaatar and expected to stabilize around the central bank's target level in the medium term. Even though the economy started to recover, the decision was made to keep the policy rate unchanged at the historical low level of 6 percent, as recovery remained dissimilar among economic sectors and their outlook was uneven, and the uncertainty was high due to the domestic spread of the Covid-19 virus. In addition, Monetary Policy Committee (MPC) expanded the scope of long-term repo financing to include service and trade enterprises with more than 200 employees at their meeting in the first quarter of 2021. The decision aims to eliminate the overlap of loans to small and medium enterprises under the Job Support Program of the Government of Mongolia, increase the effectiveness of repo financing, and further support economic and business activity. Subsequently, it was decided to provide long-term repo funding of MNT 250 billion, MNT 350 billion, and MNT 250 billion in the first three quarters of 2021 respectively. Also, to support the economy and reduce the debt burden of borrowers, the interest rate on repo financing was reduced by 0.5 percentage points.

In the second half of the year, two new variants of the Covid-19 virus spread around the world, oil prices soared, border restrictions tightened under the China's Zero-Covid policy, supply chains were disrupted, logistics delayed and transportation costs surged. These were intensified uncertainty of external and domestic economy, as well as risk of higher cost-push or supply-driven inflation. Therefore, policy decisions were made taking into account the prospects for economic recovery, inflation expectation and the risks that may arise in keeping the inflation target. More specifically, annual headline inflation reached 8.9 percent nationwide and 9.1 percent in Ulaanbaatar city as of August 2021, and it was mainly driven by base year effects, international supply disruptions and logistic delays. Even though the headline inflation increased due to the supply shocks, it was projected to stabilize around the central bank's target in the second half of 2022 because border restrictions were expected to be resolved in the short term as a part of the two countries' cooperation. Furthermore, global economic growth has accelerated, and the prices of exporting goods have remained high, but its positive impact on domestic economy remained less than expected, and labor market activity was weak and economic recovery varied across sectors due to the spread of new variants of virus, and its uncertainty. Therefore, the MPC decided to keep the policy rate unchanged in the third quarter of 2021, and to reduce the amount of long-term repo financing from the previous quarters to MNT 100 billion in the fourth quarter of 2021. At the last MPC meeting in 2021, annual headline inflation reached 10.5 percent nationwide and 10.0 percent in Ulaanbaatar city as of November 2021, which was higher than our previous forecast. The rise in inflation was mainly attributable to the supply-driven price increases, induced by border constraints, the spread of infectious livestock diseases and rising transportation costs. The supply chain disruptions, border constraints and hikes in food and fuel prices beyond expectations may lead to the risk of inflation not returning to the expected lower level. Therefore, a decision was taken to expand the targeted purpose of long-term repo financing instruments to help increase the stockpile of fuel and main food products up to the required level. In addition, the MPC decided to keep the policy rate unchanged at 6 percent because growth outlook was revised down for two consecutive quarters, a household consumption did not recover, and uncertainty in the global and domestic economic environment remained high. As the headline inflation has exceeded the central bank's target, the MPC members decided to set the repo financing interest rate at 0.5 percentage points higher than the policy rate as part of policy adjustments, also they increased reserve requirement on liabilities in foreign currency by 3 percentage points to 18 percent to prevent the risk of dollarization. Finally, the MPC announced that the central bank will adjust its monetary policy stance in a timely manner in line with the developments of economic recovery and inflation outlook.

Money market and interest rates

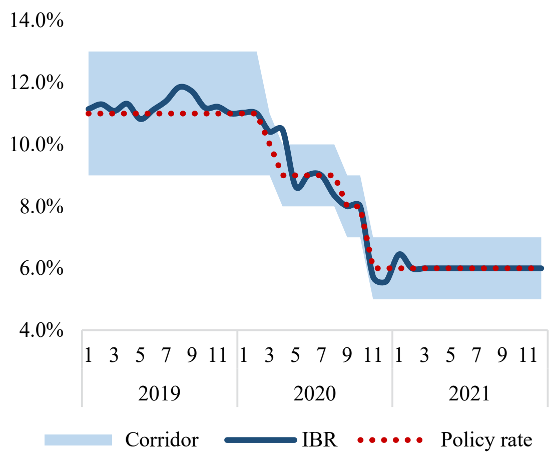
The interest rate in the interbank market influence the banks' decision to either issue the loan or to make a deposit from its' customers. Thus the Bank of Mongolia implements the monetary policy through the monetary policy instruments including open market operations and standing facilities that are consistent with the interest rate corridor, with an aim for maintaining the interbank rate to be close to the policy rate which facilitates the monetary policy transmission mechanism.

Figure 2.2: The monetary policy transmission mechanism



Source: The Bank of Mongolia

Figure 2.3: IBR



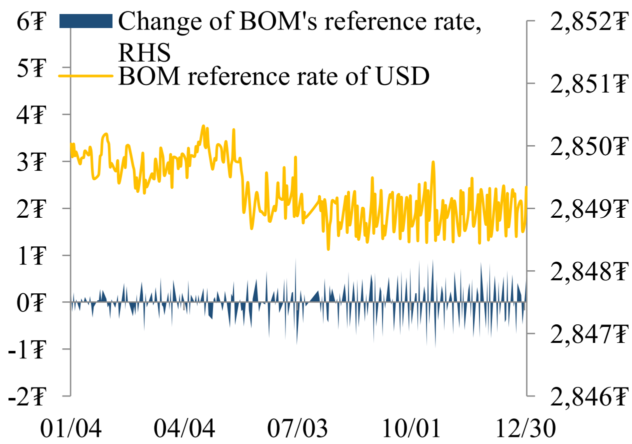
Source: The Bank of Mongolia

The policy rate had been gradually cut to a record low of 6.0 percent in 2020 and continued to be maintained throughout 2021 to reduce the adverse impact of the COVID-19 pandemic on the economy. As a result, the interbank interest rate decreased by 2.8 percentage to reach 6.0 percent in 2021 and average absolute deviation of interbank rate from policy rate has reduced to 0.0 basis point (Figure 2.3).

Exchange rate

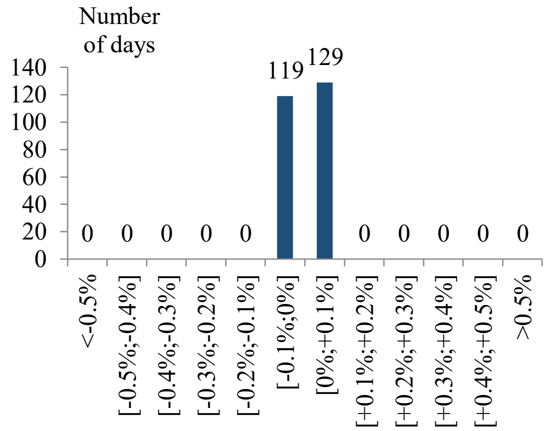
Compared to the beginning of the year, the MNT's reference rate against the USD has reached 2849.34, appreciated by 0.019 percent (Figure 2.4). Due to interventions in the domestic foreign exchange market to mitigate the exchange rate fluctuations and short-term demand and supply gap, the average daily exchange rate volatility was 0.011 percent in the reporting period, which was at a stable level. The highest daily depreciation and appreciation rates were 0.033 percent (0.95 MNT, decreased by 3.80 MNT compared to last year) and 0.035 percent (0.99 MNT, decreased by 1.07 MNT compared to last year), respectively. Moreover, the exchange rate fluctuation was within the range of ±0.1 percent (Figure 2.5).

Figure 2.4: The volatility of the Bank of Mongolia's reference rate of MNT/USD (by MNT)



Source: The Bank of Mongolia

Figure 2.5: Histogram of daily changes of the Bank of Mongolia's reference rate of MNT/USD



Source: The Bank of Mongolia

2.2 ANTI-MONEY LAUNDERING AND COMBATING THE FINANCING OF TERRORISM REGIME

I. Measures taken to exclude Mongolia from the European Union's list of high-risk third countries with strategic anti-money laundering and combating the financing of terrorism deficiencies

Mongolia was included in the list of jurisdictions with strategic anti-money laundering and combating the financing of terrorism (AML/CFT) deficiencies or so-called "Grey list" by the Financial Action Task Force (FATF) on October 18, 2019. In this regard, the European Union (EU) has added Mongolia to its list of high-risk third countries with strategic AML/CFT deficiencies, known as the EU's "Blacklist" on October 01, 2020. Therefore, in order to exclude Mongolia from the EU's list, the Financial Information Unit (FIU) has organised necessary meetings with the EU through the Ministry of Finance and the Ministry of Foreign Affairs virtually and provided progress updates on the actions taken to improve AML/CFT regime.

As a result of our continuous efforts and Mongolia's removal from the FATF's list of increased monitoring on October 13, 2020, the European Commission published a Directive No. 2015/849 on January 18, 2021 and excluded Mongolia from the EU's list of high-risk third countries with strategic AML/CFT deficiencies.

The removal of Mongolia from the EU's list of high-risk third countries is expected to have positive effects on such as establishing business relations with banks and financial institutions of EU member states, making cross-border transactions faster and increasing the opportunities to implement EU-funded projects and programs.

II. Measures taken to improve technical compliance ratings of FATF 40 Recommendations

Mongolia reports its technical compliance updates on the FATF 40 Recommendations, known as the international standards on combatting money laundering and terrorist financing, as well as the financing of proliferation of weapons of mass destruction, to the Asia/Pacific Group (APG) on Money Laundering on an annual basis.

In this regard, the Financial Information Unit (FIU) in cooperation with the member organizations of the AML/CFT National Council and Cooperation Council prepared a Follow-Up Report 2021 of Mongolia and submitted it to the APG on February 01, 2021. The FIU has developed a work plan to prepare the report and organized a total of 5 virtual meetings with the officials in charge.

This Follow-Up Report contains detailed information on actions taken and progress made to upgrade the ratings of FATF Recommendations 1, 8 and 15 which were rated as "Partially compliant". With regards to the Follow-Up Report, we have provided additional information and clarifications to the APG assessment team for a total of 5 times on a timely basis and organized a joint virtual meeting to discuss the report.

The Follow-Up Report 2021 of Mongolia was discussed and adopted at the APG Mutual Evaluation Committee meeting virtually held on July 13, 2021 and officially published on the APG's website on August 13, 2021.

It was concluded in the report that Mongolia has taken an active approach to effectively implement AML/CFT risk-based approach. Thus, rating of the Recommendation 1 was upgraded from Partially Compliant to Largely Compliant by the APG. The technical compliance ratings of Recommendations 8 and 15 were remained the same as it was deemed necessary to strengthen the relevant legal and regulatory framework (Table 2.1):

Table 2.1: Ratings of Follow-Up Report 2021 of Mongolia

№	FATF Recommendation	Previous rating	Current rating
1	Risk assessment	"Partially compliant"	**"Largely compliant"** (↑)
8	Non-profit organizations	"Partially compliant"	**"Partially compliant"** (=)
15	New technologies	"Partially compliant"	**"Partially compliant"** (=)

Source: FIU, Bank of Mongolia

In the Follow-Up Report 2021 of Mongolia, we have reported following measures taken to upgrade the technical compliance ratings of Recommendations 1, 8 and 15:

Recommendation 1: Countries shall identify and assess their money laundering and terrorism financing (ML/TF) risks and apply a risk-based approach under this Recommendation. In this regard, the FIU has initiated and conducted ML/TF National Risk Assessment of Mongolia in cooperation with the responsible public and private institutions in accordance with the AML/CFT Law. In addition, "AML/CFT Preventive Measures Regulation" was amended by the Decree No. A-31 of the Governor of the Bank of Mongolia on January 27, 2021. As a result, reporting entities are allowed to apply simplified due diligence for customers identified as low risk by the risk assessment.

Recommendation 8: Measures taken to improve legal environment of non-profit organization (NPO) sector, to conduct its ML/TF risk assessment, to establish a risk-based supervisory framework, to organize outreach activities, and to increase the investigations and prosecutions in the NPO sector were included in the Follow-Up Report. For instance, FIU, Ministry of Justice and Home Affairs, National Counter Terrorism Council and other relevant organizations have conducted the ML/TF risk assessment of the NPO sector. Moreover, in order to establish legal environment in this sector, FIU has cooperated with relevant authorities to develop and adopt the draft laws on Legal Status of Association and Fund. The adoption of these laws will help to establish legal, regulatory and supervisory framework in the NPO sector.

Recommendation 15: In order to implement the requirements of this Recommendation on new technologies, Bank of Mongolia, FIU, Financial Regulatory Commission and Ministry of Justice and Home Affairs have cooperated to draft a Law on Virtual Asset Service Provider (VASP). The draft law was submitted to the

Parliament by the Government and further discussions of the draft law were supported at the Parliament on June 17, 2021. Thus, Standing Committee of the Parliament established a working group to prepare the draft laws on VASP and amendments to the relevant laws for further discussions. A sub-working group was formed to provide technical assistance to the working group which consisted of more than 30 representatives from the public and private sector institutions including Bank of Mongolia and FIU. In this regard, we have conducted necessary research on establishing legal framework in the virtual asset sector and international best practices. The VASP Law was approved by the Parliament of Mongolia on December 17, 2021. The approval of this law will create legal environment for the virtual asset sector in Mongolia and help implement the requirements of the FATF Recommendations, prevent from ML/TF risks, establish supervisory framework for VASPs, identify them as reporting entities under the AML/CFT Law and have VASPs that meet the set standards.

To ensure effective implementation of the Recommendation 15, Bank of Mongolia, FIU, Ministry of Justice and Home Affairs, Financial Regulatory Commission, law enforcement and other relevant agencies have jointly conducted ML/TF risk assessment of virtual asset sector and reported its findings to the APG. In relations to the approval of the VASP Law, FIU has presented the importance of updating the risk assessment using the World Bank methodology at the Financial Stability Council meeting held on December 13, 2021 and the Council decided to establish a working group responsible for the risk assessment.

Box 1. Guidance on virtual asset sector

In accordance with the FATF Recommendation 15, countries should regulate the virtual asset sector and manage and mitigate the associated ML/TF risks. Virtual asset and virtual asset service provider sector is a newly emerging market not only in Mongolia, but also around the world. Therefore, in order to promote the approval of the VASP Law, FIU has developed "Guidance on Virtual Assets Overview, Market and Regulation" in November 2021 for internal use and disseminated to the relevant authorities to increase their awareness and knowledge about this sector. This guidance covers terminologies used in the virtual asset sector, such as distributed ledger technology, blockchain, cryptocurrency and coins. Also, it provides the overview of the market participants, international and Mongolian market situation of the virtual asset sector, and risks of abusing virtual assets for criminal use as well as the FATF Standards.

As indicated in the Follow-Up Report 2021 of Mongolia, a total of 38 Recommendations out of FATF 40 Recommendations have been rated as Compliant or Largely Compliant. The technical compliance rating of each FATF Recommendation is shown below (Table 2.2):

Table 2.2: Mongolia's technical compliance ratings of FATF 40 Recommendations

(C-compliant, LC-largely compliant, PC-partially compliant, NC-non-compliant)

R.1	**R.2**	**R.3**	**R.4**	**R.5**	**R.6**	**R.7**	**R.8**
LC	LC	LC	LC	LC	LC	LC	PC
R.9	**R.10**	**R.11**	**R.12**	**R.13**	**R.14**	**R.15**	**R.16**
LC	LC	C	LC	LC	C	PC	LC
R.17	**R.18**	**R.19**	**R.20**	**R.21**	**R.22**	**R.23**	**R.24**
LC	LC	LC	LC	C	LC	LC	LC

R.25	R.26	R.27	R.28	R.29	R.30	R.31	R.32
LC	LC	LC	LC	C	C	C	LC
R.33	**R.34**	**R.35**	**R.36**	**R.37**	**R.38**	**R.39**	**R.40**
LC	LC	LC	C	C	LC	LC	LC

Source: FIU, Bank of Mongolia

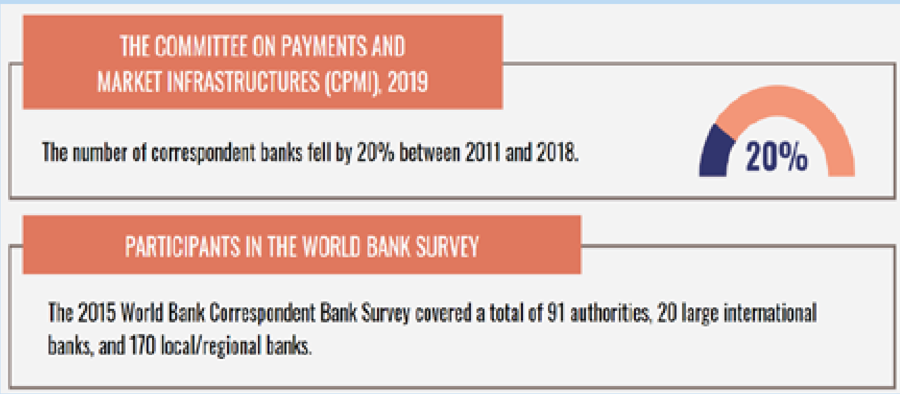
In order to effectively implement the FATF 40 Recommendations and to upgrade their ratings, FIU has updated the "Action plan to address the AML/CFT deficiencies in technical compliance of the FATF 40 Recommendations". The action plan was approved by the Chairman of the National Council, who also serves as the Minister of Justice and Home Affairs, on September 27, 2021, and member organizations of the Council are obliged to ensure its implementation. The National Council discussed the implementation of the action plan during its meeting held on December 23, 2021 and decided that responsible authorities should prepare the Follow-Up Report 2022 of Mongolia and submit it to the APG by February 01, 2022.

Box 2. International correspondent banking relationship and its importance

FATF Recommendation 13 sets out the requirements for the implementation of cross-border correspondent banking relationships by financial institutions. In this regard, the FIU has conducted a research on the current state and trends of international correspondent banking as studied by international organizations.

The correspondent banking relationship enables banks to access financial services in different jurisdictions, and to provide cross-border payment services to their customers, and further promotes international trade and financial inclusion. Since the financial crisis in 2008, correspondent banking relationships around the world have declined and there have been a number of restrictions in relations to the de-risking purposes. In particular, several banks have reduced the number of their formed correspondent relationships and established a few new ones (BIS, 2016).

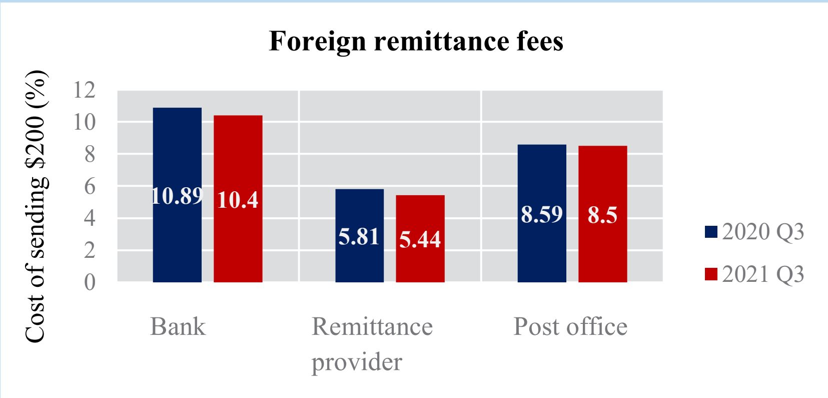
The most important factor influencing the current international correspondent banking relationship is de-risking. De-risking refers to the phenomenon of financial institutions terminating or restricting business relationships with clients or categories of clients to avoid, rather than manage, risk (US Department of State). Due to de-risking, correspondent banking relationships in the United States, the United Kingdom, and Australia have shrunk considering the low profitability, potential adverse effects on business reputation and enhanced AML/CFT supervision. In terms of international correspondent banking relationships, banks have been taking AML/CFT preventive actions in line with the regulatory measures.



A World Bank survey indicated a number of key factors that led to the cutbacks of international correspondent banking relationships (World Bank, 2015). The majority of the participants responded that they are withdrawing their correspondent banking relationship because it is not profitable enough. Furthermore, correspondent banking relationship has declined due to its high inherent risk, changes in legislations and supervisory measures, and ML/TF risk exposures.

Recent Trends in Correspondent Banking Relationships

- *Decline in nostro accounts:*
  A nostro account is a bank account held in a foreign country by a domestic bank. Correspondent banks use nostro accounts to make foreign exchange transactions. Another major trend in international correspondent banking is the decline in Nostro accounts. Latin America and the Caribbean have been hit hardest by this trend.
- *Increase in the cost of remittance services:*



  As stated in the Remittance Prices Worldwide, quarterly report issued by the World Bank, the average cost of sending $200 worldwide in the Quarter 3 of 2021 was $12.6 or 6.3% of the total amount sent (World Bank, 2021). According to the latest survey, the East Asian region has the lowest cost of receiving money (4.49% of the total amount), while the South African region has the highest cost of receiving money (8.27% of the total amount). As a result, banks remain the most expensive type of service provider in terms of remittance costs (10.40% of the total amount).

In conclusion, the current trend of correspondent banking relationships indicates that high volume of expenses, enhanced regulatory requirements and expected high risks have been adversely affecting the profitability of the correspondent activities and thus, limiting the opportunities to further improve the correspondent relationships and creating unfavorable conditions. In particular, this is a business highly influenced by economies of scale, where some banks are struggling to cover their compliance costs with their returns. The perception is that this line of business has shifted from being a low-risk/low-margin segment to a high-risk/low-margin one.

2.3 POLICY IMPLEMENTATION TO MAINTAIN BANKING SECTOR STABILITY

Banking Sector Reform Program

In 2021, the following activities were carried out within the framework of the "Banking Sector Reform Program to Create a Healthy, Reliable, Transparent, Open, Publicly Controlled, Accessible and Digital Banking System" approved by the Governor of the Bank of Mongolia Order No. A-366 of 2020.

Objective 1: Improve the legal environment for effectively decentralizing the banking sector, enhancing the corporate governance of banking activities and creating a transparent, open and publicly controlled banking system.

Amendments to the Banking Law, **the Law on Procedures for Enforcing the Law on Amendments to the Law on Banking and the accompanying Law on Banking** with the concept of reorganizing systematically important banks into open joint stock companies and other banks into joint stock companies, reducing the concentration of bank shares, creating a balance of ownership, management and control, and strengthening sound banking governance was discussed and approved by the Parliament of Mongolia on January 29, 2021.

According to this regulation of the Banking Law, the form of bank ownership should be changed to a joint stock company. This will improve the bank's management, supervision and governance, which will help protect the interests of depositors and customers and ensure the stability of the financial sector.

The relevant regulations and methodologies of the Banking Law have been amended and approved.

- By the order No. A-86 of the Governor of the Bank of Mongolia dated March 22, 2021 the "Regulation on the procedures for nomination, appointment and dismissal of an independent member of the Board of Directors of the Bank" was approved. The regulation defines the requirements and principles to be followed by an independent member of the Board of Directors of a joint stock company, and its reporting policy to the Bank of Mongolia.
- By the joint order No. A-90/85 of March 26, 2021 of the Governor of the Bank of Mongolia and the Chairman of the Financial Regulatory Commission the "Temporary regulation on procedures for developing, implementing, reporting and monitoring the reorganization of the bank into a joint stock company, the plan to change the structure of shareholders and the amount of share capital" was approved. Pursuant to this regulation, banks submitted a plan to reorganize into joint stock companies by July 1, 2021, and to change the amount and structure of share capital to the Bank of Mongolia and the Financial Regulatory Commission. The Bank of Mongolia is responsible for monitoring implementation of these plans;
- By the order No. A-104 of the Governor of the Bank of Mongolia dated April 19, 2021, the "Methodology for Identifying Systemically Important Banks" was approved, and based on this methodology, Order No. A-105 of the same day updated the list of systemically important banks. This list identified banks that are to be reorganized into open joint stock companies in accordance with the amendments to the Banking Law;
- By the order A-262/262 of the Governor of the Bank of Mongolia and Chairman of the Financial Regulatory Commission dated October 5, 2021, the "Procedure for approving changes in the share capital and shareholder structure of a joint stock company" was approved. This regulation regulates issues pertaining to changes to the amount of share capital of a bank in the form of a joint stock company when obtaining permission from the Bank of Mongolia to change the structure of shareholders and notifying the Bank of Mongolia.
- According to the Law on Amendments to the Banking Law, systemically important banks are obliged to be reorganized into open banks, and other banks into joint stock companies. In this context, Bogd Bank became the first bank to voluntarily register its shares with the authorities in the 2021Q4, fulfilling its IPO and successfully complying with the law.

Objective 2: Continue to bring the banking supervision and regulatory instruments in line with international standards and establish a healthy and reliable banking system.

The legal framework of funding bank resolution measures was set up by "Regulation on Bank Stabilization Fund" in 2021 which is based on related articles of the Banking law. Accordingly, the fund has been permitted necessary legal ground to collect contributions on an ex-ante basis from systemically important banks (SIB).

Over the past 20 years, a risk-focused banking supervision framework and a bank deposit insurance system have become two pillars of risk mitigation schemes for bank customers, depositors, lenders, and shareholders. The launch of the Bank Stabilization Fund is formed as a tool, the third pillar of the banking sector stability.

Consequently, bank resolution measures shall be financed by banking system resources. The main purpose of the fund is to ensure the stability of the banking sector by necessary financing of bank resolution measures by ex-ante and extraordinary contributions raised only from the banking system, without spending taxpayers' money in case of resolution of systemically important banks.

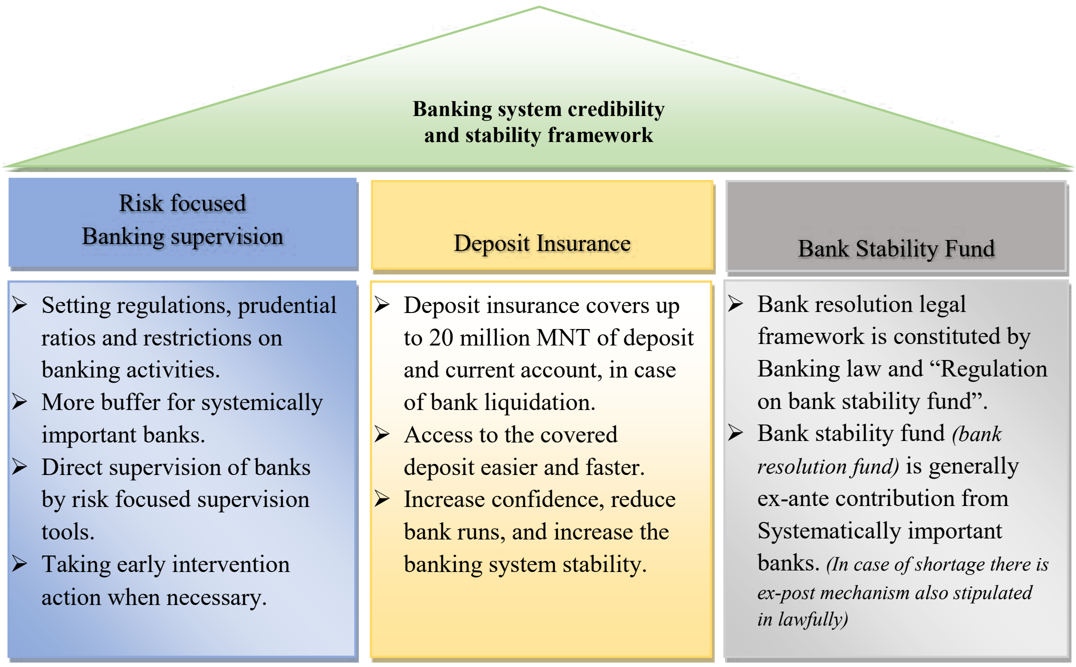
Bank's insolvency, bankruptcy, and resolution is always shocking and adverse effects to the financial markets and the public. Therefore, prompt and transparent solutions of bank enforcement measures can be reducing the public fears and anxieties, it could be useful for the stability of the banking and financial system.

Bank resolution measure is mostly required financial injection. However, there was no pre-established dedicated fund for it, in Mongolia. If the fund will be reached its target level, funding necessary for implementation of resolution measures would not be require finance from the Bank of Mongolia and Government that used to last cases.

Over the past 20 years, the establishment of a risk-based supervision framework and a bank deposit insurance system has become two pillar of risk mitigation scheme for bank customers, depositors, lenders and shareholders. The launch of the Bank Stabilization Fund is formed as a tool, the third pillar of the banking sector stability.

In Mongolia, risk focused banking supervision and deposit insurance framework were two pillars of regulatory support and credibility approach for reduction and mitigation of potential risks to the public from banking system. The establishment of the **Bank Stabilization Fund shall be** launch of a new and additional approach of banking system stability and it can be **the third pillar** of the framework. Figure 2.6.

Figure 2.6: Supporting three pillars of banking sector stability framework



Source: The Bank of Mongolia

Projects and programs implemented by the Bank of Mongolia joint with the Government

To mitigate the negative impact of the Covid-19 pandemic on the economy, the government approved and gradually implemented the "10 trillion MNT Economy Recovery and Health Protection Integrated Plan" by decree No. 42 on February 17, 2006. The action plan's set of measures aims to reduce credit risk for banks while also supporting business activities, employment, the agricultural sector, construction, and related industries.

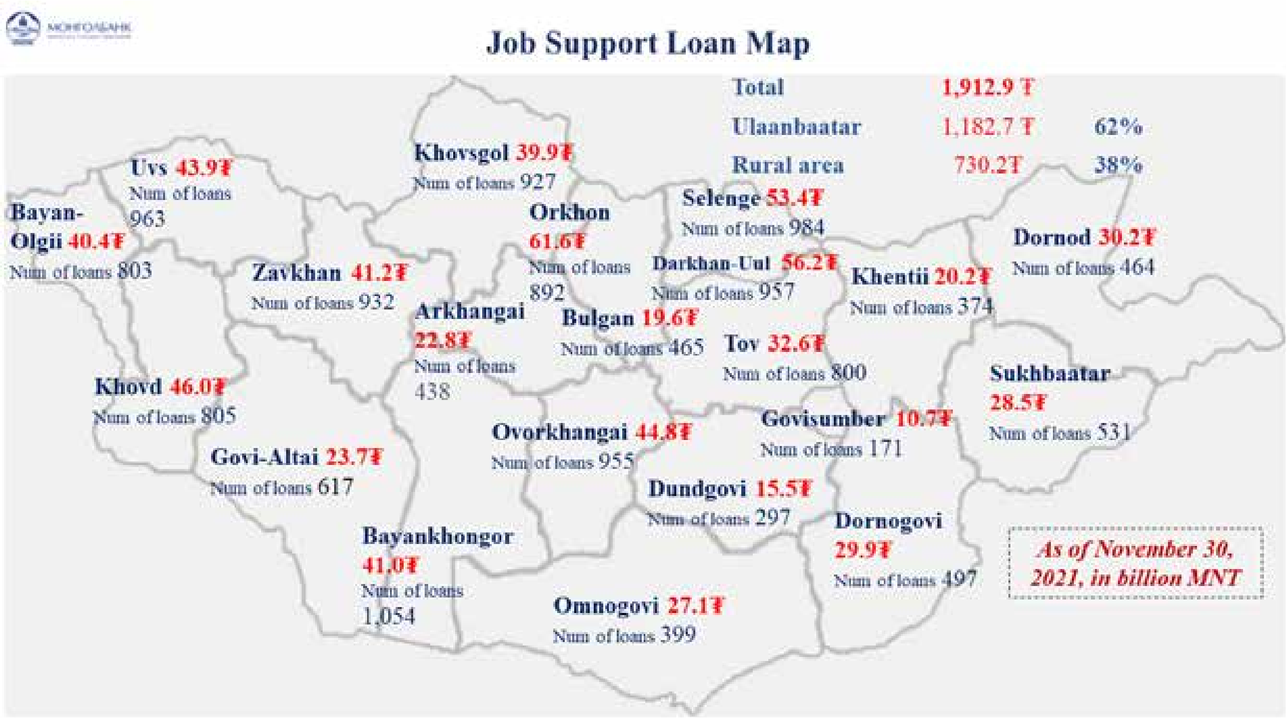
As part of the integrated plan, the Bank of Mongolia is collaborating with relevant organizations with monitoring functions to provide "Workplace Support Loans" in Section 2.1, "Mortgage Loans" in Section 2.3, "Repo Financing Loans" in Section 2.4, and "Agricultural Support Loans" for spring planting, wool and cashmere processing, and "Herder Support Loans" to support herders in Section 2.5, all of which are based on funding in the banking sector. To provide interest rate subsidy to individuals and businesses who borrowed such loans, the Bank of Mongolia has been collaborating with related institutions in a role as financial intermediary of government and monitoring banking activity.

From a total of MNT 6.5 trillion scheduled, MNT 4.3 trillion loans was issued to 62,733 borrowers with a 66 percent completion rate, maintaining 144,860 jobs for individuals and enterprises.

Job Support loans

As of December 31, 2021, 62,965 loan applications worth MNT 6.4 trillion were submitted to banks, of which 25,439 borrowers received MNT 1,952.6 billion, with an implementation rate of 97.6 percent. To specify, loans worth MNT 1,293.4 billion were issued to 5,673 enterprises, and MNT 659.1 billion were issued to 19,766 individuals, supporting total of 108,238 jobs. In addition, 208 loans worth MNT 28.2 billion were issued through the Credit Guarantee Fund, which accounted for 60 percent of the corporate loan principal.

Figure 2.7: Job Support Loan as of November 30, 2021 (in Billion MNT)

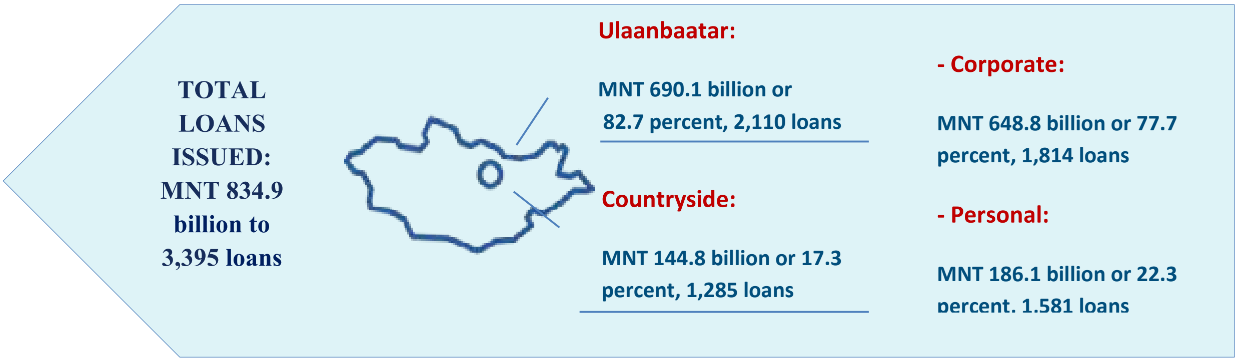


Source: The Bank of Mongolia

Repo financing loans

As of December 31, 2021, 3,395 borrowers were issued MNT 834.9 billion through the "Repo financing loans" program which supports manufacturing, service providers, and non-mining export products. Of which, MNT 186.1 billion was issued to 1,581 individuals, and MNT 648.8 billion was issued to 1,814 business entities, whit supporting a total of 36,622 jobs.

Figure 2.8: Repo Financing Loans



Source: The Bank of Mongolia

Agricultural loans

Loans equal to a total of MNT 494.3 billion were issued to 20,607 customers, including spring planting for agriculture, wool, leather, cashmere, meat stockpiling, wheat procurement, and herder support. MNT 270.7 billion were issued to 20,221 rural customers, while MNT 223.6 billion went to 386 Ulaanbaatar customers. In detail, loans for supporting herders accounted for 40.4 percent of total loans, or MNT 199.6 billion; loans for spring planting accounted for 8.8 percent, or MNT 43.3 billion, loans for cashmere preparation accounted for 19.2 percent, or MNT 94.9 billion; and loans for wheat and oilseeds accounted for 8.6 percent or MNT 42.4 billion, loans for meat storage accounted 19.7 percent, while MNT 13.8 billion were loans for leather procurement and wool procurement loans.

Table 2.3: 31st December, 2021 (in Billion MNT)

№	Loan Type	Loan Amount	Count	End Date
1	Cashmere preparation	94.9	38	2021/07/30
2	Wool preparation	3.2	4	2021/09/30
3	Leather preparation	13.2	9	2021/12/30
4	Spring planting	43.3	629	2021/10/31
5	Meat stockpiling	97.6	46	2021/12/31
6	Wheat and oilseed	42.4	11	2021/12/31
7	Herder's support	199.6	19,870	2021/12/31
	Total	**494.3**	**20,607**	

Source: The Bank of Mongolia

2.4 MANAGEMENT OF FOREIGN EXCHANGE RESERVE

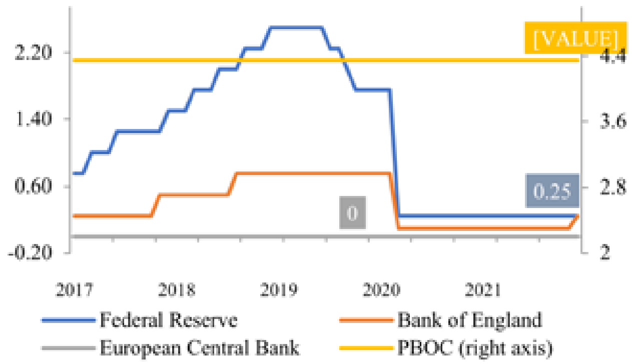
Subject to Article 21 of the Law on the Central Bank of Mongolia, the Bank of Mongolia implements foreign exchange reserve management to seek returns only after ensuring liquidity and security of the foreign exchange reserves. The structure of the foreign exchange reserve management is aimed at creating a monitoring system consistent with international standards, which determines the rights, responsibilities, and supervision of the parties involved with its management.

In 2021, the Bank carried out their foreign exchange reserve management in line with the generally accepted asset management principles and within the scope of established risk limits. In terms of the general structure, the Bank determines their foreign currency asset and investment composition, optimal investment duration, and eligible financial instruments.

The COVID-19 pandemic situation has slowed global economic growth and destabilized the international investment environment. The major central banks have maintained a loose monetary policy and supported economic growth amid trade disputes and political uncertainty.

The Federal Reserve Bank, European Central Bank and The Bank of England kept its policy rate near 0 while other major central banks have maintained its policy rate (Figure 2.9).

Figure 2.9: Central Bank rates (%)

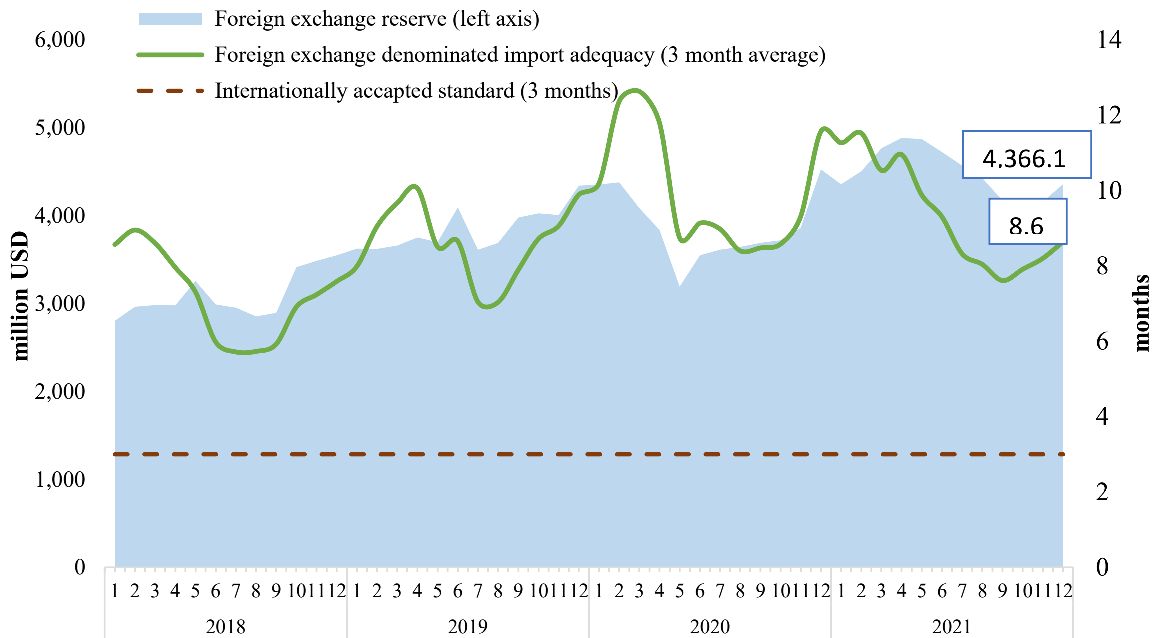


Source: The Bank of Mongolia

During the fiscal year, the Bank prioritized its assets' security by investing in major reserve currencies, allocated and unallocated gold, current and deposit accounts with highly regarded central banks such as the Federal Reserve System, the Bank of Japan, the Bank of England, and the Bank of France, as well as money market instruments issued by the Bank for International Settlements and other supranationals. Meanwhile, the investment portfolio consists of 0-5 year US Treasury bonds and Supranational bonds, which earned a higher return than the international benchmark in 2021.

The Bank of Mongolia purchased around 20.8 tons of gold from the domestic market in 2021, which decreased by 12 percent compared with the last year. The main reason for the increase in gold purchasing for last 2 years was the COVID-19 pandemic situation. Due to the favorable gold price in the international market, the gold reserve was managed above the benchmark level within the approved deviation.

Figure 2.10: Foreign Exchange Reserves (in million USD) and Adequacy (monthly)



Source: The Bank of Mongolia

The Bank of Mongolia carried out its foreign exchange reserve management in line with investment composition, optimal investment duration, and within the scope of established risk limits. As of December 31, 2021, the Foreign exchange reserves reached USD 4,366.1 million, decreased by 3.71 percent or USD 168.2 million from the beginning of the year. This result illustrated to:

- 34.6 weeks or 8.6 months of foreign currency-denominated import payment of last 3 months average,
- 26.5 weeks or 6.6 months of foreign currency-denominated import and service payment of last 3 months average,

The current level of foreign exchange reserve adequacy is 2-5 months higher than the internationally accepted standard that requires reserve to be equal to 12 weeks or 3 months of foreign currency-denominated import payment (Figure 2.9). The foreign exchange reserve level does not meet the National Security concept adopted by the Parliament on 15 of July 2010, which requires maintaining foreign exchange reserve at a level not less than the annual foreign currency-denominated import payment.

2.5 PAYMENT SYSTEM OF MONGOLIA

As part of its effort to develop the national payment system, the Bank of Mongolia received the Bloomberg TV Mongolia Awards 2021 for the Innovation of the Year for successfully converting the national payment T-card into EMV chip technology, which currently accounts for around 60 percent of payment card market. With the introduction of this technological innovation, the privacy and security of the T-card has reached international standards, and the card information can be tokenized to make low-cost transactions, such as public transportation, parking, and tolls remotely. In relation to it, ISO / IEC 7816-5: Integrated circuit cards-Registration of application providers has been approved as a national MNS standard, and T-card chips allow customers to develop and use personal and financial information in an application adapted to their country's payment system.

To keep up with the fast pace of technological innovation and support introduction of new technology-based products, services, and business models of financial services markets, the "Regulation for Regulatory Sandbox" was approved by the joint order of the Governor of the Bank of Mongolia, the Minister of Finance, the Chairman of the Financial Regulatory Commission, and the CEO of the Deposit Insurance Corporation. The purpose of this regulation is to support Fintech startups to test their products and services in a safe environment for a defined period. In line with this, the Bank of Mongolia established an Innovation Office in 2021, which provides an environment for Fintech to introduce innovative products and services to the public, exchange views on the legal environment and infrastructure solutions, and, if necessary, test software and hardware.

Moreover, the "QR code message structure and instructions" have been approved by the Governor of Bank of Mongolia, and all payment system participants will be able to use them starting in May 2022. According to this standard, no fees will be charged from customers for their purchase transactions using a QR code. As a result, new, high-tech payment channels that satisfy international standards enable payments to be made in an easier, faster, and more secure way.

It should also be noted that the COVID-19 pandemic, technological advances, and other economic impacts have accelerated the digitization of payments around the world. According to the statistics, the daily average of payment card transactions increased from 555,000 in 2020 to 827,000 in 2021 with 49 percentage increase compared to the previous year. The daily average of low value transactions rose by 52 percent totaling 268 thousand transactions in 2021 compared to 177 thousand in 2020. This digital payment shift is also being observed in our country aided by the current infrastructure that allows customers to choose from a number of convenient financial services, such as contactless card payment, internet banking, mobile banking, and QR code transactions.

During the period of state of readiness, the Bank of Mongolia decreased the fee for low-value (real-time) interbank transactions to MNT 200. This decision will exempt customers from certain fees, enable them to make payments through electronic channels, and therefore, ensure the reliability, efficiency, and security of the national payment system, and increase the transaction capacity.

Another major decision was to increase the maximum transaction limit for low-value interbank payment systems through the Automatic Clearing House System (ACH+) from MNT 3 million to MNT 5 million. This decision to raise the maximum transaction limit for low-value interbank payment was based on our research focusing on a number of factors, such as system overload, risk, MNT exchange rate, and average salary. In this way, interbank transactions worth up to MNT 5 million will be credited directly to customers' accounts in real time, and individuals, particularly small and medium-sized businesses, will be able to make one-time high-value, low-fee transactions for their products and services.

Within the framework of Payment System Modernization Project financed by Asian development bank, the Bank of Mongolia has successfully launched the new Payment Card System on 25th of April 2021. The system meets international standards, provides high transaction processing speed and capacity, capable of withstanding system load, supports many new transaction types, categories and ensures confidentiality and security of payment system. The system enables participants to compute and calculate its reserves, isolate in the dedicated account, and manage them, resolve on-time disputed or erroneous transactions through adjustment procedures on negotiations basis.

In 2019, the Bank of Mongolia fully renewed its low value payment system and introduced an Automatic Clearing House Plus system. In the reporting year the system's sub-system Central Addressing Module was launched successfully. With introduction of the sub-system, customer's account information is registered in the system and is used to verify and authorize account identifications prior to interbank payment processing.
On average 20,000 transactions were cancelled or rejected daily due to the account name and account number discrepancy, however the usage of Central Addressing Module has drastically reduced the number of erroneous transactions. Currently more than 11 million current accounts of 16 system participants are registered in the sub-system.

An introduction of Mobile Payment Tokenization System is one of the priority projects being implemented and finalized by the Bank of Mongolia. The implementation of the system will allow payment card information to be recorded and listed on mobile phones and then used as a mobile wallet. Payments will be processed remotely with high speed and security furthermore reducing card information loss, fraud, and fraudulent transactions. Moreover, banks and financial institutions will be able to connect and utilize mobile payment and token service integrated package and can preserve duplicate expenses on infrastructure investment. At present, the Bank of Mongolia has signed a cooperation agreement with the system supplier and started the implementation operations.

In the reporting period, the Security Operations Center was successfully established at the National Transaction Center, a comprehensive software system that monitors confidentiality and security operations, conducts evaluations, prevents from, and responds to the cyber-attacks. With rapid development of the payment system functionality and the increasing use of electronic payments, the concern of safeguarding information confidentiality and security is becoming increasingly vital. Thus, the launch of the security center is crucial for maintaining payment system security and integrated network operability at a higher level of safety and preventing from potential risks.

Furthermore, within the framework of the Payment System Modernization Project, 460,000 National brand T-card (EMV/NFC) blanks have been distributed to the card issuing banks at discounted price.

Payment System Oversight, license

In accordance with the National Payment System Law, Clearing System Operator and Payment Agent Operation Regulation, Payment Card Regulation, and Electronic Money Regulation, the Bank of Mongolia has received a total of 12 license applications this year and resolved as follows:

Newly issued license:

- License to issue and acquire payment cards to 1 entity;
- License to issue payment instrument e-money to 2 entities;
- License to operate as a mobile banking processor to 1 entity;
- License to operate as a payment card processor to 1 bank, 1 entity;
- License to operate as a settlement agent to 1 bank.

License applicants of e-money issuer, system operator, issuer, and acquirer of payment cards (in total 3 entities) were refused to issue the relevant licenses due to non-compliance with laws and regulations.

The Bank of Mongolia has been collecting legislative, descriptive, and statistical documents from the payment system participants, including operators, and has been monitoring its compliance and adherence to the regulations as part of its oversight activity. Moreover, the Bank of Mongolia does on-site inspection regularly to ensure safety, reliability, and efficiency of the payment systems. In 2021, the on-site inspection of the participants of the payment system was performed covering the entities and activities listed below:

- Inspection of the operation of the Central Bank Payment System Operator (Banksuljee system, low-value and payment card clearing system of NETC);
- Inspection of the operation of other payment system operators (payment card clearing system of TDB);
- Comprehensive inspection of the participating banks in the payment system;
- Inspection of the payment card processors;
- Comprehensive inspection on the operations of electronic money issuer.

Supervisors reported and corrected any discrepancies identified during the inspection to the full extent of their authorities. In accordance with the pandemic situation of Mongolia, some inspections were conducted remotely for the first time.

Assessment of the “Banksuljee system”, the high value payment system, was conducted to ensure the compliance of the system with the Financial Market Infrastructure Principles and 5 responsibilities set by the Bank for International Settlements.

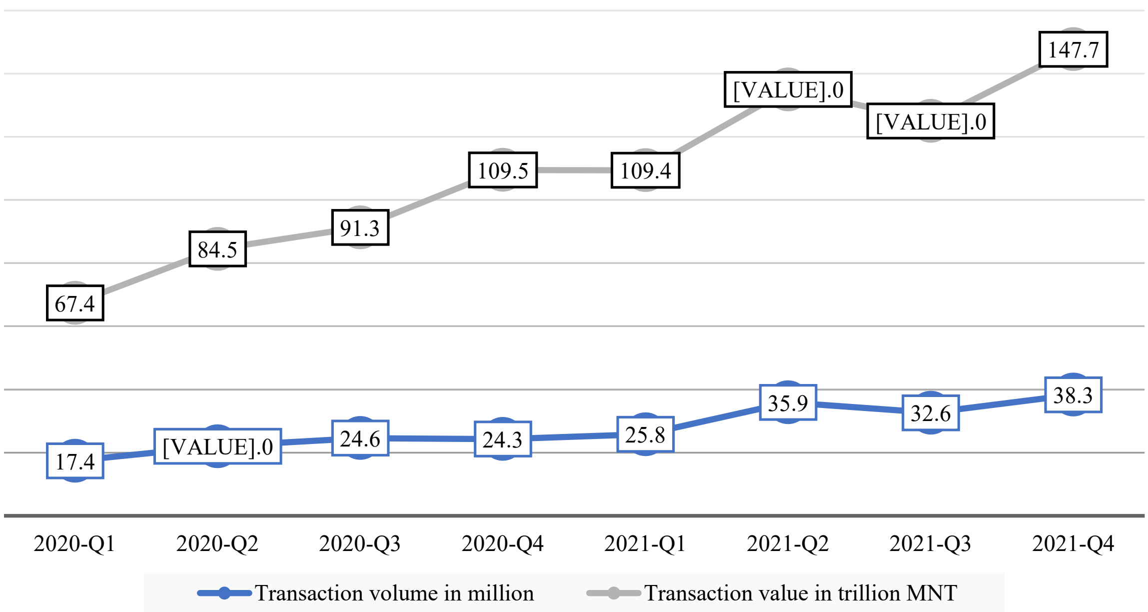
The assessment concluded that out of the 24 infrastructure principles, 5 responsibilities 13 principles were fully observed, 4 principles generally observed, 1 principle partially observed, and 7 principles were inapplicable. Assessment on the Central Bank Securities Settlement System of the Bank of Mongolia shows that 13 out of 24 principles were fully observed, 4 principles were generally observed, 7 principles were not applicable.

Total number of interbank transactions made during the reporting year increased by 50.2 percent whereas the transaction amount increased by 46.6 percent compared to the previous year. Figure 2.11 illustrates the quantitative data of interbank transactions between 2020-2021 shown in Table 2.4.

Table 2.4: Interbank transactions, volume and value, 2020-2021 (volume in thousands, value in trillion)

	2020		2021			
	Volume	**Value**	**Volume**	***Change (%)***	**Value**	***Change (%)***
I quarter	17,375.0	67.4	25,791.1	*48.4%*	109.4	*62.2%*
RTP[12]	12,599.9	3.1	19,008.1	*50.9%*	4.3	*39.3%*
ACH[13]	4,454.9	0.2	6,402.9	*43.7%*	0.9	*281.5%*
RTGS[14]	320.2	64.2	380.0	*18.7%*	104.3	*62.5%*
II quarter	22,014.9	84.5	35,907.2	*63.1%*	135.0	*59.8%*
RTP	15,498.3	3.7	22,949.2	*48.1%*	5.52	*51.2%*
ACH	6,113.6	0.6	12,421.1	*103.2%*	2.44	*280.5%*
RTGS	403.1	80.2	536.9	*33.2%*	127.0	*58.4%*
III quarter	24,626.8	91.3	32,633.7	*32.5%*	125.0	*36.8%*
RTP	17,435.7	4.07	25,377.5	*45.6%*	6.1	*50.1%*
ACH	6,764.7	0.61	6,664.8	*-1.5%*	0.9	*45.0%*
RTGS	426.4	86.7	591.4	*38.7%*	118.0	*36.1%*
IV quarter	24,302.6	109.5	38,278.9	*57.5%*	147.6	*34.8%*
RTP	17,705.5	4.12	30,815.8	*74.1%*	7.68	*86.4%*
ACH	6,171.8	0.87	6,767.9	*9.7%*	1.07	*23.3%*
RTGS	425.2	104.5	695.3	*63.5%*	138.9	*32.9%*
Total	88,319.3	352.7	132,610.9	*50.2%*	516.9	*46.6%*
RTP	63,239.4	14.9	98,150.6	*55.2%*	23.6	*58.2%*
percentage	*71.6%*	*4.2%*	*74.0%*		*4.6%*	
ACH	23,505.0	2.4	32,256.7	*37.2%*	5.3	*124.7%*
percentage	*26.6%*	*0.6%*	*24.3%*		*1.02%*	
RTGS	1,574.9	335.5	2,203.6	*39.9%*	488.1	*45.5%*
percentage	*1.8%*	*95.1%*	*1.7%*		*94.42%*	

Figure 2.11: Interbank transactions, volume and value, 2020-2021



Source: The Bank of Mongolia

[12] RTP – Low-value payment system (real-time)
[13] ACH – Low-value payment system (bulk)
[14] RTGS – Banksuljee, high-value payment system

As shown in Figure 2.10, transactions volume and transaction values have increased steadily compared to the same period of the previous year. Acceleration of non-cash payments is due to Covid-19 pandemic, technological advances, and other economic impacts the digitization of payments. At the end of the 2021, 38.3 million units worth 147.7 trillion MNT were transferred, which is an increase of 14 million units and 38.2 trillion MNT compared to the end of the previous year.

Payment card

The increase of the usage of payments card every year indicates the public's interest in non-cash payment instruments for day-to-day transactions. Banks are issuing 6 different types of payment cards, including the National brand T-card, Visa, MasterCard, Union Pay, American Express, and JCB. As of 2021, the National brand T-card occupied 59.1 percent of total card usage and used extensively in the market.

Table 2.5: Usage of payment cards, 2018-2021

I. Card usage (million)	2018	2019	2020	2021	Growth (%)
Cardholder	4.3	3.7	4.1	4.4	*7.3%*
Active cardholder	1.6	1.9	1.9	2.2	*15.8%*
II. Number of cards – by type of card (thousand)					
T card	3115.6	2600.8	2594.6	2,600.3	*0.2%*
Visa	680.1	392.7	519.0	661.6	*27.5%*
Mastercard	28.4	76.3	123.4	151.3	*22.6%*
Unionpay	458.0	664.6	828.0	1,022.3	*23.5%*
Amex	7.3	4.5	4.1	3.5	*(13.7%)*
JCB	1.8	9.2	8.7	7.3	*(16.4%)*
III. Number of devices[15]					
POS	42,014	59,703	70,753	84,302	*19.1%*
MPOS	3,784	2,803	2,036	105	*(94.8%)*
POB	2,177	2,242	2,915	2,844	*(2.4%)*
ATM	2,358	1,259	1,084	1,049	*(3.2%)*
CDM	-	388	42	19	*(54.8%)*
CRM	-	1,674	1,595	1,764	*10.6%*
Online trade	-	773	1,112	5,008	*350.4%*
KIOSK (with POS)	-	163	264	584	*121.2%*
Other	-	0	0	0	-

Source: The Bank of Mongolia

The table 2.5 shows that the number of payment cards increased by 7.3 percent in the reporting year and the number of active card users increased by 15.8 percent. In terms of device data, the number of POS devices increased by 19.1 percent compared to previous year, indicating an increase in card and non-cash payments for goods and services.

Table 2.6: Card payments, 2020-2021 (volume in thousand, value in trillion)

Devices		2020	2021	Change	Change (%)
POS	Volume	371,838.1	489,852.6	118,014.5	*31.4%*
	Value	8,641.0	12,640.7	3,999.7	*46.3%*
MPOS	Volume	102.5	23.2	(79.3)	*(77.4%)*
	Value	3.1	0.8	(2.3)	*(73.5%)*

15 Starting from the fourth quarter of 2019, 9 types of devices have been registered

POB	Volume	1,390.1	1,019.9	(370.2)	*(26.6%)*
	Value	331.5	258.3	(73.2)	*(22.1%)*
ATM/CRM/CDM	Volume	105,566.3	81,563.2	(24,003.0)	*(22.7%)*
	Value	27,162.3	28,394.9	1,232.6	*4.5%*
Online trade	Volume	1,555.2	3,629.8	2,074.6	*133.4%*
	Value	109.1	260.1	151.0	*138.4%*
KIOSK (with POS)	Volume	323.2	838.8	515.6	*159.5%*
	Value	7.5	20.5	13.0	*173.6%*
Other	Volume	0.0	0.0	-	-
	Value	0.0	0.0	-	-
Total	Volume	480,775.5	576,927.6	96,152.1	*20.0%*
	Value	36,254.4	41,575.3	5,320.9	*14.7%*

Source: The Bank of Mongolia

In terms of transaction volume, the highest number of POS transactions were 489.9 million in the reporting year. In terms of transaction value, ATMs, CRMs and CDMs accounted for the largest amount of 28.4 trillion MNT. Compared to the previous year, KIOSK (with POS) was the most used device, with transactions increasing by 159.5 percent in volume and by 173.6 percent in value, respectively, as shown in Table 2.6.

2.6 BANKING AND FINANCIAL SECTOR LEGAL REFORMS

Throughout reporting year, the Bank of Mongolia (the Bank of Mongolia) has progressed legislative reforms improving mandate and operations of the Central Bank as well as creating economic and financial stability of the country as a prerequisite for its long-term development. As in the "State Monetary Policy Guidelines for 2021" approved by Parliament Resolution No.32 of 2020, core goals of the reform were to improve anti-money laundering and counter-terrorist financing mechanism by harmonizing national legislation with the recommendations of the Financial Action Task Force (FATF). The resolution also aims to create effective and efficient framework for financial agreements and contracts related dispute resolution and protection of financial consumers' rights.

The Bank of Mongolia also led and actively engaged in approval process of the Law on Virtual asset services provider with supporting research findings to lawmakers to follow FATF Recommendations and to upgrade the risk assessment ratings. The law defines virtual assets, the virtual service providers, sets general and specific requirements as per international standards and establishes registration procedure of virtual asset providers and its monitoring mechanism. In addition, it creates the basis of the system to comply with FATF Recommendations to minimize money laundering and terrorism financing risk and its monitoring framework. Based on situation analysis of the banking sector of Mongolia, the Bank of Mongolia had prepared amendments to the Banking Law submitted and enacted in the Parliament during its 2021 autumn session. The concept of the law establishes requirement for a bank to be public company and to single shareholding limit of 20 percent of bank equity capital thus reducing concentration of bank ownership, and balancing management and control function.

The Parliament passed Law on Deposits, Loans and Money transfer activity of Bank and Authorized legal entities on May 21,202, and the law became into force from July. As part of the policy document "Interest rate reduction strategy" approved in 2020 by Parliament Resolution No.21, the revision of the law aims to minimize capital and operating cost as well as to improve protection of customers rights. Specifically, the law sets general requirements/terms for products and services offered by banks and licensed entities to persons and legal entities, principles for granting loans, rates and fees charged at their operation. With approval of the law, the Bank of Mongolia has prepared loan origination and collateral evaluation regulations in accordance with General Administrative Law of Mongolia.

The Bank of Mongolia also established a working group tasked with studying rationale, impact and cost analysis and drafting relevant laws in scope of above policy document. Those draft laws cover such areas of collateral of movable or intangible assets, asset evaluation, anti trust, financial leasing, business licensing, taxation, credit information, legal entities registration, collateral assets, and other related areas. With those efforts, market participants will see elimination of unnecessary burden in enforcing contractual obligation during dispute resolution process.

Article 2.2 of the Monetary Policy Guidelines for 2021 stipulates strengthening the legal environment protecting financial customers. In 2021, the Bank of Mongolia re-drafted the Law on Financial consumer protection and submitted it to lawmakers. This initiative implemented among the Bank of Mongolia, Financial Regulatory Commission, and Asian Development Bank (ADB) through "Promoting the development of financial consumer protection and technical assistance on financial education" (Promoting a Coordinated Framework for Financial Consumer Protection) project.

The Parliament ratified intersectoral legislations, which will intensify digital transition by aligning technological innovations with the banking and financial sector, ensure optimal regulation, and promote development for the banking sector. This includes ratification the law on Digital signature which has positive effect on fast financial intermediation, the law on Personal data protection ensuring bank customers' confidentiality, and law on Cybersecurity protecting state and private sector's information infrastructure.

2.7 NATIONAL PROGRAM FOR FINANCIAL LITERACY

The Bank of Mongolia, the Ministry of Finance, the Ministry of Education, Culture and Science, and the Financial Regulatory Commission jointly launched the "National Mid-Term Program for Financial Literacy" in 2016 to ensure financial stability, increase financial participation, and improve financial decision-making of the citizens in Mongolia.

In cooperation with relevant government and professional organizations, the program provides financial literacy to the public in four priority areas: school children, young people, rural residents, and through mass communication/media.

In addition, the Bank of Mongolia and the Ministry of Food and Agriculture has been jointly approved a medium-term plan to focus on providing financial education to micro, small and medium enterprises and service providers.

This program is expected to yield the following positive externalities:

- Increase public knowledge of financial products and use them more effectively;
- Improve citizens ability to choose the right financial product for their needs;
- Prevent financial fraud and reduce the number of victims;
- Increase individual savings and decrease non-performing loans;
- Support participation and investment in the stock market.

Activities under the program are focused on the following key topics:

- Basic concepts of finance;
- Budgeting and financial planning;
- Savings and deposits,;
- Credit and loans;
- Fintech & Cryptocurrency;

- Investments;
- Protection against financial risks (e.g. insurance);
- Savings for retirement;
- Concepts related to social insurance and tax;
- Understanding the financial service providers and institutions.

Within the framework of this program following actions were taken in 2021:

Legal environment

Government of Mongolia

The Government approved the “National program to develop Mongolia’s financial market until 2025” through resolution No.299 in 2017, with the objective 6.2 to “Every Mongolian citizen shall possess the knowledge, skills and confidence necessary to manage his/her personal and household finance in an appropriate way” has been implemented in 2021.

Monetary policy strategy

The Monetary Policy Guidelines for 2021 was approved by the Parliament of Mongolia through Resolution No. 32 on November 5, 2020, with the objective 3.3 specified to “support financial inclusion and consumer protection activities by improving financial education of citizens, micro, small, medium enterprises and service providers” has been implemented in 2021.

Draft law on financial consumer protection

According to Article 5.1.7 “Protect legal rights and interests of bank customers and depositors” of the Law on the Central bank (Bank of Mongolia), a draft law on financial consumer protection was developed. It was decided to discuss the draft law at the meeting of the Parliament’s Standing Committee on Economics and present it to the Parliament.

The purpose of this law is to protect financial consumers’ rights, set requirements for financial products and services, determine the rights and obligations of the parties in charge of resolving complaints and disputes, and provide financial education to the public.

Loan Rate Reduction Strategy

With the recommendation from the Financial Stability Committee, the Bank of Mongolia is implementing the “Loan Rate Reduction Strategy 2018-2023” and the objective No.11 of the strategy states “Implementation of programs and activities to improve the financial education of financial institutions, their customers and the public”. Moreover, in order to reduce the credit risk cost of the “Loan interest rate reduction strategy” approved by the Parliament Resolution No. 21, the provisions on “Protecting the interests of financial consumers and improving the basic financial knowledge of the public” are being implemented.

Financial literacy for school children:

- On August 1, 2019, the Minister of Education, Culture, Science, and Sport issued decree No. A/491 on “Renewal of training curriculum”, which the “Business Studies” was approved as an elective subject for the secondary school curriculum. To implement this, social studies teachers are teaching business studies and the Bank of Mongolia is supporting this work.

- The annual "Global Money Week 2021" campaign held from March 22 to April 12. This year's slogan was "Learn-Save-Earn" and it aimed to improve the financial education of children and youth and draw public awareness to it. The Bank of Mongolia host the campaign with the Ministry of Education and Science, the Deposit Insurance Corporation, the Mongolian Banking Association, the Authority for family, child, and youth development, the National Center for Lifelong Learning, and the German Sparkasse Bank in Mongolia and commercial banks. As part of the campaign, the Bank of Mongolia held a panel discussion with stakeholders on "current financial literacy status and its future trends in Mongolia". During the campaign, about 80 competitions with 20,000 entries were organized which includes Tik Tok, hand drawings, and essay competitions to promote the importance of savings to children across the country. Moreover, meetings on "How to manage money", "Personal finance and household budget", "Expenses and savings", and "Digital money" were also organized for more than 117,000 high school students.
- The opening ceremony of the "World savings Day 2021" was jointly organized by the Bank of Mongolia, the Deposit Insurance Corporation, the Sparkasse Banking Fund of Germany, and the Mongolian Banking Association under the slogan "Let's Save", in Zuunmod, Tuv province. This year's inaugural event was special in the way that the opening ceremony was held in the countryside for the first time. During the ceremony, commercial banks introduced their products and services for children and young people, opened on-site savings accounts, and presented presentations on the importance of savings, and its benefits. Within the framework of the campaign, in cooperation with partner organizations, online competitions were organized among children and youth to support the public's financial education and make savings a habit. In addition, training and meetings were held for more than 500 secondary school children to raise awareness of the benefits of savings.

Financial literacy for youth

- Under the National Program for Financial Literacy, a 3-credit compulsory course on "Personal Finance" is available at 13 accredited universities.
- A memorandum of understanding was signed between the Bank of Mongolia and the Authority for family, child, and youth development in 2020 to ensure the implementation of the Law on Youth Development, the Monetary Policy Guidelines, and the National Program for Financial Literacy. According to the memorandum the Bank of Mongolia trained 35 staff members of the Authority for family, child, and youth development from the capital city and its branches of the countryside as trainers to provide financial education to young people.
- A total of 830 students took the "Personal Finance" trainings and lectures both in-class and virtually in 2021.
- The Bank of Mongolia, in cooperation with the National Center for Lifelong Learning, the Financial Regulatory Commission, and the Microfinance Development Fund, has trained 883 financial trainers in the past and provided knowledge and information to young people. In the reporting year, trainers from the National Lifelong Learning Centers have conducted about 1,229 in-class and virtual courses and 1,363 separate discussions on financial education.
- Published 35,000 copies of financial literacy hand-outs on different financial topics, including "How to Manage Money?", "Loans", "Household Budget", "Savings", "Price Stability" and "Exchange Rates"

Financial literacy through mass communication/media

A webpage for financial education, www.sankhuugiinbolovsrol.mn has been regularly updated and provided financial literacy content.

The “Financial Education” Facebook page was regularly updated about topics such as “Personal finance, savings, investment, digital payment, and it had over 15000 followers at the end of 2021.

- On the Mongolian National Public Radio 11 episodes of the “Financial Tree” program aired to support the understandings of financial literacy topics of the people and all episodes were broadcasted live on the Facebook page of the radio.
- “Financial Education” Facebook page was updated with 342 news, information, infographics on financial recommendations.

Within the framework of providing financial education to micro, small and medium enterprises and service providers

- In the framework of the “National Program for Financial Literacy”, in cooperation with the EBRD, and with the support of the European Union, developed a “Medium-Term Plan to Improve the Financial Literacy of Micro, Small and Medium Enterprises and Service Providers”. The plan was jointly approved by the Governor of the Bank of Mongolia and by the Minister of Food, Agriculture and Light Industry. Furthermore, the plan performs an important part in protecting the legitimate interests of financial consumers and supporting the proper management of personal and business finances and it will be implemented over 5 years.
- To ensure the implementation of the “Medium-term plan to improve the financial literacy of micro, small and medium enterprises, and service providers”, the Ministry of Food, Agriculture and Light Industry, Financial Regulatory Commission, Small and Medium Enterprises Agency, Small and Medium Enterprise Service Support, National Center for Lifelong Learning, the Credit Guarantee Fund, the Deposit Insurance Corporation, the Mongolian National Chamber of Commerce and Industry, and the Mongolian Banking Association had formed a working group to continuously implement the plan. During the reporting period, 32 trainers from stakeholder representatives have been trained to provide financial literacy for the MSMEs, developed the trainer’s curricula and organized trainings to the MSMEs as well.

Cooperation with international organizations

The Sparkasse Banking Fund of Germany in Mongolia

- It has been 4 years since the Bank of Mongolia, the Mongolian Bankers Association, the German Savings Bank Foundation for International Cooperation “Sparkasse” and the Ostprignitz-Ruppin Sparkasse started implementing “Introduction of dual vocational training for bank specialists” and organizing “The World Savings Day in Mongolia”. During this period, 94 trainers were prepared and a total of 255 participants from 11 commercial banks successfully participated in the 6-module training. This year, a total of 30 specialists from Ulaanbaatar have successfully graduated.
- To maintain the project results for a longer period, the implementation processes have begun to update the project of “Banking and Finance Academy” under the MBA and establish a “New Institute” for banking and financial sector employees in Mongolia with co-financing from the German Ministry of Economic Cooperation and Development.
- The Bank of Mongolia, the Mongolian Banking Association, the Sparkasse Bank Foundation of Mongolia in Germany, and the Mongolian Banking and Finance Academy jointly developed the “dual vocational training and standard” and “new banker’s training program’s requirements” were approved by the order No. A-313 of the Governor of the Bank of Mongolia dated November 25, 2021.

European Bank for Reconstruction and Development (EBRD)

The Bank of Mongolia, in cooperation with the EBRD, is implementing a project “Developing a Financial Education Program for MSMEs” with the support of the European Union.

In 22th of March 2021 was held online international conference to review the project, opened by G.Enkhtaivan, Deputy Governor of the Bank of Mongolia, Hannes Takacs, Vice President of the EBRD Mongolia, Pierre Yves-Lucas, Head of the EU Delegation to Mongolia, Shaun Mundy, Senior Vice President of the Financial Education Group, OECD / IFRS (OECD / INFE) Executive Secretary Flore-Anne Messy. During the conference, the project advisory team presented the results of the “Financial Education Needs for MSMEs” survey, trainer training, financial education strategy for MSMEs, and the process for training entrepreneurs.

OECD International Network on Financial Education

The Global Money Week-2021 campaign with the technical assistance of anInternational Financial Education Network (OECD / INFE) of Organization for Economic Co-operation was organized across the country under the slogan “Learn-Save-Earn” within partner organizations. The campaign was organized by the Bank of Mongolia, the Ministry of Education and Science, the Deposit Insurance Corporation, the Mongolian Banking Association, the Authority for family, child, and youth development, the National Center for Lifelong Learning, the German Sparkasse Bank’s fund and commercial banks from March 22 to April 12, where reached 16 952 children and young people directly and 45 000 indirectly . During the campaign, the stakeholders held a discussion on *“Current Status and Future Trends of Financial literacy in Mongolia”*.

THE BANK OF MONGOLIA'S MONEY MARKET OPERATIONS | 3

3.1 OPEN MARKET OPERATIONS

Central Bank Bills

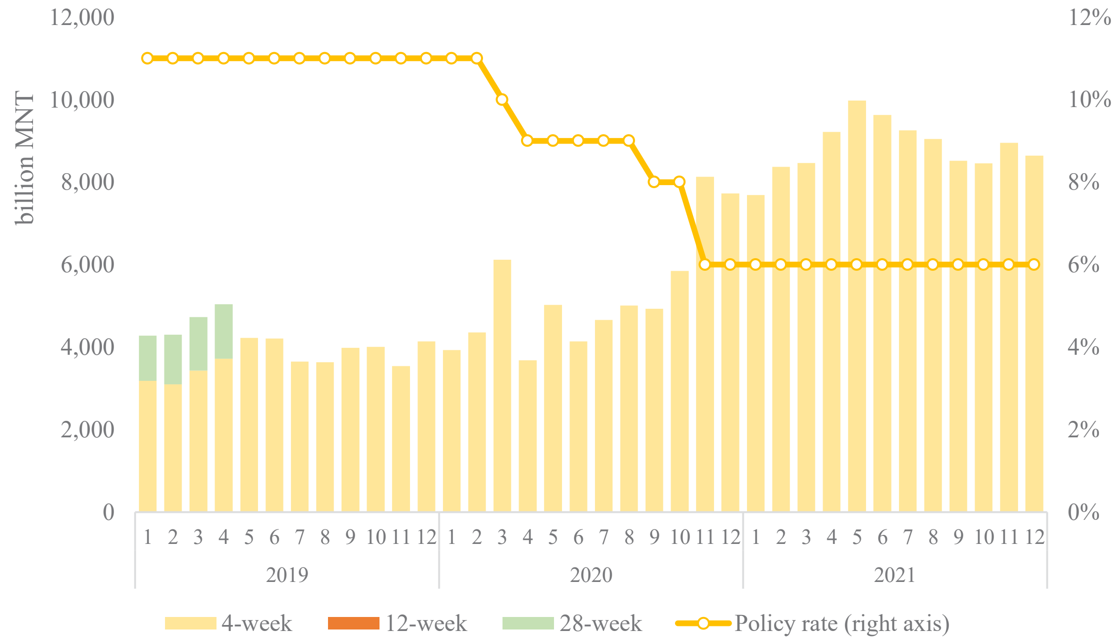
Open Market Operations or Central Bank Bills (CBB) auction is the main instrument of the Bank of Mongolia to implement its monetary policy objectives by managing the fluctuation in the interbank short-term rate and the reserves of the banking system. In 2021, the Bank of Mongolia auctioned the following types of CBB with different yields, maturities, and types of bids.

- The Bank of Mongolia has issued CBB with a maturity of 4 weeks every Monday with a fixed rate tender and no ceilings on the bidding amount. The interest rate of this CBB (the shortest maturity of CBB traded) is considered as a policy rate and this type of CBB plays a crucial role in absorbing the excess reserves in the banking sector and assists the banks in managing its reserves.
- The Bank of Mongolia has issued CBB with a maturity of 28 weeks on Wednesdays of every two weeks with pre-announced auction amount and the interest rate ceiling. The aim of this type of CBB is to absorb systemic structural excess reserves, increasing trade of long-term security in the interbank market and determining the yield curve for the tenor of up to 6 months, and improving the monetary policy transmission mechanism.

The total outstanding amount of CBB has reached 8,644.96 billion tugrug at the end of 2021, which is an increase of 8.38 percent or 669.76 billion tugrug from the end of 2020. Changes in the reserves of the banking system are impacted by both liquidity supply and absorption operations. In 2021, the Bank of Mongolia has supplied liquidity through purchase of gold with the amount of 2,838.5 billion tugrug to build foreign exchange reserves. In addition to that, the government's net lending has increased by 501.9 billion tugrug in reporting period which contributed to increased supply of the liquidity in the market. On the other hand, the tugrug liquidity was absorbed through foreign exchange market intervention by the Bank of Mongolia in amount equivalent to 3,321.1 billion tugrug.

Furthermore, interest rate intervals of the variable rate tender CBB have been changed to zero by A-114 decree of the Governor of the Bank of Mongolia on 13th of May in 2021, which led to a lower demand for the long term CBB. As a result, outstanding amount of CBB consisted of 4 weeks CBB only, by the end of the 2021.

Figure 3.1: The total outstanding amount of CBB (by maturity, in billion tugrug)



Source: The Bank of Mongolia

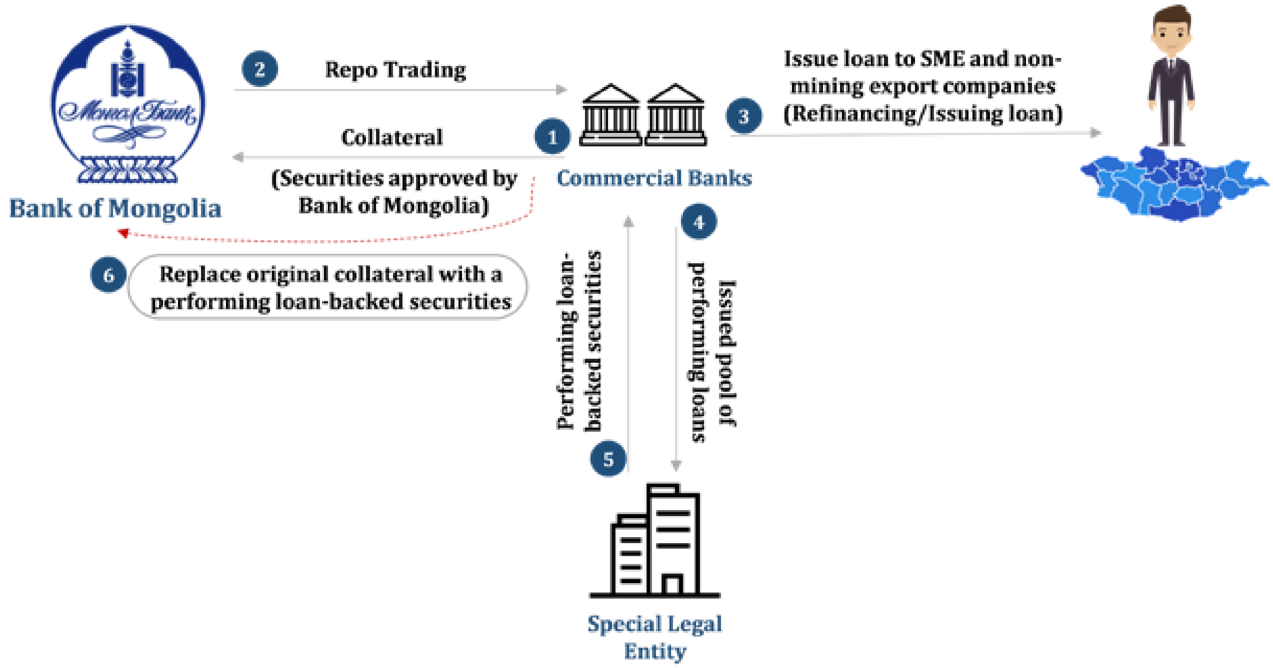
Repo trading

The central bank's repo operation is an operation that provides liquidity to the banks using securities that banks hold as collateral, and the banks agree to repurchase the collateral at the end of the period. In line with the Bank of Mongolia's strategy to reduce interest rates and to eliminate the adverse impact of the COVID-19 pandemic on the economy, the tenor of the repo operation agreement was extended to two years, and the collateral list was expanded. Long-term repo financing operations were used in the previously approved SMEs and non-mining exports to expand services, manufacturing, wholesale and retail trade companies with 200 or more employees to create and support inclusive growth and to diversify the economy. In addition, long-term repo trading sources have been provided to enterprises and individuals by the loan conditions approved by the Governor's Decree 89, 185, and 247 of 2021. These changes will

1. Mitigate the adverse effects of the economic downturn and financial intermediation,
2. Economic diversification and support exporting enterprises, and
3. Opportunities to launch new products in the financial markets.

The Bank of Mongolia financed MNT 825.0 billion to banks through repo trading in the reporting year. Figure 3.2 shows a scheme for banks to issue loans, securitize their loans, and obtain financing from the Bank of Mongolia.

Figure 3.2: Long-term financing scheme with performing loan-backed securities

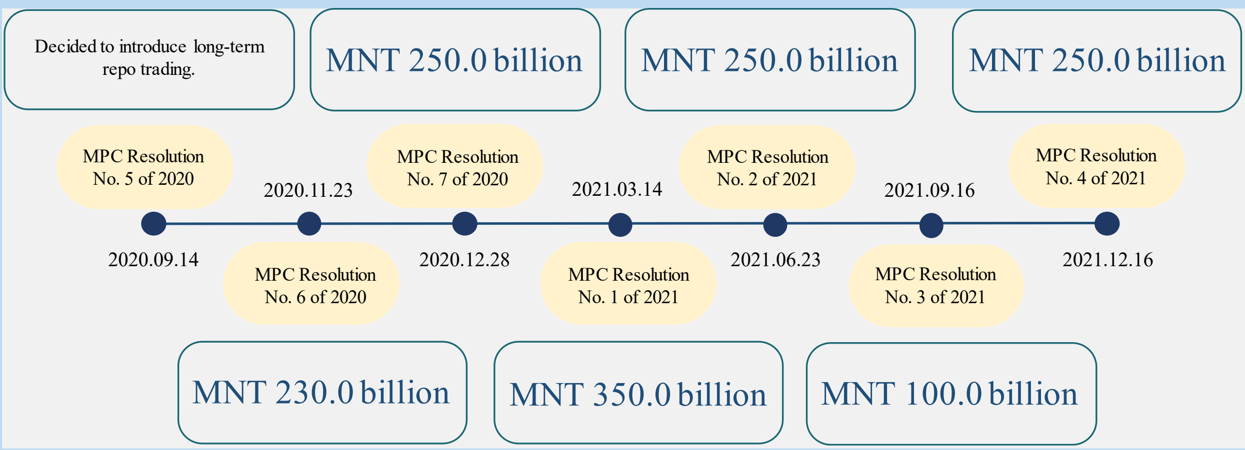


Box 3.1. Information on long-term repo trading

According to Governor's Decree A-425, the Monetary Policy Committee has decided to set the terms of repo trading, total financing amount, and loan terms quarterly. The Monetary Policy Committee approved MNT 950.0 billion in financing in 2021, of which the Bank of Mongolia disbursed MNT 825.0 billion to commercial banks (Figure 3.1). Additional terms of long-term repo loans were renewed on July 6, 2021, and the existing non-mining exports and SME sectors will include services, manufacturing, and wholesale and retail trade with 200 or more employees. As of the end of this year, a total of MNT 834.9 billion loans have been disbursed by commercial banks (Figure 3.2).

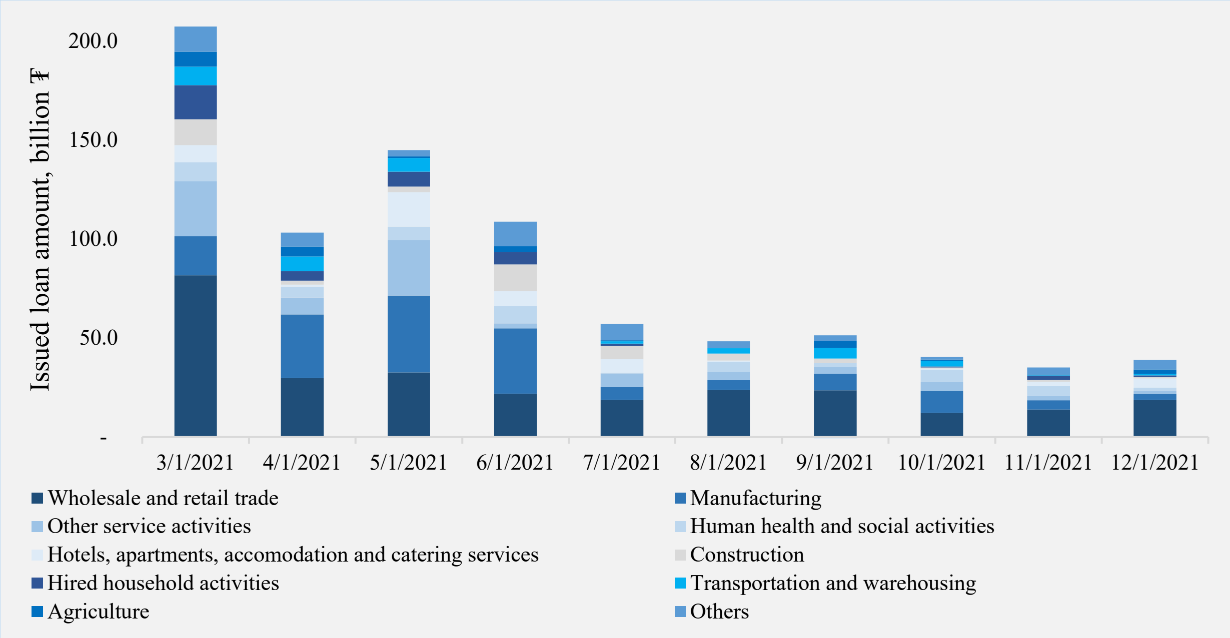
In addition, 40.5 billion MNT worth of securities were issued by "SFC Assets One SLE," and 160.4 billion MNT were issued by "SFC Assets Two SLE." The Bank of Mongolia is arranging to replace the pledged initially Central bank bills with these securities.

Figure 3.3: Monetary Policy Committee decisions related to long-term repo trading



Source: The Bank of Mongolia, Monetary Policy Committee

Figure 3.4: Long-term repo newly issued loan amount, by sector



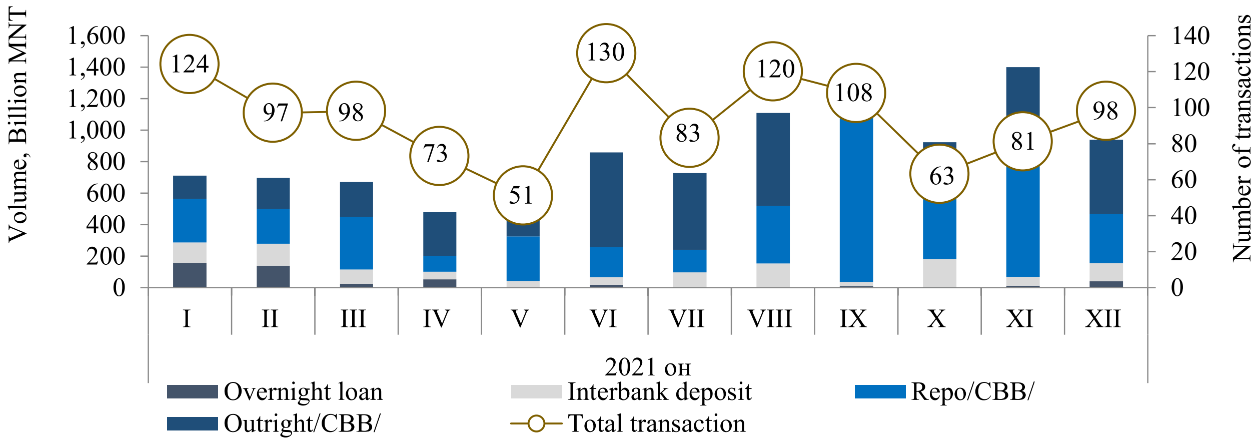
Source: The Bank of Mongolia

In addition, the Monetary Policy Committee, by Resolution No. 4 of December 16, 2021, decided to expand long-term repo financing to the stockpile of fuel and main food products to the required level. Therefore, the Bank of Mongolia provided a total of MNT 297 billion in financing to banks for up to 12 months to build up fuel reserves in December 2021.

Interbank market transaction

The Bank of Mongolia has been ensuring the stable operation of the interbank market daily. During the reporting year, the monthly average of the interbank market's overnight transaction reached 38.9 billion tugrug, interbank repo transaction reached 400.5 billion tugrug, outright purchase of CBB reached 330.8 billion tugrug. The average maturity of interbank market transactions was 9.9 days, which is a decrease of 2.7 days from the previous year (Figure 3.5).

Figure 3.5: Total transaction of the interbank market (by instrument, in billion MNT)

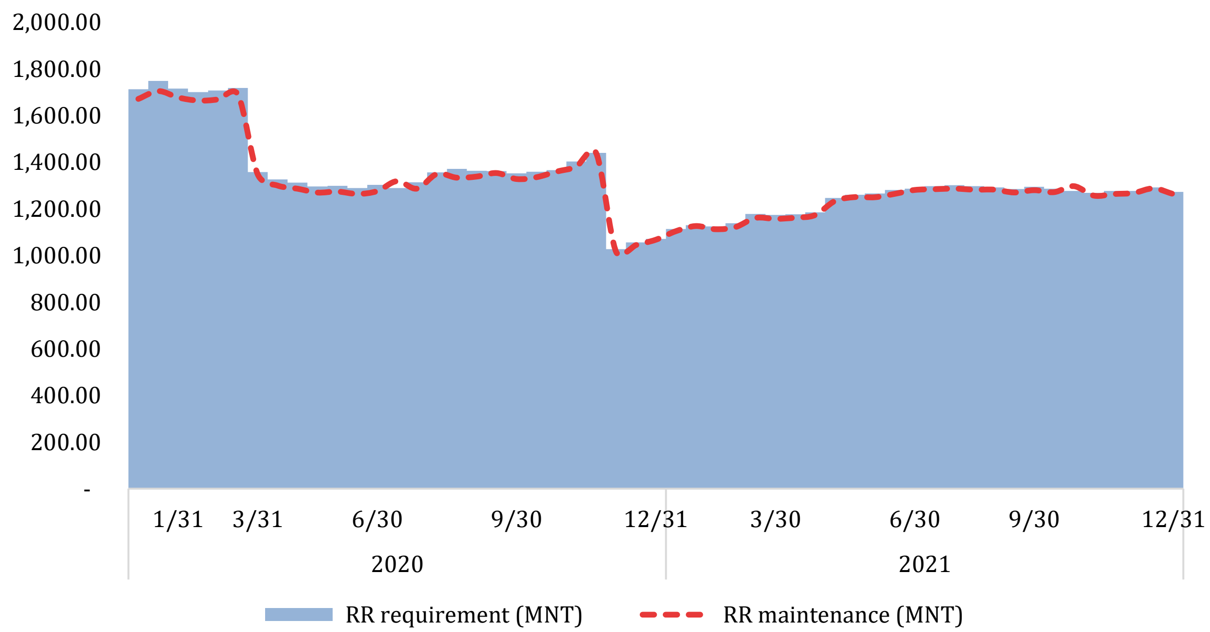


Source: Bank of Mongolia

Reserve requirement

According to Article 11.1 of the Law on the Central Bank, the Bank of Mongolia may use the bank's reserve requirement to implement its monetary policy. In accordance with this, the Monetary Policy Committee of the Bank of Mongolia may discuss and set the required reserves for banks to hold in accordance with Article 27-3, Clause 4.3 of the Central Bank Law. On 16th of December 2021, Monetary Policy Committee has made a decision to increase the bank's required foreign exchange reserve by 3 percentage points from 15 percent to 18 percent in order to reduce the dollarization of banks' liability and maintain the relative stability of its domestic currency (tugrug). As a result, the foreign exchange reserve for the banking system was set at MNT 1,423.4 billion during the maintenance period from December 29, 2021, to January 11, 2022. This number was an increase of MNT 144.9 billion or otherwise a 11.3 percent increase compared to the same period of the previous year. The reserve requirement for domestic currency (tugrug) was last updated during the November 23, 2020, meeting of the Monetary Policy Committee where the requirement was reduced from 8.5 percent to 6 percent. In the year of 2021, there has been no changes to the domestic currency reserve requirement.

Figure 3.6: Reserve requirement for domestic currency (tugrug) and its maintenance (2020/01/01-2022/01/11, billion ₮)



Source: The Bank of Mongolia

3.2 CENTRAL BANK STANDING FACILITIES

In order to reduce the interest rate volatility at the interbank market, the Bank of Mongolia offers standing facilities that either absorb or provide liquidity to assist the banks to manage their reserves. These standing facilities include the overnight deposits that absorb the excess reserve and the overnight repo financing that provide liquidity to the banks.

Within the Bank of Mongolia's interest rate policy framework, the lowest and the highest rate of the Central bank's interest rate corridor is determined by the overnight deposit rate and repo financing rate, respectively. During the reporting period, the interest rate corridor width has been 200 basis points (policy rate ±100 basis points).

In 2021, the Bank of Mongolia provided 2,787 billion tugrug to the commercial banks through a repo financing facility with a weighted average interest rate of 7% and received a total of 41,270.5 billion MNT of overnight deposit with a weighted average interest rate of 5% from banks.

3.3 OTHERS

Intraday credit

The intraday credit is an instrument of the Bank of Mongolia that assists the payment system to run smoothly by providing liquidity to the banks who are in a short-term liquidity issues during a day. Intraday credit must be repaid within the same day and it has zero-interest rate. In 2021, there was no case of using this facility.

Secured loan

In accordance with the “Secured loan regulation” approved by the A-174 decree of the Governor of the Bank of Mongolia on June 15th, 2018, as a lender of last resort, the Bank of Mongolia provides secured loans to banks in order to support bank’s liquidity by preventing liquidity issues. In 2021, no secured loans in accordance with this regulation were provided to the banks.

However, to improve the financial situation of the banks and maintain the stability of the banking sector, taking into account the socioeconomic situation during the COVID-19 pandemic, the Bank of Mongolia has extended the validity of the “Temporary regulation on Bank of Mongolia loan to the banks” approved by the Governor of the Bank of Mongolia’s Order A-192 on June 3, 2020, until December 31, 2021. In 2021, in accordance with this regulation, 14.3 billion tugrug of the secured loans were issued to banks to support their liquidity.

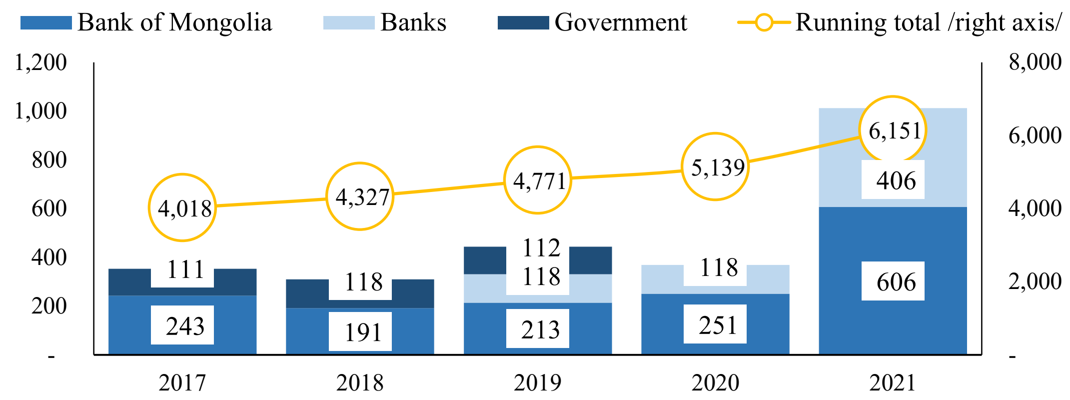
Mortgage program financing

In 2013, the Bank of Mongolia and the Government of Mongolia initiated the “Establishing stable housing finance scheme” sub-program as the second part of the “Assisting construction sector and further stabilizing housing price” program. The main objective of the mortgage program is to help low and middle income households with affordable housing, thereby reduce air and soil pollution, neutralize migration from rural areas to the capital city.

As of the end of 2021, a total of MNT 6.2 trillion mortgage loans have been distributed to 103.9 thousand households by the Bank of Mongolia, the government of Mongolia, and commercial bank funds (Figure 3.7).

In line with the “Law on Preventing and combating COVID-19 and Reducing its Social, Economic negative impact”, Parliament Resolution No.32 of 2020 and “10 trillion MNT Economy Recovery and Health Protection Integrated Plan” a total of 2 trillion MNT is approved to be distributed until 2024. In 2021, a total of 1.0 trillion MNT loans were distributed and for the consequtive 2022 and 2023 years, a total of 1.0 trillion MNT loan is planned to be distributed.

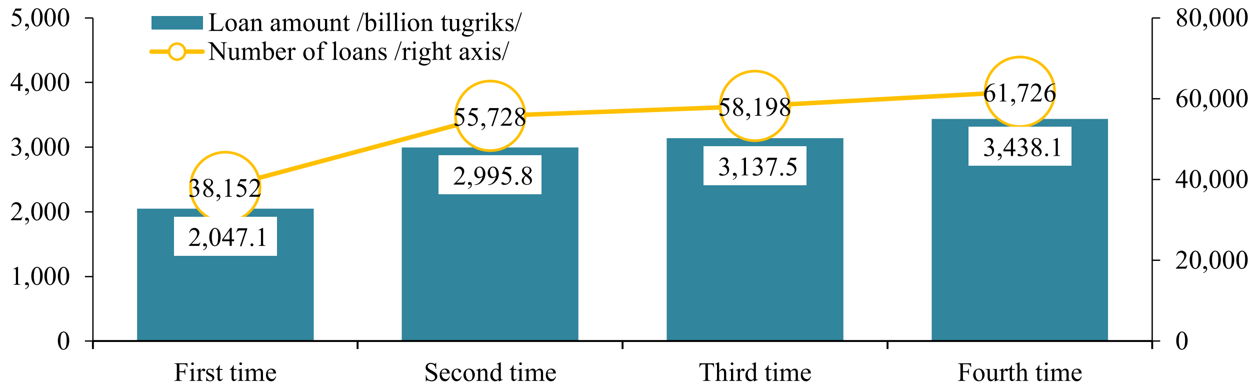
Figure 3.7: Mortgage financing, in billion MNT



Source: Bank of Mongolia

In accordance with the "Law on Preventing and combating COVID-19 and Reducing its Social, Economic negative impact" and Parliament Resolution No.32 of 2020, mortgage loan repayment deferral measures have been taken four times. As a result, a total of around 214 thousand households (double-counted) deferred their mortgage loan repayments for duration of 25 months. Throughout this period, an aggregate repayment of 783 billion tugriks (of which, 341 billion in principal repayment, 442 billion in interest repayment) has been deferred (Figure 3.8).

Figure 3.8: Mortgage loan repayment deferral



Source: Bank of Mongolia

Beginning in 2024, the mortgage loan program is set to be transferred to the Government of Mongolia. Thus, on June 7th, 2021, an amendment to the December 20th, 2018, joint decree 285/A-334 between the Minister of Finance and the Governor of the Bank of Mongolia "Plan to exclude the Bank of Mongolia from a program to structure stable mortgage financing scheme", was approved.

Financing the rent backed security program

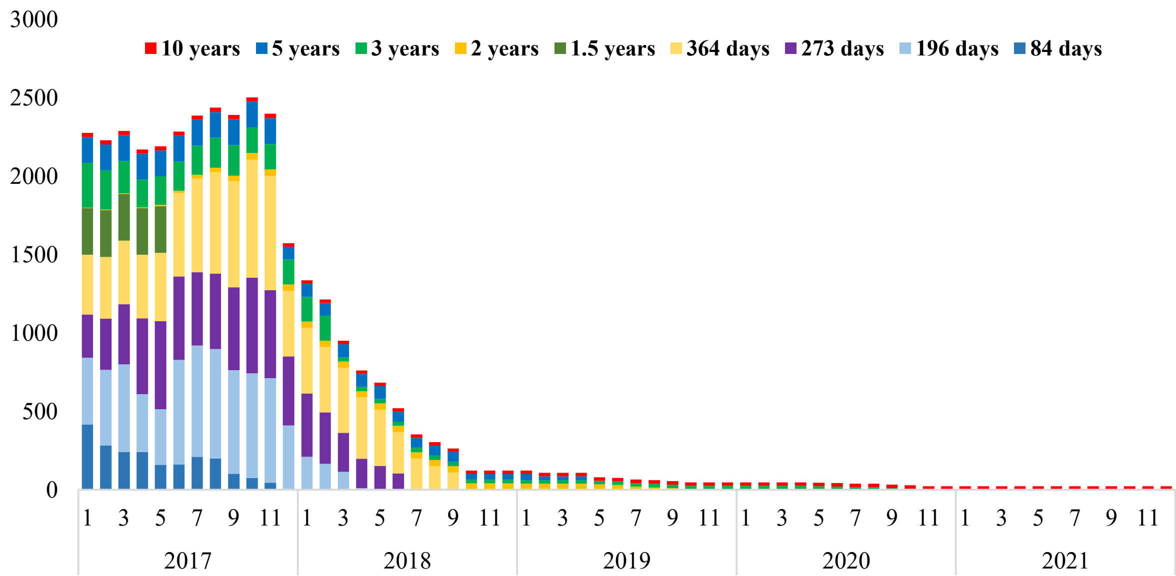
In accordance with Article 10.5 of the "Law on Preventing and combating COVID-19 and Reducing its Social, Economic negative impact" and Article 2.6 of the Parliament Resolution No.32 of 2020, the Rent backed security program is implemented by the Capital city housing corporation, a special condition project intended to provide housing for government and civil servants performing in high-risk environment. In order to finance the project, the Governor of the Bank of Mongolia's Order A-417, 2020 approved the purchase of MNT100 billion rent backed securities. As a result, in 2021 the Bank of Mongolia purchased MNT 65.6

billion rent backed securities. A total of 1,177 government and civil servants were provided with housing through the program.

3.4 GOVERNMENT SECURITIES (GS)

Starting from October 2012, the government issued and traded government securities in the primary market through the Bank of Mongolia to improve the government's financial management and to improve the money market instruments. The government securities are considered as a risk-free investment in the financial market and the interest income earned on these securities is exempt from taxation which is an advantage for investors. It is also considered that the regular trading of government securities supports the development of the financial market in many ways, such as setting risk-free interest rates in the financial market, otherwise known as a yield curve, and determining the impact of short-term interest rates on long-term interest rates, and it also increases the financial market activity. However, by the order of the Ministry of Finance (MOF), the issuance of the government securities was terminated in November 2017.

Figure 3.9: Outstanding Government Security amount acquired through the Bank of Mongolia's auctions (billion tugrug)



Source: The Bank of Mongolia

By the end of 2021, the outstanding amount of government securities reached 22.5 billion MNT and remaining government securities all have maturity of 10 years (figure 3.9). "The regulation on the operation of domestic government securities in the primary and secondary market" was approved by Government Resolution No.77 on February 20th, 2019. However, there has been no Government bonds were traded on the secondary market, even though the relevant regulation were still effective, and the platform was available. Since there have been no new government securities were issued in a primary market and only the outstanding government securities were expiring throughout the year, hence, it contributed largely to the increase of outstanding balance of CBB to 8.0 trillion tugrug in 2020, and 8.6 trillion tugrug in 2021.

3.5 FOREIGN EXCHANGE INTERVENTION

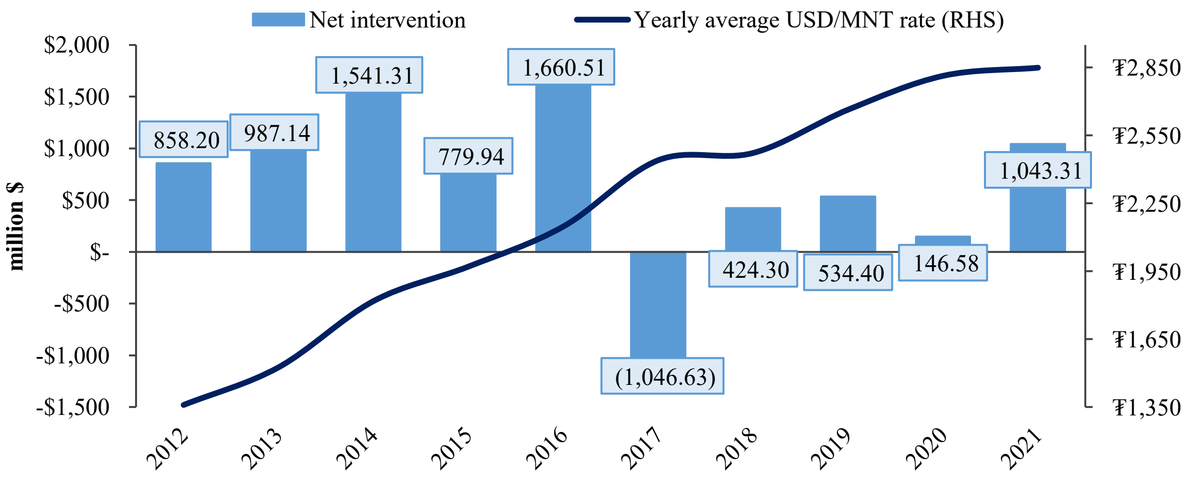
The Bank of Mongolia has been working to ensure that togrog's exchange rate flexibility is consistent with macroeconomic fundamentals. Therefore, the Bank of Mongolia has been intervening in the domestic foreign exchange (FX) market to mitigate the exchange rate fluctuations caused by the short-term demand and supply gap.

Due to lockdowns and business activity restrictions, domestic foreign exchange market activities have remained relatively low at the start of 2021. With the increased vaccination and loosened lockdown, economic and business activities recovered, and foreign exchange demand, depreciation pressure on the MNT rate against foreign currency has increased accordingly. From the point of Balance of payment, export revenues increased 22% YoY in 2021 caused by the sustainable high price of mining commodities in the global market. However, increased price of fuel, food material, equipment imports, and accumulated loss on the income account was the primary reason for the current account loss.

As of 2022, external demand will sustain stability as the global economy recovers, and the price for Mongolia's mining export commodities is expected to remain relatively high, creating positive expectations in terms of foreign trade. The resumption of border operations will increase exports and improve foreign exchange inflows with imports of goods and services also expected to increase in line with economic activities.

As a result, the Bank of Mongolia intervened in the FX market with a net amount of USD 1043.3 million, through FX market instruments.

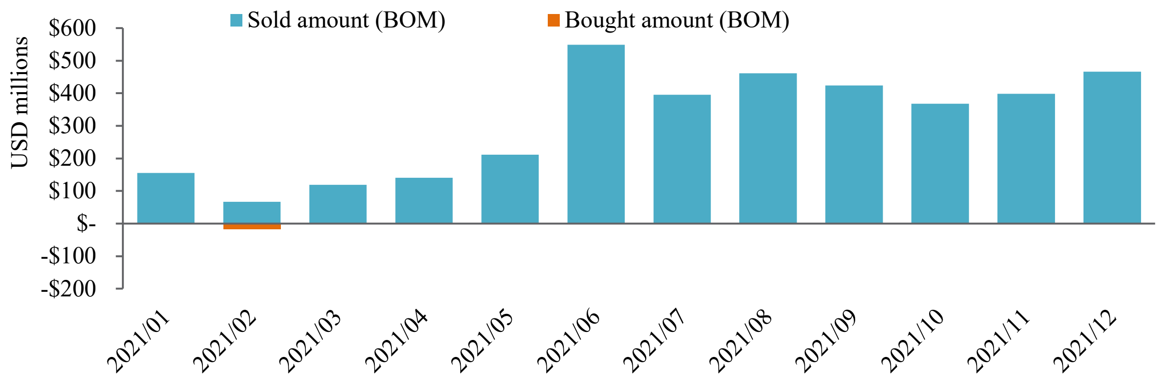
Figure 3.10: Net FX intervention of Bank of Mongolia in 2012-2021 (in million USD)



Source: The Bank of Mongolia

In 2021, the Bank of Mongolia has organized 102 FX auctions and sold a total of USD 3,607.9 million through FX auctions and FCOTS, which is an increase of 44.1% from the previous year. According to the joint resolution of the Minister of Finance, Chief Cabinet Secretary, and the Governor of the Bank of Mongolia, the Bank of Mongolia has bought a total of USD 2,564.5 million from state-owned and dominantly state-owned entities. According to the Central bank law, the Bank of Mongolia fulfilled the role of financial intermediary of the Government of Mongolia by executing principal and interest payments of foreign loans and bonds that total USD 566.4 million.

Figure 3.11: USD auction (USD millions)

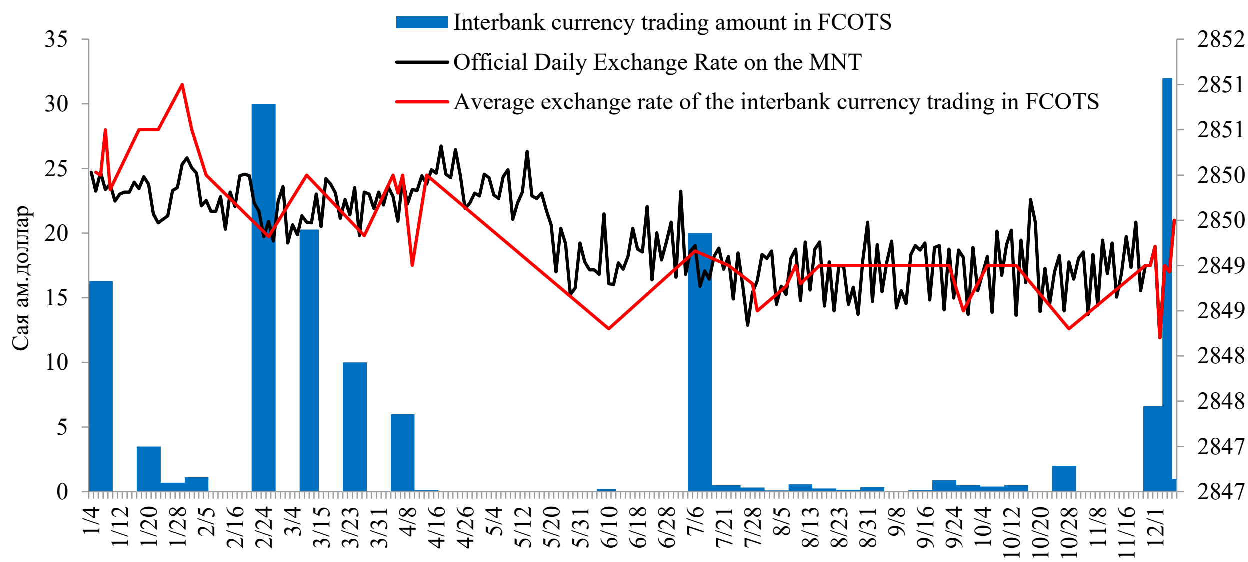


Source: The Bank of Mongolia

Foreign currency online trading system

The “Foreign Currency Online Trading System” not only simplifies the process of currency trading between banks but also improves the process of formation of spot rates in the market by creating equality of information, reducing the customer and settlement risk as well as providing individuals and enterprises with exchange rate information from the field.

Figure 3.12: Interbank currency trading in Foreign currency online trading system (USD millions)



Source:The Bank of Mongolia

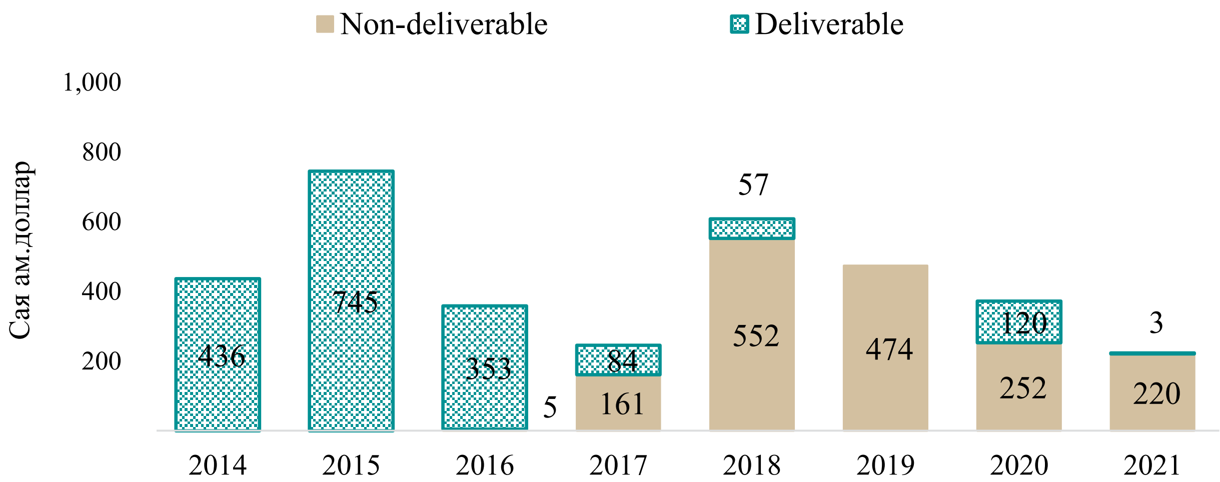
In 2021, banks have executed 50 trades through the Foreign currency online trading system which equals a total of 33.1 million USD. The Bank of Mongolia intervened in the FX market to a net of USD 199 million through the same trading system.

Financial derivatives

The Bank of Mongolia introduced short-term financial derivatives in 2010 and long-term swap agreements in 2014, to support the short-term liquidity of the commercial banks and the economy as a whole, mitigate exchange rate risk, to reduce the pressure on the spot market and dollarization in the domestic FX market.

As the Covid-19 pandemic affected the global financial markets in 2020, the Bank of Mongolia renewed the Long-term swap agreement with Governor's decree no. A-162 on June 30th of 2021. Therefore, low interest rates and the availability of long-term financing will support the economy and reduce the exchange rate risk in the domestic market.

Figure 3.13: Long-term swap agreements between the Bank of Mongolia and commercial banks (USD millions)



Source: The Bank of Mongolia

In the reporting period, the Bank of Mongolia hasn't entered into short-term USD swap agreements with commercial banks. With regards to the long-term swap agreements, the banks make agreements with the Bank of Mongolia using external financings with over one-year maturity. Therefore, in 2021, the long-term swap agreements between the Bank of Mongolia and banks amounted to USD 223.7 million, of which 3.2 million were deliverable and 220.4 million were non-deliverable swaps. Compared to 2020, the total amount of long-term swap agreements has decreased by 37.3%, or USD 138.8 million. Nonetheless, USD 225.8 million of long-term swaps has matured and its outstanding amount decreased by USD 32.1 million to USD 1,625.7 million.

3.6 GOLD FINANCING & PURCHASE OF PRECIOUS METALS

The Bank of Mongolia has started to provide financing to domestic gold mining companies through commercial banks to increase the foreign exchange reserves and to intensify the Gold-2 national program based on the Law on Preventing and combating COVID-19 and Reducing its Social, Economic negative impact, and Parliament Resolution No. 32 of 2020.

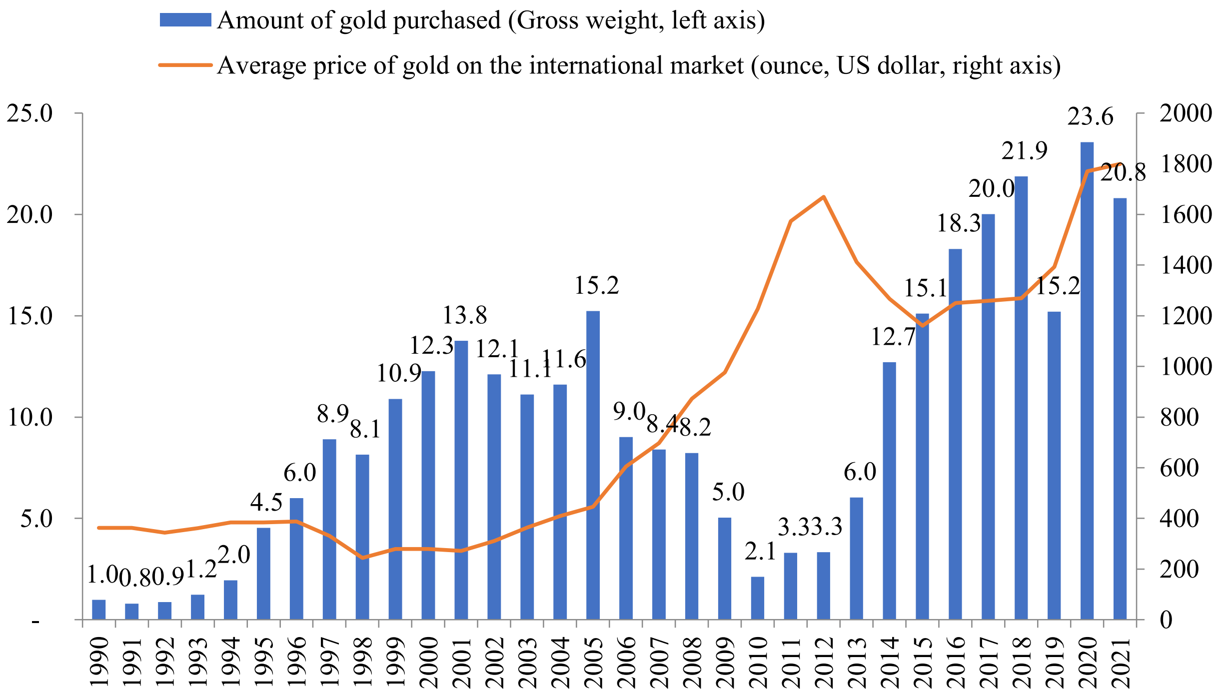
Within the framework of the Gold-2 national program, the Bank of Mongolia has disbursed MNT 23.5 billion in advance payments, MNT 309.7 billion in long-term financing, and a total of MNT 333.2 billion in financing to 15 gold mining companies through 4 commercial banks in 2021.

By the end of the reporting period, the Bank of Mongolia had purchased a total of 4.36 tons of precious metals from 15 gold mining companies that received financing, which was 21% of the total purchases of the reporting year.

The Bank of Mongolia is engaged in the refining of precious metals purchased from the domestic market to increase the foreign exchange reserves in accordance with Articles 7 and 8 of the Law on the Treasury fund.

In 2021, 21 tons of precious metals were purchased from 118 gold mining companies and 73 individuals who hold the special license to trade precious metals and increase the foreign exchange reserve by about 800 million US dollars.

Figure 3.14: Precious metal purchase by the Bank of Mongolia (annually)



Source: The Bank of Mongolia

ORGANIZATIONAL STRUCTURE OTHER ACTIVITIES AND FINANCIAL STATEMENTS OF THE BANK OF MONGOLIA

4

4.1 ORGANIZATIONAL STRUCTURE

The Bank of Mongolia's organizational structure consists of eleven departments, one center, one institute, three independent units in the head office together with five regional divisions, twelve regional branches, and an overseas representative office. The Bank maintained the efficiency of its overall operations with a total of 641 employees, with 520 employees in the head office and 121 employees in the regional branches and divisions.

Within the framework of the medium-term internal operations reform program in 2021, the Bank of Mongolia carried out several activities aimed towards organizational restructuring, strengthening human resource capacity and the legal environment, reinforcing international cooperation, and implementing advanced technologies and practices.

The Bank's organizational restructuring includes dividing the General Management Department into two functions, reorganized into the General Management and the Administration and Planning Department, and the Information Security Unit of the Information Technology Department was incorporated into the Administration and Planning Department. The Public Education and Information Center was divided into two functions, reorganized into the Public Financial Education Center and the Press Unit, and the Press Unit was incorporated into the Administration and Planning Department.

The structure and functions of the Legal Department have been revised.

The Bank has continued to ensure its human resource policy of strengthening human resource capacity, developing leadership skills, improving employee retention rate through continuing to train our employees, and improving their working conditions and compensations, and resolving social issues.

Regarding the implementation of the revised version of the Labor Law from January 1, 2022, the Governor of the Bank of Mongolia approved the new Labor Regulations of the Bank of Mongolia.

The Bank is reforming its information technology system to create conditions for its employees to effectively collaborate online, and to store, share, use and analyze information collected for official purposes in electronic form through introducing the latest technology in its activities.

The Bank of Mongolia is continuously improving its legal environment to redefine the activities of the Bank, form efficient decision-making processes, and improve its transparency and control systems.

The government has approved a detailed action plan for the implementation of the monetary policy guidelines for 2022 and an internal work plan for the Bank of Mongolia.

4.2 FOREIGN RELATIONS

Highlights from the international cooperation of the Bank of Mongolia:

The Bank of Mongolia successfully participated in the “Knowledge Partnership Program” implemented by the Bank of Korea under the “Memorandum of Understanding” signed between the two central banks on August 14, 2011. The joint team of the Bank of Mongolia, Sang Myung University, and the Bank of Korea conducted this year’s research on “Establishing a Central Big Data Processing and Integration System” and published the results of the project.

IMF’s Article IV consultation has been held in Mongolia which contains a tripartite meeting between the IMF, the Bank of Mongolia and the MOF, as well as close discussions between the Bank of Mongolia and IMF on a wide range of topics, including the Banking Law of Mongolia, financial stability, fiscal policy, external debt, and external sector assessments. The Mission expressed the view that it is important to improve the balance between the public and private sectors and ensure macroeconomic and financial stability to overcome the post-pandemic difficulties, prepare for economic recovery and conduct large-scale reforms.

In order to expand the Bank of Mongolia’s foreign relations and initiate new cooperation, a “Memorandum of Understanding” was signed on August 6, 2021, with the State Secretariat for Economic Affairs of Switzerland. The Bank of Mongolia employees will be able to participate in the Bilateral Assistance and Capacity Building for Central Banks (BCC) funded by the Agency. This program will strengthen the capacity of the Bank of Mongolia in monetary policy analysis, macroeconomic research and statistics and bring it closer to international standards. The BCC program of the State Secretariat for Economic Affairs of Switzerland has been implemented since 2013 and focuses on the development of analytical and technical expertise of central banks in developing countries.

The Bank of Mongolia has continued to cooperate with international institutions such as the Asian Development Bank, the International Monetary Fund, the World Bank, and the International Finance Corporation, all providing necessary technical assistance to the Bank of Mongolia online throughout the year.

At the 2021 International Economic Cooperation Forum organized by the Bank of Korea in Seoul, the Deputy Governor G. Enkhtaivan presented in the discussion on Eurasian Economic Cooperation: Digital Transition of Mongolian Banking System. During the forum, the Deputy Governor G. Enkhtaivan held a bilateral meeting with the Deputy Governor of the Bank of Korea, Min Jwa Hong, and exchanged views on issues related to the banking sector of the two countries, cooperation, and joint research.

The Bank of Mongolia participated virtually in a customized bilateral program at the Istanbul School of Central Banking under a 2011 “Cooperation Agreement” with the Central Bank of the Republic of Turkey. In the 2021 program, the Research and Statistics department participated in the “Consolidation and dissemination of consumer loan information” subject.

The Bank of Mongolia was appointed to Steering Committee of the IMF’s Caucasus, Central Asia, and Mongolia Regional Training Center (CCAMTAC). In addition, directors of the Bank of Mongolia’s departments and divisions shared their experiences and made presentations at the e-training organized by the center.

The Bank of Mongolia and the Southeast Asian Central Banks Research and Training Centre jointly organized a monetary policy and financial stability seminar on “Analysis and Modelling of Macro-Financial Linkages” and the event was opened by the Deputy Governor G. Enkhtaivan.

In 2021, the Bank of Mongolia regularly participated in the annual and board meetings of the International Monetary Fund, the World Bank, the Asian Development Bank, the European Bank for Reconstruction and Development, and Southeast Asian Central Banks Research and Training Centre.

The Bank has continued to cooperate closely with the Deutsche Bundesbank, the National Bank of Poland, the Federal Reserve, the Istanbul School of Central Banking, the Swiss National Bank - Study Center Gerzensee, the International Banking and Finance Institute of Banque de France, the International Monetary Fund's Regional Training Institute in Singapore, the Joint Vienna Institute, and the World Bank's Reserves Advisory & Management Partnership program, and other central banks during COVID-19 pandemic to strengthen our human resource capacity and competence.

4.3 COMMUNICATIONS OF THE CENTRAL BANK OF MONGOLIA

International tendency

The main purpose of public relation of the Central Bank of Mongolia is to explain its goal by the law, strategic ways to reach the goal, decisions made by the Central Bank of Mongolia, its basis, and further events to economical participants. This has been an important policy tool which is to evolve internationally to reduce information inequality, manage the expectation of economical participants effectively, set up economic stability. Such tool is to improve efficiency, provide institution openly, and strengthen independence. Since 1990, National banks have begun their main object to ensure the stability of their national currency, which has been given importance to public relation. Specially, the public relation has been an important tool since the world economic crisis from 2008-09. During the crisis, explain the implementing policies openly has been the only way to increase trust and improve policy result of the central banks. Therefore, it's been playing an important role to soften economic shock and stabiles the market during world pandemic covid-19. Economic revival after pandemic depends heavily on clients, business owners, investors, financial participants and their expectation, therefore, public relation has been a highly important.

The Bank of Mongolia transparency, public relations

During the uncertainty of Covid-19, the Bank of Mongolia is implementing policy package to aim to keep the stability of macro economy and financial system, explaining the policy and decisions to public openly. Public relation has been an important tool to prevent financial fluctuations, overcome economic difficulties and support further revive during pandemic. The Bank of Mongolia has worked to improve the quality of public relation and information content, and paid special attention to the following:

- **Policy decisions.** Monetary policy committee has been announcing the meeting date and meeting decisions to public through monetary policy news or press conference.
- **Report, study brochure, statistical news.** Monetary policy decisions ground and calculations, inflation report includes economic analysis, other published reports from the Bank of Mongolia, statistical news have been delivered to public with constant improvements.
- **Information accessibility, targeted groups**. The Bank of Mongolia has been paying more attention to deliver the information contents in a simple way as the brief contents, infographics, posters and videos. Furthermore, the Bank of Mongolia has chosen to deliver the information based on specific demand of professional market participants, decision-making government organizations, international research centers, press organizations and citizens and businesses.
- **Channels of the Bank of Mongolia's public relations.** The Bank of Mongolia website (official website), social media/network accounts have been updated daily with qualified and improved contents. In 2021, press conferences, meetings, seminars, training and other events have been organized online to manage the risks during pandemic.

Transparency and Public relations assessment of the Bank of Mongolia

We are introducing international good practices in the Bank of Mongolia's public relations activities have improved with current needs. As a result, is clear the Bank of Mongolia's Transparency and Relations Assessment (DoBC Consulting 2021) the relative publicity of the Central bank policies and activities has increased.

The assessment collected from the total of 1056 surveys from 9 districts, 158 organizations representative in Ulaanbaatar, the sample survey conducted by an external professional organization shows the following results include:

12) Matrix evaluation has been increased
The people of all the respondents (51%, 42%) matrix evaluation was close to the average sense and the matrix evaluation of remote farthest quarter communities 50%, 42% did not differ from the collection mean. Researchers seems to be more experienced the Bank of Mongolia's activities than the citizen's survey. Participants in the private and public sectors are more confident, more learned and more khowledgeable whereas participants from professional organizations, researchers and regulators are above average confidence. The results of this survey relatively improved than the results of the 2017. It can be seen that it has reached above average level.

2) EG index rating improved
The Eijffinger and Geraats (2002) is used to assess central bank transparency. The EG index has a total 15 questions in 3 subgroups in 5 groups. The questions have 2 or 3 options/answers. The answers are 0, 0.5 and evaluate with a score of 1. The index is calculated as the sum of these scores. The EG index is a minimum of 0 and maximum 15. As the index value moves to 15, this means that the Central bank's transparency is good. The transparency of the Bank of Mongolia according to the EG index 37% of all researchers score 12-15 points, 20% as 6-9 points, 7% as 3-6 points, 1% as 0-3 points and the EG average index is 10.4 points or 69.3 percent.

The Bank of Mongolia's confidence is estimated above average and people having more confidence while organizations have moderate confidence. The Bank of Mongolia's public relations performance was estimated above average in the sample and below estimated by organizations.

In addition, the news, informations and activities provided by the Bank of Mongolia, have reached the public and improved since 2016. Confidence in the Bank of Mongolia is growing and public relations is showing the results.

Research conferences

The Bank of Mongolia's research conference, which encourages students and researchers to conduct economic and financial research, was organized remotely through video conferencing due to COVID-19. The conference was coincided with the 30th anniversary of the establishment of the two-tier banking system in Mongolia. Furthermore, 20 issues of the bi-weekly overview of the external environment reports were published to improve access to research conducted by the Bank of Mongolia and report changes in the global economy and financial markets.

The Bank of Mongolia's Information" newsletter

The Bank of Mongolia had released 6 editions of the "Bank of Mongolia's Information" newsletter and distributed 2800 copies within the central bank's departments, local branches, and to different stakeholders and institutions such as the office of the President, the Government, the Parliament, commercial banks, universities, and provincial officials.

The Bank of Mongolia, The National Police Agency, and the Mongolian Banking Association have jointly organized the 4th campaign under a slogan “ “ from July 19 to October 31, 2021, which aims to warn the public against financial fraud.

Training to provide basic economic and financial knowledge to journalists

In the first quarter of 2021, 30 journalists from several media organizations was enrolled in 4 days of training which aims to provide basic knowledge of economics and finance, and the certificates were awarded to the journalists at the end of the training. Furthermore, it was already planned that the journalists who had completed the basic knowledge training would have undergo advanced training, however it was delayed due to the COVID-19 situation. Moreover, morning meetings and trainings were organized every month to provide journalists with current news and informations about the economy. In those meetings, the Governor of the Bank of Mongolia, the First Deputy Governor, the Deputy Governor and the directors of departments had participated in the meeting by providing information. In 2021, a total of 12 training sessions were held, and about 180 journalists attended the meetings.

4.4 MEASURES OF ANTI-MONEY LAUNDERING AND COMBATING FINANCING OF TERRORISM

The Financial Information Unit (FIU) has implemented the following necessary measures to strengthen Mongolia’s anti-money laundering and combating financing of terrorism (AML/CFT) regime as stated in the Monetary Policy Guidelines for 2021.

I. National strategy

In the Financial Action Task Force (FATF) 40 Recommendations, Recommendation 1 states that countries should identify and assess their money laundering and terrorism financing (ML/TF) risks, and Recommendation 2 states that countries should have national policies and measures which are informed by the risk assessment results. Moreover, the AML/CFT Law stipulates the organization of ML/TF National risk assessment, as well as development and approval of the AML/CFT National policies and programs based on the results of this assessment.

In this regard, ML/TF National risk assessment of Mongolia was conducted in 2020-2021 by a working group established by the decree of the Minister of Finance with 128 representatives from more than 52 public and private sector institutions. The working group assessed the ML/TF risks in each of the regulated sectors, including banking, securities, insurance, and designated non-financial businesses and professions. Based on the FATF 40 Recommendations and the results of the National risk assessment, the FIU has developed “AML/CFT National Strategy of Mongolia” and its action plan in accordance with the Law on development policy, planning and its management and relevant general regulation and methodology. Moreover, under the World Bank project, we have collaborated with an international consultant to develop the National strategy in line with international best practices.

In the “AML/CFT National strategy”, a total of 8 objectives and over 50 sub-objectives were set in order to meet the requirements of international standards and strengthen and improve effectiveness of the AML/CFT regime of Mongolia. The National strategy and its action plan were presented and discussed at the meetings of the National Council, Cooperation Council, and National Counter Terrorism Council for a total of 6 times in 2021. In addition, we have reflected comments received in the National strategy and its action plan and organized a one-day discussion.

As per the amendments made to the Law on development policy, planning and its management and the AML/CFT Law on December 17, 2021, “AML/CFT National strategy” shall be approved by the Parliament, not the Government. In this regard, the FIU in cooperation with the member organizations of the National Council and Cooperation Council has been conducting necessary research for the approval of the National strategy in accordance with the relevant legislations.

This National strategy will help ensure effective implementation of the Action plan for 2021-2030 under the “Vision-2050” Long-term development policy of Mongolia approved by the Resolution No.52 of the Parliament in 2020, Guideline for the five-year development of Mongolia in 2021-2025 approved by the Resolution No.23 of the Parliament in 2020, and the Government Action Plan for 2020-2024 approved by the Resolution No.24 of the Parliament in 2020.

II. Domestic and international cooperation

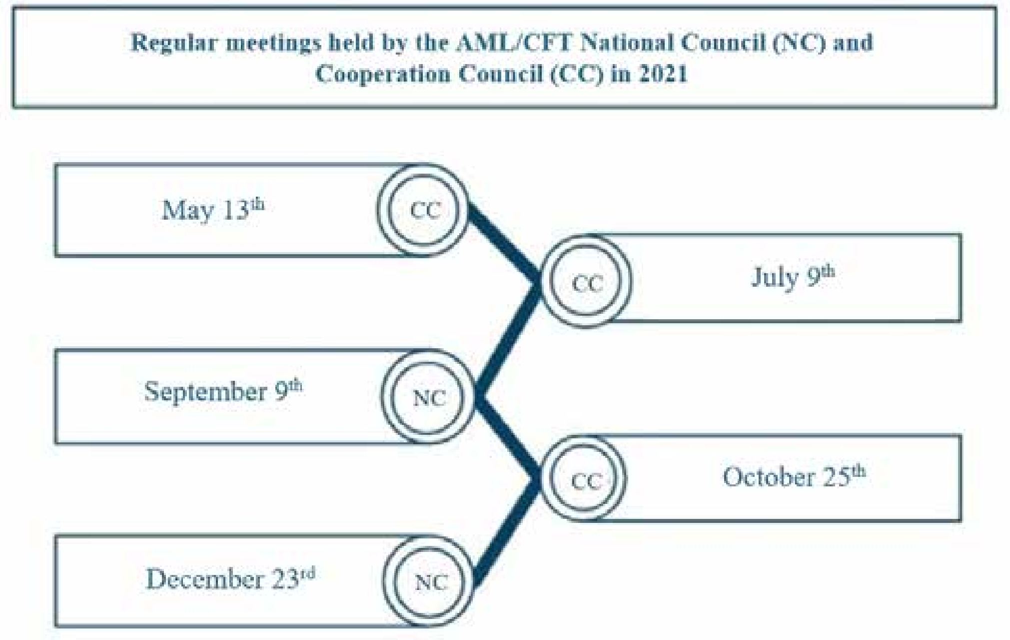
International and domestic cooperation among the public and private sector institutions plays a significant role in strengthening AML/CFT framework. In this regard, the FIU acts as the secretariat of the AML/CFT National Council and Cooperation Council which consist of representatives from more than 17 government authorities. Throughout 2021, the FIU has closely cooperated with the international bodies and member organizations of the National Council and Cooperation Council, as well as the private sector.

Figure 4.1: Member organizations of the AML/CFT National Council and the Cooperation Council

Source: FIU, Bank of Mongolia

In 2021, the AML/CFT National Council held a total of 2 meetings, whereas the AML/CFT Cooperation Council held 3 meetings as follows:

Figure 4.2: Meetings held by the AML/CFT National Council and Cooperation Council



Source: FIU, Bank of Mongolia

The National Council and the Cooperation Council discussed and resolved following key issues in strengthening AML/CFT framework during their regular meetings held in 2021:

- AML/CFT National risk assessment report of Mongolia;
- Draft AML/CFT National strategy and its action plan;
- Submission of Mongolia's Follow-Up Report of 2021 & 2022 to the Asia Pacific Group on Money Laundering for upgrading the technical compliance ratings of the FATF 40 Recommendations;
- Requirements for reporting to the Asia Pacific Group on Money Laundering;
- Regulatory framework, further developments and AML/CFT risk assessment of the virtual asset sector;
- "Action plan to address the AML/CFT deficiencies in technical compliance of the FATF 40 Recommendations" approved by the Chairman of the National Council and the Minister of Justice and Home Affairs on September 27, 2021 and the implementation progress of the action plan;
- Cooperation with the local universities in enhancing the AML/CFT capacity.

The member officials of the Cooperation Council were renewed by the Decree No. A-110 of the Governor of the Bank of Mongolia dated May 4, 2021. This Council is chaired by the Bank of Mongolia and consisted of 27 representatives from 17 government agencies. Moreover, five working groups were established under the Cooperation Council on conducting research and analysis, implementing targeted financial sanctions, improving the legal environment, supervision and law enforcement. Action plan of each working group was approved and being implemented.

The Cooperation Council signed a Memorandum of Understanding with the University of Internal Affairs of Mongolia on December 17, 2021 to strengthen the AML/CFT capacity in Mongolia. In this regard, the Memorandum of Understanding will focus on enhancing the capacity building of the workforce, training the trainers, conducting research and analysis, and organizing outreach activities for combating the money laundering and terrorism financing.

For enhancing the foreign cooperation, the FIU worked closely with international organizations for combatting the money laundering and financing of terrorism in 2021. For instance, technical assistance projects have been implemented with international donor organizations such as the World Bank, the Asian Development Bank, and the U.S. Department of the Treasury. In addition, the FIU has not only provided necessary information and research to the following international organizations, but also actively organized their virtual trainings and workshops in 2021: FATF, Asia-Pacific Group on Money Laundering, Eurasian Group on combating money laundering & financing of terrorism, and Egmont Group. In this regard, the FIU has organized over 15 international seminars, trainings, and conferences in which more than 575 representatives from the member organizations of the National Council and the Cooperation Council as well as the private sector participated in duplicate numbers.

III. Supervision

In order to ensure effective implementation of the AML/CFT Law, the FIU has been regularly collaborating with the supervisory bodies such as Bank of Mongolia, Financial Regulatory Commission, and professional associations. In this regard, the FIU has provided necessary support for the following professional associations in monitoring the compliance of reporting entities with their legal obligations in 2021: Mongolian Bar Association, Mongolian Advocates' Association, Mongolian Chamber of Notaries, and Mongolian Institute of Certified Public Accountants.

As a part of outreach activities, guidance on the supervision of designated non-financial businesses and professions was developed for the professional associations. In addition, supervisors of the regulatory bodies attended in the virtual trainings and seminars by the international organizations on topics such as risk-based supervision, cooperation, and information exchange, and the FIU organized trainings for reporting entities on fulfilling their AML/CFT obligations and raising awareness on the associated risks.

The FIU publishes consolidated statistics on supervision conducted by the regulatory bodies for combating money laundering, terrorism financing and proliferation financing (PF) of weapons of mass destruction. The following table shows the supervision statistics and actions taken against all the reporting entities (Table 4.1):

Table 4.1: AML/CFT/PF supervision statistics

Items	2018	2019	2020	2021
Number of on-site examinations on banks	14	24	19	17
Number of on-site examinations on reporting entities other than banks	1025	269	146	5897
Number of administrative action notes issued to banks and other reporting entities	4	-	1	47
Number of rectification orders issued to banks and other reporting entities	272	245	444	261

Source: FIU, Bank of Mongolia

IV. Receipt of Information

The FIU receives Cash transaction reports (CTR) and Foreign settlement transaction reports (FSTR) of MNT 20 million or more as well as Suspicious transaction reports (STR) from the reporting entities specified in Article 4 of the AML/CFT Law. Additionally, the FIU receives Customs declaration reports of MNT 15 million or more in cash or its equivalent in foreign currency, financial instruments and electronic money according to the Article 15 of the AML/CFT Law (Table 4.2).

There was a need to improve data collection form since it was time consuming to prepare detailed and breakdown statistics required for the FATF's Mutual Evaluations, National Risk Assessment, and other reports on AML/CFT. In this regard, the "Regulation on statistical information of the Financial Information Unit" was updated and approved by the Decree No. A-93 of the Governor of the Bank of Mongolia on March 31, 2021. In the new forms, statistics were classified separately for each reporting entity with detailed breakdown in terms of both quantitative and qualitative characteristics.

Table 4.2: Number of reports received by the FIU (2018-2021)

Name of report	2018	2019	2020	2021
Cash transaction	669,910	562,926	402,496	336,518
Suspicious transaction	1,596	2,385	3,014	1,801
Foreign settlement transaction	126,944	131,715	143,191	211,176
Customs declarations received	1,413	11,870	5,520	2,660

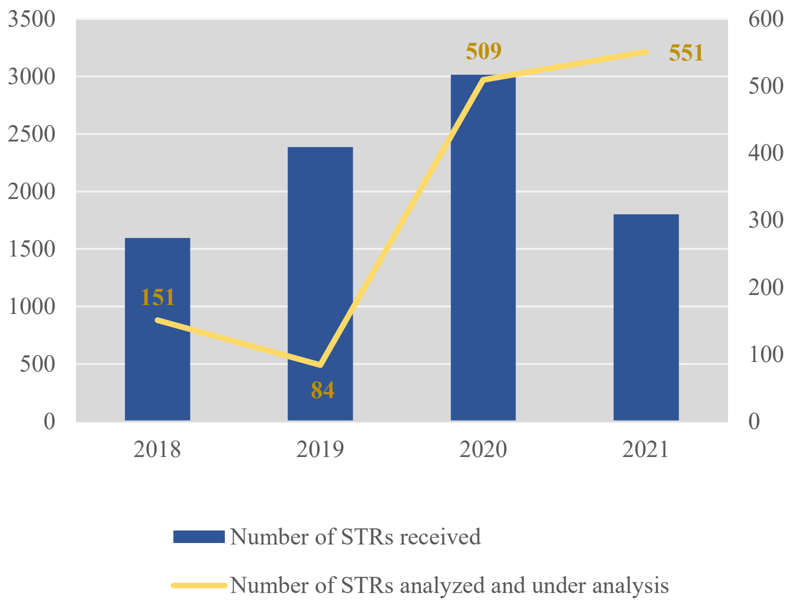
Source: FIU, Bank of Mongolia

In 2021, a total of 1,801 STRs were received, a 41 percent decrease from the previous year and a 52 percent decrease in the number of customs declarations report since border, customs, travel and domestic traffic have been restricted due to the Covid-19 global pandemic. However, the number of FSTRs increased by 32 percent compared to the previous year.

V. Analysis of Information

According to the Article 18.1.1 of the AML/CFT Law, the functions of the FIU are defined as receiving, collecting, and analyzing information reported from reporting entities, as well as information in databases of relevant local and foreign institutions. In this context, the FIU analyzed the following STRs in 2021 (Table 4.3).

Figure 4.3: Number of STRs received, analyzed and in the process of analysis (2018-2021)



Source: FIU, Bank of Mongolia

Table 4.3: Number of STRs received, analyzed and in the process of analysis (2018-2021)

Items	2018	2019	2020	2021
Number of STRs received	1,596	2,385	3,014	1,801
Number of STRs analyzed and in the process of analysis	151	84	509	551

Source: FIU, Bank of Mongolia

Although the number of STRs received decreased compared to the previous year, the number of STRs analyzed and in the process of analysis increased by 7.6 percent from the previous year. This is due to the fact that the FIU analysts regularly participated in relevant trainings and seminars and strengthened their skills and capabilities.

VI. Exchange of information

VI.a. Exchange of information and cooperation with domestic organizations

Within the framework of domestic cooperation, FIU cooperates and collaborates with competent domestic authorities by exchanging information and providing support and assistance with the investigation and prosecution of crimes within the framework of preventing and combating money laundering, financing of terrorism, and proliferation of weapons of mass destruction in accordance with the Article 18.6 of the AML/CFT Law. In this regard, the following information was exchanged in 2021 (Table 4.4).

Table 4.4: Information exchange between the FIU and competent authorities

Items	2018	2019	2020	2021
Number of information disseminated to domestic law enforcement authorities from FIU for further investigation	181	48	505	539
Number of inquiries obtained by FIU from domestic law enforcement authorities for information exchange	2,510	2,396	3,336	3,665
Number of responses to inquiries received from domestic law enforcement authorities	2,300	2,634	3,310	3,834

Source: FIU, Bank of Mongolia

The FIU exchanges information with domestic authorities following the relevant legislation; thus, from 2020, FIU has signed an agreement with the General Authority for State Registration to obtain the right to access the electronic state registration database. Therefore, in the context of implementing this information exchange and cooperation agreement, the FIU is electronically accessing inquiries and information on the initial registration of individuals and legal entities for its internal use.

For combating money laundering and terrorism financing, cooperation and coordination are crucial not only for government agencies, but also for the private sector, including banks, non-bank financial institutions and designated non-financial businesses and professions. Accordingly, we are in search for international best practices to improve and simplify the information exchange between the public and private sectors in the field for combating money laundering and terrorism financing.

VI.b. Exchange of information with Foreign Counterparts

In accordance with the FATF Recommendation 29, the FIU exchanges information related to money laundering, terrorism financing, and other predicate offenses with the other foreign FIUs, including Egmont Group members and other FIUs on the basis of signed Memorandum of Understanding. Thus, the exchange of information with foreign counterparts over the recent years are as follows (Table 4.5).

Table 4.5: Information exchange with foreign counterparts

Items	2018	2019	2020	2021
Number of requests sent by FIU-Mongolia to the foreign FIUs and similar organizations	231	238	353	140
Number of responses to requests sent to foreign FIUs and similar organizations	193	202	247	165
Number of requests received by FIU-Mongolia from foreign FIUs and similar organizations	126	133	123	149
Number of responses to requests received by FIU-Mongolia from similar foreign organizations	126	144	112	129

Source: FIU, Bank of Mongolia

The FIU exchanges information and organizes trainings and seminars to cooperate in the field for combating money laundering, and terrorism financing in accordance with the Memorandum of Understanding between FIUs. In this regard, FIU started the process for signing the Memorandum of Understanding with three foreign counterparts in 2021, including the FIU of the Macao Special Administrative Region of the People's Republic of China, the FIU of Timor-Leste, and the Cambodia FIU to expand international cooperation. Later, in November 2021, we have completed the necessary process and signed the Memorandum of Understanding with the FIU of Timor-Leste.

VII. Information system and software

The FIU has started introducing goAML program since December 2019 to increase the efficiency of the implementation of its functions described in relevant legislation, including receiving information related to money laundering, terrorism financing, or related crimes as well as other financial information from reporting entities, conducting analysis, and disseminating information to law enforcement authorities based on the analysis result.

The FIU focused on implementing the goAML program in 2020-2021. In cooperation with banks, we developed a data reception scheme of the goAML program per the internal system of banks, instructed banks on how to send and receive three types of reports and transactions specified in the law, and identified and corrected errors promptly.

In the first and second quarters of 2021, the guidance for software users and reporting entities of the goAML program was translated and delivered to the reporting entities. On March 25, 2021, we have started the testing of the portal for receiving reports of the goAML program with banks. Also, template file was created for additional information in the suspicious transaction report and completed the test, reflecting the relevant suggestions. Furthermore, in the third quarter of 2021, we held two online meetings with relevant bank employees to discuss software use, errors, and correction. Furthermore, FIU analysts' training, and troubleshoot errors during the portal usage and test reporting of banks continued throughout 2021.

As a result, all banks have been introduced to goAML software in advance and started sending reports. Further, the FIU intends to connect all non-bank reporting entities to the goAML portal in 2022 and officially receive information from all reporting entities through the software.

VIII. Awareness raising activities

The FIU has developed and disseminated the following awareness-raising documents on anti-money laundering and terrorism financing for reporting entities in 2021:

- Strategic Analysis Report – 2020
- Annual report of FIU-Mongolia – 2020
- Official translation of FATF's "Guidance for a risk-based approach to Virtual Asset and Virtual Asset Service Providers"
- Guidance on Virtual Assets Overview, Market and Regulation has been developed for regulators and working group members and has been disseminated to relevant officials.
- "Suspicious Transaction Reporting Guideline" and "Red flag indicators of Money Laundering and Terrorist Financing" for non-bank financial institutions, insurance companies and insurance licensed entities, licensed securities market entities, savings and credit cooperatives, real estate brokers, and dealers of precious metals and precious stones.
- "Virtual Assets – Red flag indicators of Money Laundering and Terrorist Financing" for Virtual asset service providers.

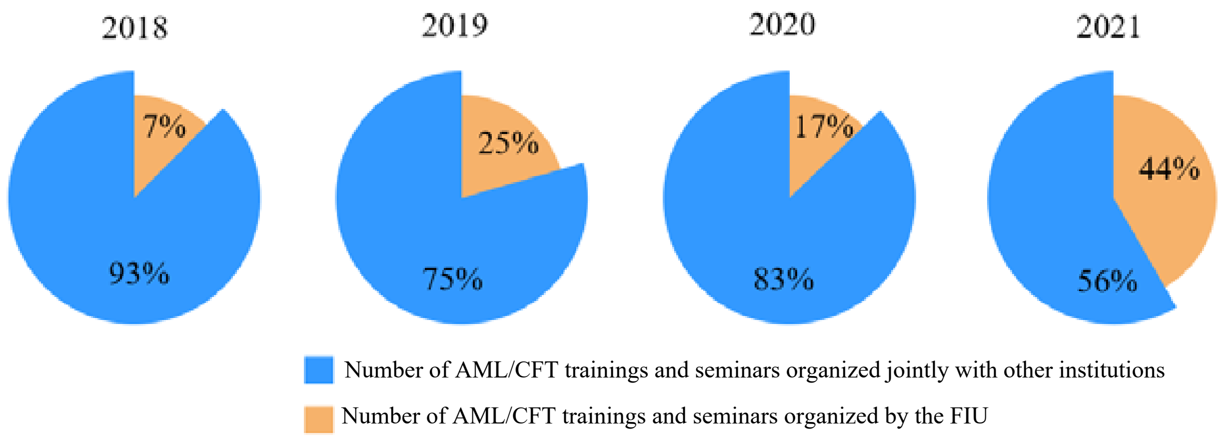
Above mentioned guidelines and recommendations have been published on the FIU's website, fiu.mongolbank.mn.

IX. Strenghtening capacity and improving efficiency of resources

The FIU has been continuing to work with the U.S Department of the Treasury's Technical Assistance Program to build the capacity of analysts and educate the staff on the new aspects of AML/CFT activities and recent changes. Within the framework of international and domestic cooperation, the FIU staff members regularly participated in professional trainings and seminars on combating money laundering and terrorism financing, also regularly organized outreach activities on combating and preventing from money laundering and terrorism financing.

For example, in 2021, the FIU organized a total of 34 trainings individually and in cooperation with relevant authorities. More than 2,700 representatives of the public and private sectors participated in these training with the key topics, including regulatory environment of the virtual asset sector, the methodology for identifying the beneficial owner, e-gambling operations, the nature of related suspicious transactions, the prevention of e-fraudulent transactions, FATF 40 Recommendations, international practice, and risk-based supervision.

Figure 4.4: Number of AML/CFT trainings, seminars and attendees organized by the FIU and jointly with other institutions (2018-2021)



Items	2018	2019	2020	2021
Number of AML/CFT trainings and seminars organized by the FIU	1	7	4	15
Number of attendees of AML/CFT trainings and seminars organized by the FIU	40	444	136	1377
Number of AML/CFT trainings and seminars organized jointly with other institutions	13	21	20	19
Number of attendees of AML/CFT trainings and seminars organized jointly with other institutions	543	1081	886	1387

Source: FIU, Bank of Mongolia

4.5 INTERNAL AUDIT

The Internal Audit Department has performed its main function to support the Bank in achieving its goals and objectives by reducing operational risks, conducting on-site audits and remote surveillance, making recommendations on improving risk management and internal control, and monitoring its implementation.
The Internal Audit Department carried out 13 comprehensive on-site audits and 7 partial audits as per the annual audit plan approved by the Governor of the Bank of Mongolia in 2021. The audit findings and recommendations were presented to the Board of Directors, further actions and recommendations were issued, and its implementations were closely examined.

The Department coordinated the assurance process of the Bank of Mongolia's financial statements of the year of 2020 undertaken by an external auditor and monitored the implementation of the recommendations given by the external auditor.

To introduce a risk based audit methodology in the Internal Audit Department operations, we have been working with the World Bank "Strengthening Fiscal and Financial stability Project" in Mongolia and were provided consulting services. The work plan for 2021 was developed and agreed with the consultant. The comparative study has been done based on materials submitted by consultant and other countries information technology auditing methods as well as the COBIT system, the "General Information technology audit guidelines of the Bank of Mongolia" were first drafted and based on international standards related to risk assessment the "Guidelines for Audit Risk assessment and Audit Plan Development" draft were developed.
In addition, the "Internal Audit Charter of the Bank of Mongolia" has been updated in accordance with international standards, and the draft charter is to be improved further bringing it into line with the specifics of the Bank of Mongolia.

The request of extension of "Strengthening Fiscal and Financial Stability Project" has been submitted and approved, and we are continuing to work with the World Bank consultant to update the Bank of Mongolia's internal audit operations in line with international standards.

4.6 RISK MANAGEMENT

During the reporting year, the Risk Management Unit (RMU) set the long and mid-term strategic asset allocations, benchmarks, and limits and monitored the performance of the strategic asset allocation and compliance of the limits and executed reporting. Within risk management related to domestic market operations, the RMU established the list of eligible assets to be pledged as collateral for central bank financing operations, developed methodologies for collateral evaluation, determined the discount rates, and monitored its compliance. Moreover, within the operational risk management framework, potential operational risks are identified, assessed, controlled, reported, and managed to maintain at the lowest level.

Financial risk management

Credit risk

As part of credit risk management, the deposit limit of the official foreign exchange reserves has been set by investment type, customer bank and financial institution, credit rating, and country. In order to prevent credit risk that may arise from the persisting uncertainty covering global economy and financial markets due to Covid-19 situation, the reserves were placed mainly at the central banks of developed countries, government-guaranteed institutions and international financial institutions. In addition, in order to limit credit risk, the maximum amount of deposits to be placed in foreign banks and financial institutions was determined by the portfolio optimization method. The strategic investment structure was approved and its implementation was monitored.

During the reporting period, in terms of concentration risk management, credit risk models and best practices of central banks and international financial institutions were used to set limits on respective banks and financial institutions, and market-based measures such as assessing credit risk exposed from market movement, were adopted in credit risk management. Moreover, we have planned to further develop the approach and methods used for the assessments as part of actions to improve credit risk management.

Regarding the credit risk management of domestic market operation, the Bank of Mongolia has made projections on the expected credit loss for financial assets in accordance with the International Financial Reporting Standard 9, based on which it has established a provision and made it possible to properly manage risks in the event of actual risk. In addition, research was carried out to determine new types of eligible collateral, methodology for estimating their fair value, and determining their discount rate. Accordingly, the list of eligible collateral for central bank financing was renewed. Specifically, the RMU conducted research on collateral policy and analyzed the financial assets of the Bank of Mongolia and collateral with its guarantees under central bank financing. The relevant risk management measures were taken following the working plan approved by the Governor of the Bank of Mongolia. Furthermore, the study of the best practices of other central banks and research works was conducted to improve the methodology for revaluation of financial assets of the Bank of Mongolia and results were reflected in amendments of related regulations and guidelines. In addition, the daily trading limit for the participants in the interbank foreign exchange trading system was calculated, and the primary dealer of the foreign exchange trading system was selected on a quarterly basis, with its implementation regularly monitored. Research on executing the valuation of derivative transactions with domestic banks using the above mentioned system has commenced.

Market risk

Within the framework of foreign exchange reserves management, the types and amount of foreign exchange required for repayment of foreign debt and minimizing exchange rate risk are determined based on the togrog exchange rate policy, structure of foreign debt payments of the government, import structure, projected foreign exchange outflows by domestic banks, and structure of the domestic foreign exchange market. The implementation of the foreign exchange reserves management was regularly monitored. At the same time, to minimize the risk of depreciation of investment instruments due to changes in the market interest rates, the risk of interest rate fluctuations was managed by determining the duration and the optimal amount of deviations for each reserve tranche.

Due to low interest rate environment resulted from the easing policies of governments and central banks to cushion the negative effects of the Covid-19 pandemic, impact of global supply chain disruption, and world economic recovery, fluctuations in the commodity market, especially the high volatility in gold market prices has necessitated a more specific assessment of market risk. Therefore, we upgraded the software for market risk calculations of foreign exchange reserves and started estimating market risks on daily basis. Furthermore, we established a projection method for determining the investment structure of foreign exchange reserves in case of abrupt movement in the low interest rate environment and started utilizing it in the calculations of the strategic investment.

During the reporting year, financial assets owned by the central bank under the “Troubled Asset Relief Program” were valued at fair value following the Accounting Policy Document of the Bank of Mongolia and potential market risks were reflected in the balance sheet. Additionally, the collaterals of the financial assets were recalculated at fair value. Moreover, revaluation of long-term swap agreements made with domestic banks to protect against exchange rate risk, increase foreign exchange flows, and reduce interest rates and foreign currency lending, is done on weekly basis and it is reflected in the balance sheet.

Liquidity risk

Within the framework of foreign exchange reserves management, the total portfolio was divided into short-term and long-term investment tranches to prevent liquidity risk. The short-term portfolio was placed mainly in international financial organizations and central banks amid persistent economic and financial market uncertainty caused by the Covid-19 pandemic, despite of recovering signs of the developed economies in 2021.

In order to determine the adequacy of the reserves, the optimal short-term liquidity portfolio was determined based on macro indicators such as short-term and long-term external liabilities, export and import projections, in accordance with the methodologies commonly used by the IMF and other central banks. We have also managed and placed the reserves in highly liquid instruments such as current accounts, short-term deposits and short-term government securities to ensure the highest liquidity.

Monitoring and reporting foreign exchange reserves management

The market valuation, reporting of risk, and return performances of the foreign exchange reserves were conducted daily, and the established investment structure and limit performance were monitored and reported. Additionally, financial indicators and updates on credit ratings, stock price and news about foreign counterparties were scrutinized and results of analysis were used for credit risk analysis and presented to the management on a quarterly basis. Moreover, foreign exchange reserves management reporting principles and practices of other central banks and international financial institutions were analyzed, and the best practices were introduced in our reserve management reporting.

Operational risk management

In the reporting year, we worked with the World Bank, studied the theoretical researches and the best practices from other central banks to improve our operational risk management framework, strengthen the risk governance system, and successfully utilized the risk identification and assessment tools.

The more precise and detailed “Plan to ensure the safety and continuity of the main operations of the Bank of Mongolia in case of Covid-19” was newly developed and approved in order to improve the ability to ensure preparedness of the “Plan to ensure the safety and continuity of operations of the Bank of Mongolia in case of pandemic”, which was approved in 2020. In addition, a new cost-benefit analysis methodology for operational risk management was studied and introduced, and a new “Guidelines for cost-benefit analysis” was developed and approved.

For the sixth year in a row, Risk Control and Self-Assessment, a commonly used assessment tool for operational risk management, has been conducted by all employees and action has been taken based on the results. In previous years, these assessments were conducted electronically, but in the reporting year, an assessment software was introduced to reduce the manual work associated with the process of risk assessment by staff, consolidation, and evaluation of operational risks. It was an important step to reduce human error and to make data available for dynamic analysis of risk evaluation. In addition, inclusion of information on a risk event in the risk database, whenever it occurs and regularly monitoring and reporting to management on the performance of key operational risk indicators (KRIs) make an important contribution to measuring operational risk in real terms, identifying the root causes of the risk factors and taking appropriate action. During the reporting period, RMU conducted a process mapping and risk assessment of the Bank of Mongolia's accounting process of salaries, bonuses and vacation pay, and based on the results, took appropriate measures to reduce operational risks in those operations.

Regular trainings and meetings with the appointed operational risk management officers at each business units are the main gateways for information sharing and establishment of the risk management culture within the Bank of Mongolia that promotes dissemination of risk management knowledge and practice and supports cooperation among units. In the reporting year, training on operational risk management was developed in the form of a video in response to the pandemic outbreak and distributed to all units.

4.7 CASH MANAGEMENT

In accordance with the Central Banking Act, the Bank of Mongolia, within the framework of its exclusive right of issuing Mongolian national currency, conducts activities related to issuance, withdrawal and maintaining a proper denominational structure of currency in circulation.

Development of Cash in Circulation

By the end of 2021, the total value of cash in circulation reached 1,105 trillion MNT, increasing by 11.5 percent or 114.1 billion MNT compared to the same period of the previous year. The volume of cash in circulation increased by 5.5 percent or 27.3 million pieces compared to the previous year and reached 526.4 million pieces.

Table 4.6: Changes in cash in circulation

№	Denomination	Volume (million pieces)		Value (million togrog)	
		2021	2020	2021	2020
1	1 togrog	33.6	33.2	33.6	33.2
2	5 togrog	152.6	150.7	30.5	30.1
3	10 togrog	1,072.2	1,025.2	107.2	102.5
4	20 togrog	1,800.1	1,715.1	90.0	85.8
5	50 togrog	3,817.8	3,532.8	76.4	70.7
6	100 togrog	7,460.7	6,993.9	74.6	69.9
7	200 togrog	36.7	36.6	0.2	0.2
8	500 togrog	8,665.8	8,240.0	17.3	16.5
9	1000 togrog	20,588.0	20,490.8	20.6	20.5
10	5000 togrog	79,927.1	77,617.8	16.0	15.5
11	10000 togrog	218,555.0	211,975.6	21.9	21.2
12	20000 togrog	763,441.3	659,619.7	38.2	33.0
Total		**1,105,550.9**	**991,431.3**	**526.4**	**499.1**

Source: The Bank of Mongolia

Over the past one year, banknotes of all denominations grew in both value and volume. In particular, the 20000 togrog note had the highest growth rate of 20.7%.

In terms of value, the high-denomination banknotes accounted for the majority of currency in circulation. Specifically, 10000 togrog and 20000 togrog notes together accounted for 88.9 percent of the total value of cash in circulation in 2021, of which 69.1 percent were 20000 togrog notes.

The share of the remaining notes in the total value decreased by 0.9 percentage points from the previous year and reached 11.2 percent. This is related to the fact that the demand for the high-denomination banknotes has been increasing every year.

Figure 4.5: Denominational structure of cash in circulation by value

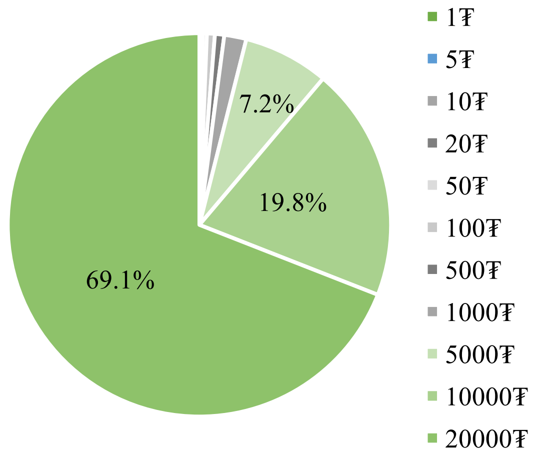
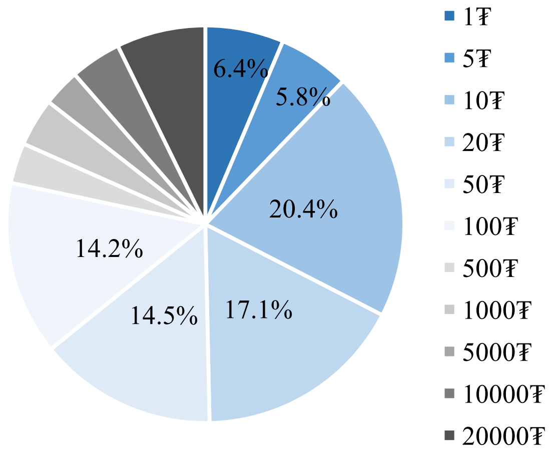


Figure 4.6: Denominational structure of cash in circulation by volume



Source: The Bank of Mongolia

At the end of the reporting year, low denomination notes from 1 to 100 togrog accounted for 78.3 percent of total volume of cash in circulation, and the remaining notes accounted for 21.7 percent. This is due to the fact that low-value notes are less used for payments and therefore remain in the hands of individuals outside the bank and are not returned from circulation to the central bank.

Reprinting of banknotes

As part of its activities concerning issuing, reprinting, safekeeping and reserving of national currency, the Bank of Mongolia focuses on improving the security features of banknotes with the latest technologies in order to prevent counterfeiting and ensure the public confidence in the national currency.

Banknotes with upgraded security features

The renewed denominations of 100, 500 and 1000 togrog, which were reprinted in 2020, were put into circulation from February 8, 2021. These banknotes had been upgraded with highly secured features such as 3 dimensional color-shifting feature which changes its color when tilted and a tactile feature for visually impaired individuals.

Commemorative Banknotes

On the occasion of the 100th Anniversary of the People's Revolution, the Bank of Mongolia issued a 10000 Togrog Commemorative Banknote with high level, modern security features and introduced to the public on July 10, 2021.

The Commemorative Banknote has the following features:

- The Logo of the 100th anniversary of the People's Revolution is a 3 dimensional, color-shifting feature that changes color from green to gold when tilted;
- The horseman on the lower-right corner of the banknote is a 3 dimensional, color-shifting feature and contains rings of different colors moving their positions when tilted;
- 7 raised lines are tactile features for visually impaired;
- The windowed security thread with the text "100 years of the People's Revolution" in Mongolian;
- Soyombo visible under UV light.

In addition, on the reverse side of the commemorative note, there is a portrait of the leader of the People's Revolution D.Sukhbaatar alongside his declaration of independence with the map of Mongolia behind. The map of Mongolia is an interactive new feature which turns from blue to yellow under UV light and when the map area is rubbed gently with hard objects the rubbed mark disappears in some time.

Activities against counterfeiting of currency

In accordance with Article 9 of the Law on the Central Bank, the Bank of Mongolia fights against currency counterfeiting, determines banknote's authenticity and destructs counterfeitted notes.

According to the report from 2010, mostly higher denominations from 500 togrog were counterfeited, and 20000 togrog accounted for 88.4% of these counterfeits, 9% were 10000 togrog, and the remaining 2.7% were 500, 1,000 and 5,000 togrog notes.

Whoever involved in such action and used counterfeit notes shall be charged under Article 18.7 of the Criminal Code of Mongolia "Making, using of counterfeited banknotes, securities or payment instruments". In particular, a conviction for the making or deliberate use, storage, carrying and delivery of counterfeit national currency entails imprisonment for a term of 2 to 8 years.

As part of its activities to combat counterfeiting, the Bank of Mongolia continues to improve the quality, design and security features of banknotes in line with international advanced technologies. In particular, since 2018, banknotes of 50, 100, 500, 1000, 5000 and 20000 togrog have been upgraded with advanced security features.

Furthermore, relevant trainings and promotions are organized on a regular basis, in order to prevent counterfeiting and educate the public about the security features of banknotes.

During the reporting period, an online training was held on the topic "Mongolian banknotes, their security features and counterfeiting" as a part of a seminar for commercial bank employees organized by the Economic Research and Training Institute of the Bank of Mongolia. In addition, educational posters and leaflets on the security features of the new 100, 500 and 1000 togrog banknotes were printed and are ready for distribution to commercial banks and public places, and a video introducing the security features of the 10000 togrog commemorative banknote was posted on the Bank of Mongolia's website and other social networks.

The impact of the Covid-19 epidemic on cash demand

In general, the amount of cash in circulation mainly follows the fluctuation of the economic growth. However, with heightened uncertainty due to sudden shocks and crises, people trust more in cash and the demand for cash increases. This pattern is clearly observed during the 2020-2021 COVID-19 pandemic.

In 2019, the value of cash in circulation decreased by 7% compared to the previous year and reached 897.4 billion MNT, which led to an expectation of a possible decrease in demand for cash in the future. However, despite the contraction of the economy by 5.3 percent in 2020, due to the public preparedness for disasters and imposing lockdowns, cash in circulation increased by 10 percent at the end of the year, reaching 991.4 billion MNT. This confirms the fact that during pandemic, when uncertainty increased, general public prefers to have cash on hand and hoard cash.

Figure 4.7: Growth of cash in circulation in terms of value

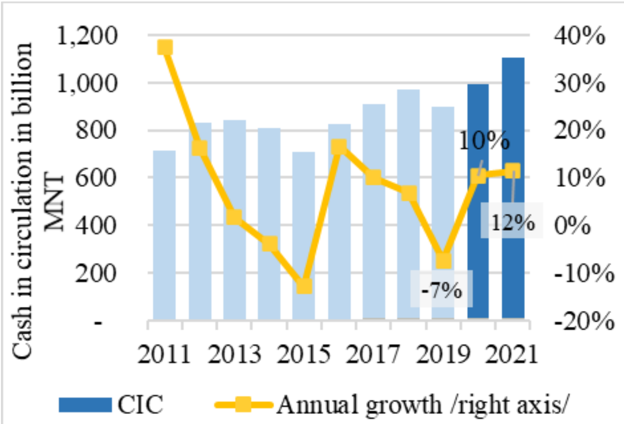
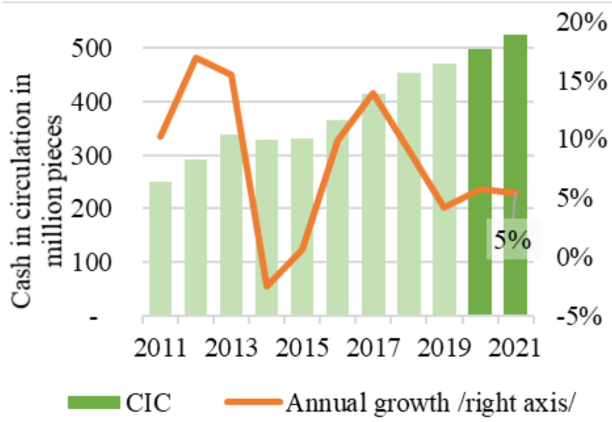


Figure 4.8: Growth of cash in circulation in terms of volume



Source: The Bank of Mongolia

In 2021, as the economy gradually improved and the risk of the pandemic decreased, the value of cash in circulation reached a historical high of 1.1 trillion MNT. This increase is 12 percentage points higher than in 2020 and is the highest increase in cash in circulation since 2017. Thus, the demand for cash in Mongolia has increased over the years of the COVID-19 pandemic.

4.8 INFORMATION TECHNOLOGY

In 2021, the Information Technology Department of the Bank of Mongolia ensured the safety, reliability and uninterrupted operation of the interbank payment system, the interbank foreign exchange trading platform, credit scoring system and the electronic information systems used in the organizations internal operations.

In addition to improving and upgrading existing systems, the following activities have been implemented by introducing a new techniques and technologies into our operations. Such as:

- Developed and launched a new long-term swap agreement program in the field of interbank foreign exchange trading platform. By implementing such program, it eliminated the possibility of mechanical errors, and allowed banks to control previously concluded and active agreements and updated rates while prior operation was done manually by hand.
- Developed a new foreign exchange trading system to trade Bank of Mongolia with business entities. Frequent and high repetitive paper basis FX trading with banks and large business entities requires time-consuming and labor-intensive costs. This critical process has been automated to prevent errors and reduce time and costs.

- Individuals and business entities can now obtain loan information from their financial institutions directly from the e-Mongolia system. The Bank of Mongolia’s credit database system has been connected to the National Data Center’s e-Mongolia system, and new software has been developed and launched to enable citizens and businesses to obtain their credit information free of charge.
- Developed and launched software to connect Bank of Mongolia’s internal systems to the National Data Center’s HUR system. As a result, the departments and offices of the Bank of Mongolia have been able to verify the accuracy of the information used in their operations through the HUR system.
- Credit information of 44,612 individuals and business entities from the credit database has been excluded. In accordance with the order of the Governor of the Bank of Mongolia, individuals and business entities had met the requirements of no more than one overdue or bad credit history, and the loan must be repaid before July 1, 2021, was not included in the credit information inquiry.
- Developed and launched goAML system for the need of Financial Information Unit. The basic and test environment, software, database and network protection of this new system have been fully implemented and put into full operation.

Furthermore, we have taken further measures to ensure the continuous operation of information technology, improve information security and prevent viral and cyber-attacks.

4.9 SUMMARY OF LEGAL ACTS AND DECREES ISSUED BY THE BANK OF MONGOLIA IN 2021

1	Regulations of state inspector	2021.02.01	A-37	Determines the legal status and redefined basic principles of its duty.
2	The operation control of the security unit operator guideline	2021.02.03	A-41	Ensures the security of electronic transaction centers.
3	Sandbox regulatory environment regulations	2021.03.01	A-63/64/32/A-27	Provides opportunities to test innovative products, services and business models based on new technologies in financial services in a practical/ real-time environment with a limited scope and period
4	Procedures for nomination, appointment and dismissal of an independent member of the Board of Directors of the Bank	2021.03.22	2021/A-86	Establishes procedures for nomination, appointment, and dismissal of an independent member of the Board of Directors of the Bank
5	Temporary procedure for developing, implementing, reporting, and reviewing the structure of shareholders and the plan to change the amount of share capital to restructure the bank into a joint stock company	2021.03.26	A-90/85	Sets the temporary procedure to restructure the bank into an open joint stock company, changing the structure and size of the bank's share capital in accordance with this law, and developing, implementing, and reporting on the plan
6	Regulation for issuing statistical information by the Financial Information Unit	2021.03.31	2021/A-93	Sets procedure on dissemination of unified statistical information on measures taken in connection with the implementation of the Law on anti-money laundering and counter-terrorist financing, monitoring, and accountability of law enforcement
7	Temporary procedure for the bank to amend the loan agreement in electronic form	2021.04.12	A-100	Introduces legal norms pertaining receipt of the borrower's proposal to defer payment obligation and extend the term of Government subsidized mortgage program and other loan agreements with preferential interest rate, to enter into an agreement to amend the loan agreement and to notify the borrower
8	Guidelines for identifying influential banks in the banking system	2021.04.19	A-104	Ensures the implementation of Article 3.1.20 of the Banking Law and identifying influential banks in the banking system

9	Regulation of automatic clearing house system	2021.05.25	A-128	Defines the rights and responsibilities of Automatic Clearing House(ACH) participants
10	Bank stabilization fund regulations	2021.06.25	A-155	Sets operation of the bank stabilization fund required to implement the banking resolution measures
11	Approval of the renewed long-term swap agreement procedure	2021.06.30	A-162	Revises principles, rights and obligations of the parties including long-term external swap agreements with the Bank of Mongolia to increase foreign exchange inflows, reduce interest rates, increase foreign currency loans, and establish a system to hedge against foreign exchange risk
12	Approval of the general terms and conditions of service fees	2021.07.21	A-192	Re-establishes the general terms and conditions of the Bank of Mongolia's service fees and commissions
13	Amendments to the temporary procedure for amendments to the loan agreement by the Bank in electronic form	2021.07.08	A-188	Changes date of regulation
14	Regulations for developing, approving, and implementing bank stabilization plans	2021.09.06	A-226	Sets regulations developing a Bank Stabilization Plan to maintain the bank solvency
15	Guidelines for estimating the fair value of a derivative transaction	2021.09.09	A-229	Establishes general methodology for estimating the fair value of long-term and short-term derivative transactions with international financial institutions and identification of data sources to conduct for evaluation
16	Sandbox Board Rules	2021.09.24	A-251/252	Introduces activities of the Board of Directors to organize, coordinate and oversee the implementation of innovative products, services and business models based on modern technologies in financial services in a limited environment and in a timely manner
17	Procedures for approval of changes in the share capital and shareholder structure of a bank in the form of a joint stock company	2021.10.05	A-262/262	Sets regulations on obtaining permission from the Bank of Mongolia to change the share capital of a bank in the form of a joint stock company and change the structure of shareholders
18	Procedures for issuing permits for payment services, operating systems, and monitoring the activities of licensed entities	2021.10.08	A-266	Provides payment services, issue licenses to operate the system, and monitor the activities of licensed entities
19	Regulations for high-value payment systems	2021.10.08	A-267	Sets monitoring the operation of the system
20	Procedures for conducting declarations of influence by officials and inspectors authorized to conduct inspections of the Bank of Mongolia	2021.10.13	A-272	Introduces keeping and receiving the statement of influence of an official and supervisor authorized to conduct supervision of the Bank of Mongolia
21	Guidelines for calculating and announcing the exchange rate of the tugrik against foreign currencies	2021.10.18	A-275	Sets rules processing of information received in accordance with the “Procedure for issuing foreign exchange trading news,” calculation and approval of the exchange rate of the togrog against foreign currencies, and public announcement
22	Procedure for issuing foreign exchange trading news	2021.10.18	A-276	Sets rules related to banks issuing and receiving foreign exchange trading information and define the rights and obligations of participants
23	About renewing and approving the methodology for calculating the debt-to-income ratio	2021.10.20	A-277	Sets the guidelines applied by the bank to issue new consumer loans to individuals and to change the terms of previous loans

24	General conditions of the Bank of Mongolia's license fee	2021.11.09	A-295	Defines the license fee of the Bank of Mongolia to be issued to banks
25	About the approval of standard requirements for bank employees	2021.11.25	A-313	Introduces the basic requirements and working conditions for new and existing employees in the banking sector
26	Guidelines on pricing, making payments and issuing advertisements in foreign currency and units of account	2021.11.30	A-314	Determines rules on the issuance of a permit by the Bank of Mongolia specified in Article 4.1 of the Law on Payments in National Currencies
27	Logo design of the National Electronic Transaction Center	2021.12.06	A-322	Approves of National Payment T-Card Design, Logo, and Hologram and "National Electronic Transaction Center Logo Design"

4.10 ECONOMIC RESEARCH AND TRAINING INSTITUTE

Research

Within its mandate to support Mongolia's development, economic and financial policy decision making, ERTI published the following working papers in 2021:

- Policy Recommendations Based on the Analysis of Money Supply and Demand
- Explaining Inflation in Mongolian Economy: Schools of Thought
- Assessing Living Standards of Herder Households Based on Asset Valuations
- Matrices of Intersectoral Capital Flows and Its Analysis
- Estimating Key Indicators of the Labour Market in Mongolia
- Impact of COVID-19 Pandemic on Services Sector
- Anchoring of Inflation Expectations
- Credit Concentration in the Mongolian Economy

Training

Training needs assessment has been carried out among all departments and branches of the Bank of Mongolia. Some of the training activities were moved online due to the COVID-19 pandemic.

In 2021, ERTI organized the following training events among financial sector specialists and employees of the Bank of Mongolia:

- Leadership Training Workshop for Senior Officials
- "Seminar Series for Bankers" to inform commercial bank employees on topics such as Bank of Mongolia policies and regulations, anti-money laundering and combating the financing of terrorism, risk management, financial reporting standards, and banking supervision. A total of 4,556 employees from 11 commercial banks participated in the training.
- Training for Service Employees

Cooperation

As part of its mission to work closely with government agencies and ministries, ERTI initiated a bilateral assistance and capacity building program in cooperation with the Embassy of Mongolia in Geneva and the State Secretariat for Economic Affairs (SECO). The program provides technical assistance on monetary policy implementation, macroeconomic statistics, financial stability, and banking supervision.

AUDITED FINANCIAL STATEMENT

5

BANK OF MONGOLIA

INTERNATIONAL FINANCIAL REPORTING STANDARDS FINANCIAL STATEMENTS AND INDEPENDENT AUDITOR'S REPORT

31 DECEMBER 2021

BANK OF MONGOLIA

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BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

BOARD OF DIRECTORS' RESPONSIBILITY STATEMENT

The Bank's Board of Directors is responsible for the preparation of the financial statements.

The financial statements of the Bank of Mongolia ("the Bank") have been prepared to comply with International Financial Reporting Standards. The Board of Directors is responsible for ensuring that these financial statements present fairly the financial position of the Bank as at 31 December 2021 and of its financial performance and its cash flows for the year then ended.

The Board of Directors has responsibility for ensuring that the Bank keeps proper accounting records which disclose with reasonable accuracy the financial position of the Bank and which enable them to ensure that the financial statements comply with the accounting policies set out in Note 3 thereto.

The Board of Directors also has a general responsibility for taking actions, which are reasonably open to the Board to safeguard the assets of the Bank and to prevent and detect fraud and other irregularities.

The Board of Directors considers that in preparing the financial statements on pages on 1 to 104 the appropriate policies have been used, consistently applied, and supported by reasonable and prudent judgements and estimates, and that all applicable accounting standards have been followed.

Signed on behalf of the Board of Directors:

Lkhagvasuren B.
Governor, Bank of Mongolia

BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

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Signed on behalf of the Board of Directors:

Lkhagvasuren B.

Governor, Bank of Mongolia

pwc

Independent Auditor's Report

To the Board of Directors of Bank of Mongolia

Our qualified opinion

In our opinion, except for the possible effects of the matter described in the Basis for qualified opinion section of our report, the financial statements present fairly, in all material respects, the financial position of Bank of Mongolia (the "Bank") as at 31 December 2021, and the Bank's financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

What we have audited

The Bank's financial statements comprise:

- the statement of financial position as at 31 December 2021;
- the statement of profit or loss and other comprehensive income for the year then ended;
- the statement of changes in equity for the year then ended;
- the statement of cash flows for the year then ended; and
- the notes to the financial statements, which include significant accounting policies and other explanatory information.

Basis for qualified opinion

As disclosed in Notes 4 and 14 to the financial statements, the Treasury Fund is comprised of heritage assets including historical, cultural, and inherited valuables and coins issued in 1925 and is measured at revalued amount under IAS 16. The Treasury Fund included Mongolian silver and copper coins with a carrying amount of MNT 908,476 million as at 31 December 2021 (2020: MNT 908,476 million), that were originally issued in 1925 by the central bank of which the Bank of Mongolia is a successor (the "Coins"). The objective of the revaluation of the Coins was to reflect the historical collector value that significantly exceeds their silver and copper metal content value.

The coins and banknotes issued by the Bank are recorded as a liability at their nominal value and the coins and banknotes are not recognised as an asset when they are withdrawn from the circulation according to the Bank's accounting policy that is disclosed in Note 3 of the financial statements. As disclosed in Notes 4 and 14 to the financial statements, the Bank is of a view that the Coins were donated to the Treasury Fund by the Government, therefore, they could be recognised as an asset even though the Bank is a legal successor of the central bank which issued the Coins.

However, management was not able to provide us legal evidence that the Coins were in possession of the third party and further transferred to the Treasury Fund by the third party as an asset transfer according to IFRS 3 after 1938 when the Coins were withdrawn from the circulation, which would enable the Bank to recognise the Coins as an asset on transition to IFRS. As a result, we were unable to satisfy ourselves that the Coins were correctly recognised in the statement of financial position in accordance with IFRS, and therefore, we were unable to conclude whether the revaluation surplus in the amount of MNT 906,788 million arising on their revaluation to fair value should have been recognised as the revaluation reserve within the Bank's equity as at 31 December 2021 and 31 December 2020.

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Basis for qualified opinion (continued)

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

Independence

We are independent of the Bank in accordance with the International Code of Ethics for Professional Accountants (including International Independence Standards) issued by the International Ethics Standards Board for Accountants (IESBA Code). We have fulfilled our other ethical responsibilities in accordance with the IESBA Code.

Other information

Management is responsible for the other information. The other information obtained at the date of this auditor's report comprises Bank's 2021 Annual Report (but does not include the financial statements and our auditor's report thereon).

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information, we conclude that there is a material misstatement of this other information, we are required to report that fact. As described in the Basis for qualified opinion section above, we were unable to obtain sufficient appropriate evidence on valuation and recognition of the Coins at 31 December 2021. Accordingly, we are unable to conclude whether or not the other information is materially misstated with respect to this matter.

Responsibilities of management and those charged with governance for the financial statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS, and for such internal control as management determines is necessary to enable the preparation of separate financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

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Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Signed by:

Bayarmaa Davaa
Executive Director
PricewaterhouseCoopers Audit LLC

Approved by:

Shaukat Tapia
Partner
PricewaterhouseCoopers Audit LLC

20 June 2022
Ulaanbaatar, Mongolia

BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

In millions of Mongolian Togrogs	Note	31 December 2021	31 December 2020
ASSETS			
Cash on hand	7	177,591	233,373
Due from foreign financial institutions	8	4,473,789	4,517,392
Loans to local banks	9	1,487,308	461,314
Investments in debt securities	10	6,393,822	5,275,129
Investments in equity securities	11	6,533	6,595
Reverse repurchases agreements	12	4,522,220	4,816,068
Gold bullion and precious metals	13	1,685,633	1,785,857
Treasury Fund	14	1,115,085	1,071,665
Derivative financial instruments	15	77,103	156,419
Government securities	16	231,778	227,407
Other assets	17	319,721	423,673
Premises, equipment, and intangible assets	18	116,024	115,201
Assets held for sale		6,097	6,280
TOTAL ASSETS		**20,612,704**	**19,096,373**
LIABILITIES			
Cash in circulation	19	1,105,589	991,470
Central bank bills	20	8,622,184	7,952,438
Liabilities due to government organizations	21	1,734,116	2,132,025
Deposits from local banks	22	4,471,877	3,871,397
Derivative financial instruments	15	469,758	303,501
Liabilities due to foreign parties	23	6,914,005	5,789,508
Other liabilities	24	667,231	365,317
TOTAL LIABILITIES		**23,984,760**	**21,405,656**
EQUITY			
Charter capital	25	60,000	60,000
Accumulated deficit	25	(5,359,185)	(4,327,545)
Other reserves	25	1,927,129	1,958,262
TOTAL EQUITY		**(3,372,056)**	**(2,309,283)**
TOTAL LIABILITIES AND EQUITY		**20,612,704**	**19,096,373**

Approved for issue and signed on behalf of the Board of Directors on 20 June 2022.

Lkhagvasuren B.
Governor, Bank of Mongolia

Garid Ts.
Director of Financial Reporting and
Accounting Department

The notes set out on pages 8 to 104 form an integral part of these financial statements.

BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

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TOTAL LIABILITIES AND EQUITY		**20,612,704**	**19,096,373**

Approved for issue and signed on behalf of the Board of Directors on 20 June 2022.

Lkhagvasuren B.
Governor, Bank of Mongolia

Garid Ts.
Director of Financial Reporting and Accounting Department

BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

In millions of Mongolian Togrogs	Note	2021	2020
Interest income calculated using the effective interest method	26	286,227	234,362
Other similar income	26	22,165	42,810
Interest expense	26	(886,262)	(816,411)
Net interest expense		**(577,870)**	**(539,239)**
Credit loss allowance		(95,118)	(81,355)
Net interest expense after credit loss allowance		**(672,988)**	**(620,594)**
(Losses)/gains from trading of gold bullion and precious metals	27	(68,539)	728,315
Gold bullion and precious metals translation (losses)/gains		(12,432)	151,293
Losses less gains from derivative financial instruments		(219,426)	(242,925)
Losses less gains from trading in foreign currencies		(4,017)	(1,356)
Foreign exchange translation losses less gains		(88,878)	(457,735)
(Losses)/gains from disposal in debt securities at fair value through other comprehensive income		(1,335)	3,262
Losses from disposal in equity securities at fair value through other comprehensive income		-	(84)
Gains/(losses) from trading of financial investments in debt securities		554	(6)
Gains /(losses) from financial assets at fair value through profit or loss		59,638	(27,707)
Other operating income	28	29,368	29,623
Administrative and other operating expenses	29	(66,017)	(65,464)
LOSS FOR THE YEAR		**(1,044,072)**	**(503,378)**
Other comprehensive (loss) / income:			
Items that may be reclassified subsequently to profit or loss:			
Debt securities at fair value through other comprehensive income:			
- Losses less gains arising during the year	25	(20,036)	95,661
- Gains less losses reclassified to profit or loss upon disposal	25	1,335	(3,262)
Other comprehensive (loss) / income for the year		**(18,701)**	**92,399**
TOTAL COMPREHENSIVE LOSS FOR THE YEAR		**(1,062,773)**	**(410,979)**

BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

In millions of Mongolian Togrogs	Note	Charter capital	Other reserves	Accumulated deficit	Total equity
Balance on 1 January 2020	25	**60,000**	**1,739,806**	**(3,698,110)**	**(1,898,304)**
Loss for the year		-	-	(503,378)	**(503,378)**
Other comprehensive income		-	92,399	-	**92,399**
Total comprehensive loss for 2020		-	92,399	(503,378)	**(410,979)**
Transfer from other reserves to accumulated deficit	25	-	126,057	(126,057)	-
Balance at 31 December 2020		**60,000**	**1,958,262**	**(4,327,545)**	**(2,309,283)**
Loss for the year		-	-	(1,044,072)	**(1,044,072)**
Other comprehensive loss		-	(18,701)	-	**(18,701)**
Total comprehensive loss for 2021		-	(18,701)	(1,044,072)	**(1,062,773)**
Transfer from other reserves to accumulated deficit	25	-	(12,432)	12,432	-
Balance at 31 December 2021		**60,000**	**1,927,129**	**(5,359,185)**	**(3,372,056)**

Transfers from accumulated deficit to other reserves in 2021 and 2020 relate to unrealized gains less losses arising from revaluation of gold bullion and translation gains less losses in foreign currencies (Note 25).

BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

In millions of Mongolian Togrogs	Notes	2021	2020
Cash flows from operating activities			
Loss for the year		**(1,044,072)**	**(503,378)**
Adjustments to:			
Credit loss allowance		95,118	81,355
Losses/ (gains) from disposal in debt securities at fair value through other comprehensive income		1,335	(3,262)
(Gains)/ losses from trading of financial investments in debt securities		(554)	6
Losses/ (gains) from revaluation of gold bullion and precious metals		12,432	(151,293)
Losses less gains from derivative financial instruments		219,426	242,925
Foreign exchange translation losses less gains		94,437	584,891
Depreciation and amortization of premises, equipment, and intangible assets	29	7,568	6,090
Premises and equipment written off		3	5
Fair value (gains)/losses on promissory notes		(59,638)	27,707
Losses from disposal in equity securities at fair value through other comprehensive income		-	84
Non-monetary donation		-	(111)
Interest income calculated using the effective interest method	26	(286,228)	(234,362)
Other similar income	26	(22,165)	(42,810)
Interest expense	26	886,262	816,411
Cash flows generated from operating activities before changes in operating assets and liabilities		**(96,076)**	**824,258**
Changes in operating assets and liabilities:			
Net decrease in gold bullion and precious metals		87,792	1,474,120
Net decrease/(increase) in reverse repurchase agreements		337,273	(1,546,820)
Net (increase) in loans to local banks		(1,038,737)	(25,233)
Net decrease/(increase) in due from foreign financial institution		2,070	(1,698)
Net decrease in other assets		397,143	442,124
Net increase in central bank bills		676,302	3,316,148
Net (decrease) in liabilities due to government organizations		(370,287)	(166,179)
Net increase/(decrease) in deposits from local banks		620,756	(2,310,184)
Net increase in other liabilities		9,950	(470,042)
Net cash generated from operating activities before interest		**626,187**	**1,536,494**
Interest received		270,056	215,185
Interest paid		(891,510)	(815,171)
Net cash flow generated from operating activities		**4,733**	**936,508**
Cash flows from investing activities			
Acquisition of premises and equipment	18	(14,078)	(44,069)
Proceeds from disposal of premises and equipment		5,867	11,756

BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

Acquisition of treasury fund	14	(43,420)	(2,805)
Proceeds from disposal of equity securities at fair value through other comprehensive income		-	5,055
Acquisition of debt securities at fair value through other comprehensive income		(4,986,979)	(1,882,039)
Acquisition of investment in debt securities carried at amortized cost		(763,232)	(751,163)
Proceeds from redemption of debt securities at fair value through other comprehensive income		4,262,051	1,056,258
Proceeds from redemption of debt securities carried at amortised cost		343,677	243,880
Net cash flows used in investing activities		**(1,196,113)**	**(1,363,127)**

In millions of Mongolian Togrogs	Notes	2021	2020
Cash flows from financing activities			
Net increase of cash in circulation	19	114,119	94,053
Proceeds from liabilities due to foreign parties	23	2,237,184	284,364
Repayment of liabilities due to foreign parties	23	(1,231,344)	(45,766)
Net cash generated from financing activities		**1,119,959**	**332,651**
Effect of exchange rate changes on cash and cash equivalents		**(27,962)**	**171,961**
Net (decrease)/increase in cash and cash equivalents		**(99,383)**	**77,993**
Cash and cash equivalents at the beginning of year	**7**	**4,750,573**	**4,672,580**
Cash and cash equivalents at the end of the year	**7**	**4,651,190**	**4,750,573**

BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

1. INTRODUCTION AND OPERATING ENVIRONMENT

Introduction. The Bank of Mongolia (the "BOM" or the "Bank") is the central bank of Mongolia and operates in accordance with the constitution of Mongolia, the Law on Central Bank (Bank of Mongolia), and other laws of Mongolia. The Bank was established under the resolution of the Government of Mongolia dated 2 June 1924.

All operations of the BOM are conducted in Mongolia. The BOM system includes 17 regional offices throughout Mongolia and its representative office in London, England.

In accordance with the legislation, the primary function of the BOM is ensuring the stability of the national currency of Mongolia and to promote a balanced and sustained development of the national economy, through maintaining stability of finance markets and banking system.

The BOM does not aim to earn profits. The financial results of the BOM's activities, as well as the structure of its assets, liabilities and equity are defined by the functions of the BOM as a special central government authority.

In accordance with the Law on Central Bank (Bank of Mongolia), the main functions of the BOM are as follows:

- issue of national currency of Mongolia and organization of its circulation.
- formulation and implementation of monetary policy by regulating money supply in the economy.
- acting as depository of the Government of Mongolia (the "Government" or the "State").
- exercising banking regulation and supervision.
- organization of interbank payments and settlements.
- holding and management of the State's reserves of foreign currency.
- acting as a lender of the last resort for banks and organizing a system of refinancing.
- representing Mongolia in other central banks, international banks, and other credit institutions where co-operation is maintained between the central banks.
- exercising other functions in financial and credit areas within the competence defined by the Law.

According to the Law, the BOM provides loans to banks to support their liquidity, buys and sells securities in the secondary market, buys and sells foreign currency valuables, precious metals, sells commemorative coins made of precious and non-precious metals in the domestic and foreign markets, performs operations of servicing of the Government debt in respect of placement of Government securities, their redemption and interest payments, maintains accounts of the Government and other government institutions, including accounts of the Ministry of Finance (fiscal agent of the Government of Mongolia), accounts of international organizations and conducts other operations necessary for the performance of its functions.

The charter capital of the BOM is fully owned by the State of Mongolia. In accordance with the Law, the main task of the Board of Directors is to develop principles of monetary policy and exercise control over implementation of the monetary policy. In addition, the Governor of BOM approves annually the BOM budget of income and expenditure for the next year, approves annual financial statements of the BOM, report on fulfilment of the BOM budget of income and expenditure and distribution of profit for the reporting year, as well as performs other functions according to its authority defined by the Mongolian legislation.

Registered address and place of business. The Bank's registered address is Baga Toiruu 3, 15160, Ulaanbaatar 46, Mongolia.

BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

1. INTRODUCTION AND OPERATING ENVIRONMENT (CONTINUED)

Operating environment. Mongolia displays many characteristics of an emerging market including relatively high inflation and interest rates. The export of raw materials from the mining sector is the mainstay of the economy due to its mineral resources, including coal and copper, and its low level of industrialization. After growing close to 6 percent on average in 2017-2019, the Mongolian economy has contracted amid adverse impact of the COVID-19 pandemic by 5.3% in 2020, due to slow inbound foreign investment into the country and pre-existing macroeconomic vulnerabilities. Mongolia’s economy growth was 1.4% in 2021, which was driven by the favourable terms of trade, increase in commodity price and higher export demand. Mongolia’s economy is expected to recover gradually in 2022 as pandemic risks fade and the global recovery strengthens.

The country’s rating stood at B with stable outlook on 3 August 2021 by Standard and Poor’s Rating Services. Moody's rating agency announced Mongolia's credit rating was "B3" with stable outlook, changed from negative, on 16 March 2021.

The Government of Mongolia has made several decisions to support the economy during the pandemic including provision of low interest loans to small and medium sized enterprises and announced 6-months payment holidays for consumer and mortgage borrowings between January to June 2021, then extended it until 31 December 2022.

During the crisis, the Government has commenced a staged process of Banking sector reforms and amended the Banking Law at the parliament meeting on 28 January 2021. Its implementation will result in reducing the bank ownership concentration and ensure balance of ownership-management-control in the banking structure. The top five banks will each have to transform into a public company through an initial public offering on the stock market before 30 June 2022.

Growth prospects in 2022 will largely depend on the course of the COVID-19 pandemic, the pace of economic recovery in the neighbouring People’s Republic of China, the rebounding of commodity exports, the overall investment climate and private sector credit growth. To measurement of expected credit losses (“ECL”) the Bank uses supportable forward-looking information, including forecasts of macroeconomic variables. As with any economic forecast, however, the projections and likelihoods of their occurrence are subject to a high degree of inherent uncertainty and therefore the actual outcomes may be significantly different from those projected. Notes 3 and 32 provides more information of how the Bank incorporated forward-looking information in the ECL models.

2. FINANCIAL REPORTING FRAMEWORK AND BASIS FOR PREPARATION AND PRESENTATION

Basis of preparation. These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") under the historical cost convention, as modified by the initial recognition of financial instruments based on fair value, and by the revaluation of premises and equipment, Treasury Fund, financial instruments categorised at fair value through profit or loss ("FVTPL") and at fair value through other comprehensive income ("FVOCI"). The principal accounting policies applied in the preparation of these financial statements are set out in Notes 3. These policies have been consistently applied to all the periods presented, unless otherwise stated.

Presentation currency. These financial statements are presented in Mongolian Togrogs ("MNT") the currency of the primary economic environment in which the Bank operates and the Bank's functional currency. All values are rounded to the nearest million, unless otherwise stated.

Amendments of the financial statements after issue The Bank's management has the power to amend the financial statements after issue.

3. SIGNIFICANT ACCOUNTING POLICIES

Financial instruments – key measurement terms. *Fair value* is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The best evidence of fair value is price in an active market. An active market is one in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. Fair value of financial instruments traded in an active market is measured as the product of the quoted price for the individual asset or liability and the quantity held by the entity. This is the case even if a market's normal daily trading volume is not sufficient to absorb the quantity held and placing orders to sell the position in a single transaction might affect the quoted price.

A portfolio of financial derivatives or other financial assets and liabilities that are not traded in an active market is measured at the fair value of a group of financial assets and financial liabilities based on the price that would be received to sell a net long position (ie an asset) for a particular risk exposure or paid to transfer a net short position (ie a liability) for a particular risk exposure in an orderly transaction between market participants at the measurement date. This is applicable for assets carried at fair value on a recurring basis if the Bank: (a) manages the group of financial assets and financial liabilities on the basis of the entity's net exposure to a particular market risk (or risks) or to the credit risk of a particular counterparty in accordance with the entity's documented risk management or investment strategy; (b) it provides information on that basis about the group of assets and liabilities to the entity's key management personnel; and (c) the market risks, including duration of the entity's exposure to a particular market risk (or risks) arising from the financial assets and financial liabilities is substantially the same.

Management takes the view that valuation technique reaches accurate presentation of fair value of the derivative financial instruments. Refer to Note 33 for the main inputs used in the valuation technique.

Valuation techniques such as discounted cash flow models or models based on recent arm's length transactions or consideration of financial data of the investees, are used to measure fair value of certain financial instruments for which external market pricing information is not available. Fair value measurements are analysed by level in the fair value hierarchy as follows:

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(i) level one are measurements at quoted prices (unadjusted) in active markets for identical assets or liabilities, (ii) level two measurements are valuations techniques with all material inputs observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices), and (iii) level three measurements are valuations not based on solely observable market data (that is, the measurement requires significant unobservable inputs). Transfers between levels of the fair value hierarchy are deemed to have occurred at the end of the reporting period. Refer to Note 33.

Transaction costs are incremental costs that are directly attributable to the acquisition, issue, or disposal of a financial instrument. An incremental cost is one that would not have been incurred if the transaction had not taken place. Transaction costs include fees and commissions paid to agents (including employees acting as selling agents), advisors, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Transaction costs do not include debt premiums or discounts, financing costs or internal administrative or holding costs.

Amortised cost ("AC") is the amount at which the financial instrument was recognised at initial recognition less any principal repayments, plus accrued interest, and for financial assets less any allowance for expected credit losses. Accrued interest includes amortisation of transaction costs deferred at initial recognition and of any premium or discount to maturity amount using the effective interest method. Accrued interest income and accrued interest expense, including both accrued coupon and amortised discount or premium (including fees deferred at origination, if any), are not presented separately and are included in the carrying values of related items in the statement of financial position.

The effective interest method is a method of allocating interest income or interest expense over the relevant period, to achieve a constant periodic rate of interest (effective interest rate) on the carrying amount. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts (excluding future credit losses) through the expected life of the financial instrument or a shorter period, if appropriate, to the gross carrying amount of the financial instrument.

The effective interest rate discounts cash flows of variable interest instruments to the next interest repricing date, except for the premium or discount, which reflects the credit spread over the floating rate specified in the instrument, or other variables that are not reset to market rates. Such premiums or discounts are amortised over the expected life of the instrument. The present value calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate. For assets that are purchased or originated credit impaired ("POCI") at initial recognition, the effective interest rate is adjusted for credit risk, i.e. it is calculated based on the expected cash flows on initial recognition instead of contractual payments.

Financial instruments – initial recognition. Financial instruments at FVTPL are initially recorded at fair value. All other financial instruments are initially recorded at fair value adjusted for transaction costs. Fair value at initial recognition is best evidenced by the transaction price. A gain or loss on initial recognition is only recorded if there is a difference between fair value and transaction price which can be evidenced by other observable current market transactions in the same instrument or by a valuation technique whose inputs include only data from observable markets. After the initial recognition, an ECL allowance is recognised for financial assets measured at AC and investments in debt instruments measured at FVOCI, resulting in an immediate accounting loss.

BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

All purchases and sales of financial assets that require delivery within the period established by regulation or market convention ("regular way" purchases and sales) are recorded at trade date, which is the date on which the Bank commits to deliver a financial asset. All other purchases are recognised when the entity becomes a party to the contractual provisions of the instrument.

The Bank uses discounted cash flow valuation techniques to determine the fair value of long-term cross currency interest rate swaps that are not traded in an active market. Differences may arise between the fair value at initial recognition, which is the transaction price, and the amount determined at initial recognition using a valuation technique with level 3 inputs. If any differences remain after calibration of model inputs, such differences are initially recognised within assets or liabilities and are subsequently amortised on a straight-line basis over the term of the long-term cross currency interest rate swaps.

Financial assets – classification and subsequent measurement – measurement categories. The Bank classifies financial assets in the following measurement categories: FVTPL, FVOCI and AC. The classification and subsequent measurement of debt financial assets depends on: (i) the Bank's business model for managing the related assets portfolio and (ii) the cash flow characteristics of the asset.

Financial assets – classification and subsequent measurement – business model. The business model reflects how the Bank manages the assets in order to generate cash flows – whether the Bank's objective is: (i) solely to collect the contractual cash flows from the assets ("hold to collect contractual cash flows",) or (ii) to collect both the contractual cash flows and the cash flows arising from the sale of assets ("hold to collect contractual cash flows and sell") or, if neither of (i) and (ii) is applicable, the financial assets are classified as part of "other" business model and measured at FVTPL.

Business model is determined for a group of assets (on a portfolio level) based on all relevant evidence about the activities that the Bank undertakes to achieve the objective set out for the portfolio available at the date of the assessment. Factors considered by the Bank in determining the business model include the purpose and composition of a portfolio, past experience on how the cash flows for the respective assets were collected, how risks are assessed and managed, how the assets' performance is assessed and how managers are compensated. Refer to Note 4 for critical judgements applied by the Bank in determining the business models for its financial assets.

Financial assets – classification and subsequent measurement – cash flow characteristics. Where the business model is to hold assets to collect contractual cash flows or to hold contractual cash flows and sell, the Bank assesses whether the cash flows represent solely payments of principal and interest ("SPPI"). Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are consistent with the SPPI feature. In making this assessment, the Bank considers whether the contractual cash flows are consistent with a basic lending arrangement, i.e. interest includes only consideration for credit risk, time value of money, and other basic lending risks.

Where the contractual terms introduce exposure to risk or volatility that is inconsistent with a basic lending arrangement, the financial asset is classified and measured at FVTPL. The SPPI assessment is performed on initial recognition of an asset and it is not subsequently reassessed. Refer to Note 4 for critical judgements applied by the Bank in performing the SPPI test for its financial assets.

Financial assets – reclassification. Financial instruments are reclassified only when the business model for managing the portfolio as a whole changes. The reclassification has a prospective effect and takes place from the beginning of the first reporting period that follows after the change in the business model.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The Bank did not change its business model during the current and comparative period and did not make any reclassifications.

Financial assets impairment – credit loss allowance for ECL. The Bank assesses, on a forward-looking basis, the ECL for debt instruments measured at AC and FVOCI and for the exposures arising from loan commitments and financial guarantee contracts. The Bank measures ECL and recognises credit loss allowance at each reporting date. The measurement of ECL reflects: (i) an unbiased and probability weighted amount that is determined by evaluating a range of possible outcomes, (ii) time value of money and (iii) all reasonable and supportable information that is available without undue cost and effort at the end of each reporting period about past events, current conditions, and forecasts of future conditions.

Debt instruments measured at AC are presented in the statement of financial position net of the allowance for ECL. For loan commitments and financial guarantees, a separate provision for ECL is recognised as a liability in the statement of financial position. For debt instruments at FVOCI, changes in amortised cost, net of allowance for ECL, are recognised in profit or loss and other changes in carrying value are recognised in OCI as gains less losses on debt instruments at FVOCI.

The Bank applies a three-stage model for impairment, based on changes in credit quality since initial recognition. A financial instrument that is not credit-impaired on initial recognition is classified in Stage 1. Financial assets in Stage 1 have their ECL measured at an amount equal to the portion of lifetime ECL that results from default events possible within the next 12 months or until contractual maturity, if shorter ("12 Months ECL"). If the Bank identifies a significant increase in credit risk ("SICR") since initial recognition, the asset is transferred to Stage 2 and its ECL is measured based on ECL on a lifetime basis, that is, up until contractual maturity but considering expected prepayments, if any ("Lifetime ECL"). If the Bank determines that a financial asset is credit-impaired, the asset is transferred to Stage 3 and its ECL is measured as a Lifetime ECL. The Bank's definition of credit impaired assets and definition of default is explained in Note 32. For financial assets that are purchased or originated credit-impaired ("POCI Assets"), the ECL is always measured as a Lifetime ECL. Note 32 provides information about inputs, assumptions and estimation techniques used in measuring ECL, including an explanation of how the Bank incorporates forward-looking information in the ECL models.

Financial assets – derecognition. The Bank derecognises financial assets when (a) the assets are redeemed or the rights to cash flows from the assets otherwise expired or (b) the Bank has transferred the rights to the cash flows from the financial assets or entered a qualifying pass-through arrangement while (i) also transferring substantially all risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all risks and rewards of ownership, but not retaining control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose restrictions on the sale.

Financial assets – modification. The Bank sometimes renegotiates or otherwise modifies the contractual terms of the financial assets. The Bank assesses whether the modification of contractual cash flows is substantial considering, among other, the following factors: any new contractual terms that substantially affect the risk profile of the asset (e.g. profit share or equity-based return), significant change in interest rate, change in the currency denomination, new collateral or credit enhancement that significantly affects the credit risk associated with the asset or a significant extension of a loan when the borrower is not in financial difficulties.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

If the modified terms are substantially different, the rights to cash flows from the original asset expire and the Bank derecognises the original financial asset and recognises a new asset at its fair value. The date of renegotiation is considered to be the date of initial recognition for subsequent impairment calculation purposes, including determining whether a SICR has occurred. The Bank also assesses whether the new loan or debt instrument meets the SPPI criterion. Any difference between the carrying amount of the original asset derecognised and fair value of the new substantially modified asset is recognised in profit or loss, unless the substance of the difference is attributed to a capital transaction with owners.

In a situation where the renegotiation was driven by financial difficulties of the counterparty and inability to make the originally agreed payments, the Bank compares the original and revised expected cash flows to assets whether the risks and rewards of the asset are substantially different as a result of the contractual modification. If the risks and rewards do not change, the modified asset is not substantially different from the original asset and the modification does not result in derecognition. The Bank recalculates the gross carrying amount by discounting the modified contractual cash flows by the original effective interest rate (or credit-adjusted effective interest rate for POCI financial assets) and recognises a modification gain or loss in profit or loss.

Financial liabilities – measurement categories. Financial liabilities are classified as subsequently measured at AC, except for (i) financial liabilities at FVTPL: this classification is applied to derivatives, financial liabilities held for trading (e.g. short positions in securities), contingent consideration recognised by an acquirer in a business combination and other financial liabilities designated as such at initial recognition and (ii) financial guarantee contracts and loan commitments.

Financial liabilities – derecognition. Financial liabilities are derecognised when they are extinguished (i.e. when the obligation specified in the contract is discharged, cancelled, or expires).

An exchange between the Bank and its original lenders of debt instruments with substantially different terms, as well as substantial modifications of the terms and conditions of existing financial liabilities, are accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. The terms are substantially different if the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is at least 10% different from the discounted present value of the remaining cash flows of the original financial liability. If an exchange of debt instruments or modification of terms is accounted for as an extinguishment, any costs or fees incurred are recognised as part of the gain or loss on the extinguishment. If the exchange or modification is not accounted for as an extinguishment, any costs or fees incurred adjust the carrying amount of the liability and are amortised over the remaining term of the modified liability.

Modifications of liabilities that do not result in extinguishment are accounted for as a change in estimate using a cumulative catch-up method, with any gain or loss recognised in profit or loss, unless the economic substance of the difference in carrying values is attributed to a capital transaction with owners.

Cash and cash equivalents. Cash and cash equivalents are items which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Cash and cash equivalents include financial assets, which are on demand or with original maturities of less than three months and which are available for use at short notice, refer to Note 7. Financial assets that cannot be freely converted into cash due to insufficient liquidity or due to restrictions on their use are excluded from cash and cash equivalents. Cash and cash equivalents are carried at amortized cost because: (i) they are held for collection of contractual cash flows and those cash flows represent SPPI using Effective Interest method, and (ii) they are not designated at FVTPL.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Due from foreign financial institutions. Amounts due from other banks are recorded when the BoM advances money to counterparty banks. Amounts due from other banks are carried at AC when: (i) they are held for the purposes of collecting contractual cash flows and those cash flows represent SPPI, and (ii) they are not designated at FVTPL.

Investments in debt securities. Based on the business model and the cash flow characteristics, the Bank classifies investments in debt securities as carried at AC and FVOCI. Debt securities are carried at AC if they are held for collection of contractual cash flows and where those cash flows represent SPPI, and if they are not voluntarily designated at FVTPL in order to significantly reduce an accounting mismatch.

Debt securities including government securities are carried at FVOCI if they are held for collection of contractual cash flows and for selling, where those cash flows represent SPPI, and if they are not designated at FVTPL. Interest income from these assets is calculated using the effective interest method and recognised in profit or loss. An impairment allowance estimated using the expected credit loss model is recognised in profit or loss for the year. All other changes in the carrying value are recognised in OCI. When the debt security is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from OCI to profit or loss.

Investments in equity securities. Financial assets that meet the definition of equity from the issuer's perspective, i.e. instruments that do not contain a contractual obligation to pay cash and that evidence a residual interest in the issuer's net assets, are considered as investments in equity securities by the Bank. Investments in equity securities are measured at FVOCI as these investments are held for strategic purposes other than solely to generate investment returns. Fair value gains and losses are recognised in OCI and are not subsequently reclassified to profit or loss, including on disposal. Impairment losses and their reversals, if any, are not measured separately from other changes in fair value. Dividends continue to be recognised in profit or loss when the Bank's right to receive payments is established except when they represent a recovery of an investment rather than a return on such investment.

Loans to local banks. Loans to local banks are recorded when the BOM advances money to originate an unquoted non-derivative receivable from a counterparty bank or other borrower due on fixed or determinable dates and has no intention of trading the receivable.

These items are classified as AC based on the business model and the cash flow characteristics as the loans are held for collection of contractual cash flows and those cash flows represent SPPI and loans that are not voluntarily designated at FVTPL. Impairment allowances are determined based on the forward-looking ECL models. Note 32 provides information about inputs, assumptions and estimation techniques used in measuring ECL model.

Loans to local banks meet definition of principal market as defined by IFRS 13 requirements when the substance of related transactions relates to the Bank's function of the regulator and of protecting national currency and economy (e.g. performing monetary policy operations, stabilizing inflation, and stimulating economic growth, ensuring stability of Mongolian banking sector etc.) For management's judgements refer to Note 4.

Sale and repurchase agreements and lending of securities. Sale and repurchase agreements ("repo agreements") which effectively provide a lender's return to the counterparty are treated as secured financing transactions. Securities sold under such sale and repurchase agreements are not derecognized. The securities are not reclassified in the statement of financial position unless the transferee has the right by contract or custom to sell or re-pledge the securities, in which case they are reclassified as repurchase receivables.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Securities purchased under agreements to resell ("reverse repo agreements"), which effectively provide a lender's return to the bank are recorded as "Reverse repurchase agreement" in the balance sheet. The difference between the sale and repurchase price is treated as interest income and accrued over the life of repo agreements, using the effective interest method. Based on classification of securities sold under the sale and repurchase agreements, the BOM classifies repurchase agreements into AC.

Gold bullion and precious metals. Gold bullion consists of the stocks of gold bars of international standard held in foreign banks. Gold bullion represents a part of international reserves. Gold bullion is recorded in physical weight in troy ounces and is valued in Togrogs at the official exchange rate of the BOM. The official exchange rate is calculated based on information on gold prices determined (fixed) by participants of the London Bullion Market Association in US dollars translated into MNT at the BOM official MNT/US dollar exchange rate.

Gold bullion and silver bars of international standard held in foreign banks are measured in the statement of financial position at their fair value and revaluation is performed daily. The fair value is determined by taking into consideration the market value of gold and silver. Revaluation gain or loss is recognized in the profit or loss. Annually, unrealized gain or loss on fair value changes is transferred from the accumulated deficit to "Precious Metal Valuation Reserve" within other reserves in equity (refer to Note 25).

Apart from holding gold as gold bullion, the Bank purchases unrefined gold and silver from producers and companies in Mongolia and trades in gold and silver (refer to Note 13). Unrefined gold and silver and other precious metals including commemorative coins are recognized as inventory and carried at lower of cost and net realizable value.

Treasury Fund. A Law on State Treasury Fund was first issued in 1994. According to the law, "Treasure" is defined as precious metal and gemstones in any condition such as raw materials, alloys, chemical compounds, products, historical and cultural monuments. The Treasury fund comprises of main fund and operational fund.

Main fund includes items with extraordinary cultural and historical value listed in the "Historical, cultural and inherited valuables" approved by the Parliament. Operational fund includes refined and non-refined precious metal for the purpose of research, medical treatment, and refinery production, coins made of the precious metal, gemstones, pearl, and other items that are internally approved as treasury assets in accordance with the Bank's "Treasury Fund Operation Procedure" and as approved by the Governor of the Bank.

The Bank uses revaluation model for the Treasury Fund under IAS 16 and revalued the Treasury Fund items as per International Valuation Standards. Treasury Fund is subject to regular revaluations, with sufficient regularity to ensure that the carrying amount does not differ materially from that, which would be determined using fair value at the end of the reporting period.

Increases in the carrying amount arising on revaluation are credited to other comprehensive income and increase the revaluation surplus in equity. Decreases that offset previous increases of the same asset are recognized in other comprehensive income and decrease the previously recognized revaluation surplus in equity; all other decreases are charged to profit or loss for the year. The revaluation reserve included in equity is transferred directly to accumulated deficit or retained earnings when the surplus is realized on the disposal of the asset. Refer to Note 33 for fair value disclosure.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Foreign currency translation. The functional currency of the Bank is the national currency of the primary economic environment, in which the Bank operates. The functional and presentation currency of the Bank is the national currency of the Mongolia, Mongolian Tugrik (MNT).

Monetary assets and liabilities are translated into functional currency at the official exchange rate of the Tugrik at the end of the respective reporting period. Foreign exchange gains and losses resulting from the settlement of transactions and from the translation of monetary assets and liabilities into functional currency at year-end official exchange rates of Tugrik, are recognized in profit or loss for the year (as foreign exchange translation gains less losses). Translation at year-end rates does not apply to non-monetary items that are measured at historical cost. Non-monetary items measured at fair value in a foreign currency, including equity investments, are translated using the exchange rates at the date when the fair value was determined.

At 31 December 2021 and 31 December 2020, the principal rates of exchange used for translating foreign currency balances were:

	31 December 2021 (MNT)	31 December 2020 (MNT)
USD	2,848.80	2,849.51
SDR	3,987.16	4,104.06
EUR	3,222.99	3,495.78
CNY	447.15	436.13
JPY	24.74	27.58

Derivative financial instruments. Derivative financial instruments include cross currency interest rate swaps entered with local banks. Derivative financial instruments represent financial instruments at fair value through profit or loss and are carried at their fair value. All derivative instruments are carried as assets when fair value is positive and as liabilities when fair value is negative. Changes in the fair value of derivative instruments are included in profit or loss for the year. The Bank does not apply hedge accounting.

Other assets. Other assets mainly consist of receivables and prepayments. Receivables are accounted for on an accruals basis and are carried at amortized cost except for receivables from promissory notes. Receivables are recorded when due under the agreement. Prepayments are recorded on the payment date and are charged to the statement of profit or loss when the services are provided. Impairment allowances for receivables are determined based on the forward-looking ECL models. Note 32 provides information about inputs, assumptions and estimation techniques used in measuring ECL model.

Receivables from some promissory notes are carried at FVTPL. Subsequent measurement at fair value applies discounted cash flow approach at market rate of each reporting period. The market rate for promissory notes was considered to be the Bank’s policy rate plus counterparty credit risk. Refer to Note 32.

Receivables from remaining promissory note is carried at AC and subject to impairment assessment which are determined based on the forward-looking ECL models. Refer to Note 32.

Premises and equipment. Premises are stated at revalued amounts, as described below, less accumulated depreciation and provision for impairment, where required.

Premises owned by the Bank are initially measured at cost. Premises are subject to regular revaluations, with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Increases in the carrying amount arising on revaluation are credited to other comprehensive income and increase the revaluation surplus in equity. Decreases that offset previous increases of the same asset are recognized in other comprehensive income and decrease the previously recognized revaluation surplus in equity; all other decreases are charged to profit or loss for the year. The revaluation reserve for premises included in equity is transferred directly to accumulated deficit or retained earnings when the surplus is realized. Management believes that carrying amounts of premises as at 31 December 2021 and 31 December 2020 are not materially different from their fair values.

Equipment owned by the Bank is stated at cost less depreciation and provision for impairment, where required. Costs of minor repairs and maintenance are expensed when incurred. Costs of replacing major parts or components of premises and equipment items are capitalized and the replaced part is retired.

At the end of each reporting period management assesses whether there is any indication of impairment of premises and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset's fair value less costs to sell and its value in use. The carrying amount is reduced to the recoverable amount and the impairment loss is recognized in profit or loss for the year (to the extent it exceeds the previous revaluation surplus in equity, in case of premises). An impairment loss recognized for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's value in use or fair value less costs to sell.

Gains and losses on disposals determined by comparing proceeds with carrying amount are recognized in profit or loss for the year (within other operating income or expenses).

Depreciation. Construction in progress is not depreciated. Depreciation on other items of premises and equipment is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives:

	Useful lives in years
Building/Premises	6 – 60 years
Office and computer equipment	3 – 20 years

The residual value of an asset is the estimated amount that the Bank would currently obtain from disposal of the asset less the estimated costs of disposal if the asset were already of the age and in the condition expected at the end of its useful life. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

Intangible assets. The Bank's intangible assets have definite useful life and primarily include capitalized computer software licenses. Acquired computer software licenses are capitalized on the basis of the costs incurred to acquire and bring to use the specific software. Amortization is calculated using the straight-line method to write down the cost of intangible assets to their residual values over their estimated useful lives of 4 years.

Non-current assets classified as held for sale. Non-current assets and disposal groups, which may include both non-current and current assets, are classified in the statement of financial position as 'non-current assets held for sale' if their carrying amount will be recovered principally through a sale transaction, including loss of control of a subsidiary holding the assets, within twelve months after the end of the reporting period. Assets are reclassified when all of the following conditions are met: (a) the assets are available for immediate sale in their present condition; (b) the Bank's management approved and initiated an active programme to locate a buyer; (c) the assets are actively marketed for sale at a reasonable price; (d) the sale is expected within one year and (e) it is unlikely that significant changes to the plan to sell will be made or that the plan will be withdrawn.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Non-current assets or disposal groups classified as held for sale in the current period's statement of financial position are not reclassified or re-presented in the comparative statement of financial position to reflect the classification at the end of the current period. Held for sale premises and equipment are not depreciated. Reclassified non-current financial instruments are not subject to write down to the lower of their carrying amount and fair value less costs to sell.

Cash in circulation. The amount of banknotes and coins in circulation represents the nominal value of banknotes and coins that can be used as payment instruments and were issued into circulation by the BOM after the introduction of Togrogs into circulation in September 1993. The banknotes and coins in circulation are recorded as a liability at their nominal value when cash is issued by the BOM to banks and clients of the BOM. Cash in national currency held in the BOM's vaults and cash offices is not included in banknotes and coins in circulation.

Central bank bills. Central bank bills issued by the BOM are initially recorded at fair value and subsequently are measured at amortized cost using the effective interest method. Amortized cost is calculated by considering any discount or premium on the issue and costs that are an integral part of the effective interest rate.

Liabilities due to government organizations. Accounts of the Government and other government institutions are non-derivative liabilities to the Government or other customers and are carried at amortized cost using effective interest method. Liabilities due to government organizations mostly relate to long-term loans obtained from the Ministry of Finance, which relate to programmes financed by the International Monetary Fund (IMF), World Bank (WB) and Asian Development Bank (ADB). Refer to Note 21.

Liabilities due to foreign parties. Liabilities due to foreign parties are initially recorded at fair value and subsequently are measured at amortized cost using effective interest method. Liabilities due to foreign parties mostly relate to loan obtained from People's Bank of China (central bank of China, "PBC"), MUFG Bank Ltd, Bank of International Settlements and Cargill Financial Services International, Inc. Refer to Note 23.

Deposits from local banks. Accounts of banks are recorded when money is advanced to the BOM by counterparty banks. The non-derivative liability is carried at amortized cost. Refer to Note 22.

Provisions for liabilities and charges. Provisions for liabilities and charges are non-financial liabilities of uncertain timing or amount. They are accrued when the Bank has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

Operations with International Monetary Fund. As a result of the Bank's role in relationship between Mongolia and International Monetary Fund (IMF), the Bank enters into operations with IMF. IMF related balances, which meet definition of assets and liabilities under IFRS Framework, are recognized in the financial statements of the BOM. The Bank does not recognize in its financial statements IMF related balances, which do not meet definition of assets and liabilities under IFRS Framework.

IMF related assets and liabilities of the Bank. The IMF asset balances recognized in these financial statements include holdings of Special Drawing Rights (SDR), refer to Note 8. Liabilities due to the IMF include liabilities for allocation of SDRs. Refer to Note 23.

Assets and liabilities denominated in SDRs are translated into Togrogs at the BOM official exchange rate of Togrogs to SDR at the reporting date. The official exchange rate of Togrogs to SDR is calculated based on information on the exchange rate of SDR to USD set by the IMF and the BOM official MNT/USD exchange rate at the reporting date.

BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

IMF related balances of Government of Mongolia. Certain IMF related balances do not meet definition of assets and liabilities under IFRS Framework, given that the Bank has no contractual rights and obligations with regard to purchases of related IMF funds. These include IMF quota contribution and Extended Fund Facility (EFF) arrangement loan from IMF. The BOM acts as a depository of the Government of Mongolia in the relationship of Mongolia with the International Monetary Fund (IMF). The Ministry of Finance acts as the fiscal agent of Mongolia. Thus, claims of Mongolia on and liabilities to the IMF in respect of funds received from IMF (such as IMF quota subscription) are not recognized in the financial statements of the BOM, as they represent assets and liabilities of the Ministry of Finance.

IMF quota subscription. The quota balance is a special type asset, which represents Mongolia's subscription as a member of the IMF. Quotas vary based on the economic size of each country and are determined by the Board of Governors of the IMF. The quota determines a member's voting power in the Fund, the limits of access to the financial resources of the Fund and a participant's share in the allocation of SDRs, the Fund's unit of account. A major part of Mongolia's quota was paid in the form of non-interest-bearing promissory notes issued to the IMF by the Ministry of Finance, the remainder being credited to the IMF accounts No 1 and No 2. As at 31 December 2021, Mongolia's quota in the IMF amounted to SDR 72.3 million (2020: SDR 72.3 million). Given that quota subscription was paid through issue of promissory notes by the Ministry of Finance of Mongolia, these amounts represent assets of the Ministry of Finance of Mongolia.

IMF securities issued. These securities represent IMF's holdings of Mongolia's currency and include promissory notes issued in settlement of quota as described above and holdings arising from use of IMF credit in case of promissory notes issued in settlement of purchase of IMF funds under Extended Fund Facility arrangement.

IMF accounts No. 1 and No. 2. IMF account No. 1 is used for IMF transactions including quota subscription payments, purchase and repurchase of funds. Account No. 2 is used for settlements with the IMF in Mongolian currency. Accounts No. 1 and No. 2 are MNT 752 million as at 31 December 2021 (2020: MNT 700.6 million).

Extended Fund Facility (EFF) arrangement. The Executive Board of the IMF approved a three-year extended arrangement under Extended Fund Facility (EFF) for Mongolia in a total amount of SDR 314.5 million to support the country's economic reform program on 24 May 2017. The EFF arrangement represents loans granted to Mongolia by IMF under the EFF, which bear interest from 1.53% p.a. to 1.59% p.a. The funding was further transferred to relevant accounts opened within the Bank (e.g. accounts of the Ministry of Finance) according to memorandum of understanding between BOM and Ministry of Finance (MOF) dated 25 May 2017. The loans and repayments are denominated in SDR and the repayment is expected to be paid by the Bank on behalf of MOF to IMF within 2026. As at 31 December 2021, liabilities due to MOF under EFF program was SDR 155.2 million, which is equivalent to MNT 618,751 million (2020: SDR 157.5 million, which is equivalent to MNT 645,616 million), disclosed in Note 21.

Charter capital. Charter capital (fund) is classified as equity. Refer to Note 25.

General reserve. In accordance with the Law on Central Bank (Bank of Mongolia), at least 40% of the Bank's net income for the year shall be allocated to the general reserve, while the remaining amount (i.e. maximum 60% of net income) can be transferred to the State Budget account. General reserve includes only such portions of net income accumulated over years over which the Bank has full rights to utilize them. This reserve fund does not include amounts that were distributed to the State budget in the past or which can be distributed in the future, as these portions have been already transferred to the Government in respective years. There were no transfers in 2021 and 2020, as the Bank had an accumulated deficit in these years.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Other reserves. Other reserves consist of unrealized foreign exchange translation gains and losses, unrealized revaluation gains and losses on gold bullion and precious metals (silver), revaluation reserve (related to buildings and Treasury Fund), and reserve for FVOCI. Refer to Note 25. In accordance with its policies, the Bank transfers unrealized revaluation gains and losses on gold bullion and precious metals and foreign exchange translation gains less losses, previously recognized through profit or loss, to other reserves at the end of the year.

Credit related commitments. The Bank enters into credit related commitments, which include letters of credit and the arrangement with the People's Bank of China (central bank of China, "PBC"), which in substance represents a credit facility (line) provided by PBC in Yuan to the BOM and credit facility in MNT by the BOM to PBC (refer to Note 30).

At the end of each reporting period, the commitments are measured at (i) the remaining unamortized balance of the amount at initial recognition plus (ii) the amount of the loss allowance determined based on the expected credit loss model. In cases where the fees are charged periodically in respect of an outstanding undrawn commitment, they are recognized as revenue on a time proportion basis over the respective commitment period.

Income and expense recognition. Interest income and expense are recorded for all debt instruments, other than those at FVTPL, on an accrual basis using the effective interest method. This method defers, as part of interest income or expense, all fees paid or received between the parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts. Interest income on debt instruments at FVTPL (promissory notes) calculated at nominal interest rate is presented within 'Gains less losses from financial assets at FVTPL' line in profit or loss.

For financial assets that are originated or purchased credit-impaired, the effective interest rate is the rate that discounts the expected cash flows (including the initial expected credit losses) to the fair value on initial recognition (normally represented by the purchase price). As a result, the effective interest is credit-adjusted.

Interest income is calculated by applying the effective interest rate to the gross carrying amount of financial assets, except for (i) financial assets that have become credit impaired (Stage 3), for which interest revenue is calculated by applying the effective interest rate to their AC, net of the ECL provision, and (ii) financial assets that are purchased or originated credit impaired, for which the original credit-adjusted effective interest rate is applied to the AC.

If the credit risk on the financial asset classified in Stage 3 subsequently improves so that the asset is no longer credit-impaired and the improvement can be related objectively to an event occurring after the asset had been determined as credit-impaired (i.e. the asset becomes cured), the asset is reclassified from stage 3 and the interest revenue is calculated by applying the EIR to the gross carrying amount. The additional interest income, which was previously not recognised in P&L due to the asset being in stage 3, but it is now expected to be received following the asset's curing, is recognised as a reversal of impairment.

Fee and commission income is recognised at a point in time when the Bank satisfies its performance obligation, usually upon execution of the underlying transaction. The amount of fee or commission received, or receivable represents the transaction price for the services identified as distinct performance obligations. Such income includes fees for processing payment transactions and fees for cash settlements.

Other similar income and expense items are generally recorded on an accrual basis by reference to completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided.

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Expenses for money issuance. The BOM instructs to print its national currency denominated notes to manufacturer and prepayments associated with the banknotes and coins printed are within “Other assets” and charged to the BOM's expenses when produced banknotes and coins are delivered by printing companies to the Central Vault of the BOM.

Staff costs and related contributions. Wages, salaries, and other salary related expenses (including paid annual leave and sick leave, bonuses, and non-monetary benefits) are recognized as an expense in the year, in which the associated services are rendered by the Bank’s employees. Short-term accumulating compensated absences such as paid annual leave are recognized when services are rendered by employees that increase their entitlement to future compensated absences. Short-term non-accumulating compensated absences such as sick leave are recognized when absences occur.

Employee benefits. Based on its internal regulations, the Bank allocates certain funds to the Social development fund, which is used for improving living and working conditions of the Bank’s employees. These funds are used for payment of benefits, reimbursements, work performance remunerations of the Bank’s employees, purchasing apartments to guarantee social welfare of employees and to help employees in need etc.

Management believes that Social Development Fund as at 31 December 2021 and 31 December 2020 is sufficient to cover these liabilities and short-term liabilities for which this fund is created and that amount of recognized liability for retirement benefits is not materially different from the amount of present value of the defined benefit obligation at the reporting date.

Income taxes. In accordance with Corporate Income Tax Law of Mongolia, the BOM is exempted from income tax.

Offsetting. Financial assets and liabilities are offset, and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognised amounts, and there is an intention to either settle on a net basis, or to realise the asset and settle the liability simultaneously. Such a right of set off (a) must not be contingent on a future event and (b) must be legally enforceable in all of the following circumstances: (i) in the normal course of business, (ii) the event of default and (iii) the event of insolvency or bankruptcy.

Presentation of statement of financial position in order of liquidity. The Bank does not have a clearly identifiable operating cycle and therefore does not present current and non-current assets and liabilities separately in the statement of financial position. Instead, assets and liabilities are presented in order of their liquidity. The following table provides information for each line item in the statement of financial position, which combines amounts expected to be recovered or settled before and after twelve months after the reporting period.

BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

	31 December 2021			31 December 2020		
	Amounts expected to be recovered or settled			Amounts expected to be recovered or settled		
In millions of Mongolian Togrogs	Within 12 months after the reporting period	After 12 months after the reporting period	Total	Within 12 months after the reporting period	After 12 months after the reporting period	Total
Cash on hand	177,591	-	**177,591**	233,373	-	**233,373**
Due from foreign financial institutions	4,473,789	-	**4,473,789**	4,517,392	-	**4,517,392**
Investments in debt securities	1,810,041	4,583,781	**6,393,822**	2,155,507	3,119,622	**5,275,129**
Investments in equity securities	-	6,533	**6,533**	-	6,595	**6,595**
Reverse repurchase agreements	3,467,428	1,054,792	**4,522,220**	4,584,830	231,238	**4,816,068**
Gold bullion and precious metals	1,594,676	90,957	**1,685,633**	1,405,887	379,970	**1,785,857**
Treasury fund	1,115,085	-	**1,115,085**	1,071,665	-	**1,071,665**
Derivative financial instruments	59,298	17,805	**77,103**	90,559	65,860	**156,419**
Government securities	672	231,106	**231,778**	-	227,407	**227,407**
Loans to local banks	903,089	584,219	**1,487,308**	52,787	408,527	**461,314**
Other assets	177,959	141,762	**319,721**	191,547	232,126	**423,673**
Premises, equipment, and intangible assets	-	116,024	**116,024**	-	115,201	**115,201**
Assets held for sale	6,097	-	**6,097**	6,280	-	**6,280**
Total assets	**13,785,725**	**6,826,979**	**20,612,704**	**14,309,827**	**4,786,546**	**19,096,373**
Cash in circulation	(1,105,589)	-	**(1,105,589)**	991,470	-	**991,470**
Central bank bills	(8,622,184)	-	**(8,622,184)**	7,952,438	-	**7,952,438**
Liabilities due to government organizations	(1,114,102)	(620,014)	**(1,734,116)**	1,454,101	677,924	**2,132,025**
Deposits from local banks	(4,471,877)	-	**(4,471,877)**	3,871,397	-	**3,871,397**
Derivative financial instruments	(334,171)	(135,587)	**(469,758)**	135,001	168,500	**303,501**
Liabilities due to foreign parties	(6,629,125)	(284,880)	**(6,914,005)**	5,789,508	-	**5,789,508**
Other liabilities	(667,231)	-	**(667,231)**	365,317	-	**365,317**
Total liabilities	**(22,944,279)**	**(1,040,481)**	**(23,984,760)**	**20,559,232**	**846,424**	**21,405,656**

4. CRITICAL ACCOUNTING ESTIMATES, AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The Bank makes estimates and assumptions that affect the amounts recognized in the financial statements and the carrying amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Management also makes certain judgements, apart from those involving estimations, in the process of applying the accounting policies. Judgements that have the most significant effect on the amounts recognized in the financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include:

Going concern. Management prepared these financial statements on a going concern basis. As at 31 December 2021 and 31 December 2020, the Bank has negative equity position and net liabilities. Management believes that there is no risk that the Bank will not be able to continue as a going concern in foreseeable future as the primary function of the BOM is ensuring the stability of the national currency of Mongolia and to promote a balanced and sustained development of the national economy, through maintaining stability of finance markets and banking system. Article 38 of the Law on Central Bank stipulates that if a deficit of the Central Bank arises, the Parliament shall decide whether the Government must issue securities to cover the difference in the amount of the net deficit. Thus, the Government has no obligation to fund a net deficit of the Bank. However, issuance of government bonds for covering a deficit is a possibility, which could be used by the Parliament, if covering a deficit is necessary to enable the Bank to perform its functions and continue its operations.

ECL measurement. Measurement of ECLs is a significant estimate that involves determination of methodology, models, and data inputs. Details of ECL measurement methodology are disclosed in Note 32. The following components have a major impact on credit loss allowance:

- definition of default applied by the Bank;
- criteria for assessing if there has been a significant increase in credit risk;
- development and application of internal credit grading models, which assigns PDs to the individual credit risk grades;
- Exposure at default (EAD);
- Loss given default ("LGD"), including the judgments made in valuation of collaterals;
- selection of forward-looking macroeconomic scenarios and their probability weightings.

The Bank regularly reviews and validates the models and inputs to the models to reduce any differences between expected credit loss estimates and actual credit loss experience. Refer to Note 32 for details.

Significant increase in credit risk ("SICR"). In order to determine whether there has been a significant increase in credit risk, the Bank compares the risk of a default occurring over the life of a financial instrument at the end of the reporting date with the risk of default at the date of initial recognition. The assessment considers relative increase in credit risk rather than achieving a specific level of credit risk at the end of the reporting period. The Bank considers all reasonable and supportable forward-looking information available without undue cost and effort. Refer to Note 32.

Business model assessment. The business model drives classification of financial assets. Management applied judgement in determining the level of aggregation and portfolios of financial instruments when performing the business model assessment.

4. CRITICAL ACCOUNTING ESTIMATES, AND JUDGEMENTS IN APPLYING ACCOUNTING (CONTINUED)

When assessing sales transactions, the Bank considers their historical frequency, timing and value, reasons for the sales and expectations about future sales activity. Sales transactions aimed at minimising potential losses due to credit deterioration are considered consistent with the “hold to collect” business model. Other sales before maturity, not related to credit risk management activities, are also consistent with the “hold to collect” business model, provided that they are infrequent or insignificant in value, both individually and in aggregate. In addition, sales of financial asset expected only in stress case scenario, or in response to an isolated event that is beyond the Bank’s control, is not recurring and could not have been anticipated by the Bank, are regarded as incidental to the business model objective and do not impact the classification of the respective financial assets.

The “hold to collect and sell” business model means that assets are held to collect the cash flows but selling is also integral to achieving the business model’s objective, such as, managing liquidity needs, achieving a particular yield, or matching the duration of the financial assets to the duration of the liabilities that fund those assets.

The residual category includes those portfolios of financial assets, which are managed with the objective of realising cash flows primarily through sale, such as where a pattern of trading exists. Collecting contractual cash flow is often incidental for this business model.

Assessment whether cash flows are solely payments of principal and interest (“SPPI”). Determining whether a financial asset’s cash flows are solely payments of principal and interest required judgement.

The time value of money element may be modified, for example, if a contractual interest rate is periodically reset but the frequency of that reset does not match the tenor of the debt instrument’s underlying base interest rate, for example, a loan pays three months interbank rate, but the rate is reset every month. The effect of the modified time value of money was assessed by comparing relevant instrument’s cash flows against a benchmark debt instrument with SPPI cash flows, in each period and cumulatively over the life of the instrument. The assessment was done for all reasonably possible scenarios, including reasonably possible financial stress situations that can occur in financial markets. In case of a scenario with cash flows that significantly differ from the benchmark, the assessed instrument’s cash flows are not SPPI, and the instrument is then carried at FVTPL. Instruments that failed the SPPI test are measured at FVTPL.

Initial recognition of borrowings from the Ministry of Finance and loans to local banks. The Bank has borrowings due to the Ministry of Finance in the amount of MNT 32,267 million (2020: MNT 27,936 million) disclosed in Note 21, which relate to the borrowings received by the Ministry of Finance on behalf of the Government of Mongolia, under inter-state project financing from the Asian Development Bank (ADB).

These resources are subject to a very low interest ranging from 1% to 2.5% per annum and were conditional on lending to selected sectors of the economy or for other specified purposes at low rates.

Management have considered whether gains should arise on initial recognition of such instruments. In making this judgement management made a conclusion that these borrowings should be considered as instruments of a principal market represented by an inter-state project, financing aimed to serve the public interest that is often provided at just a token or even free of charge. Further, the funding from these institutions was also available at low interest rates to certain Mongolian local banks for selected sectors or specific purposes. As a result, no initial recognition gains should be recognized.

4. CRITICAL ACCOUNTING ESTIMATES, AND JUDGEMENTS IN APPLYING ACCOUNTING (CONTINUED)

As a result of financing, the Bank is able to advance funds to eligible banks at advantageous rates. Management have considered whether losses should arise on initial recognition of such instruments. As the transactions are with unrelated parties, management's judgement is that this lending is at the market rates and no initial recognition losses should arise. In making this judgement management also considered that these instruments represent a principal market.

Fair value of financial derivatives. The Bank regularly enters into derivative contracts with mainly local banks for the purposes of increasing foreign currency flow, diminishing the growth of interest rates and the amount of foreign currency loans, and creating foreign currency exchange risk mitigation framework. These derivatives are measured at fair value through profit or loss.

The Bank entered into a long-term cross currency interest rate SWAP arrangement with the local banks since December 2017. The arrangement is to swap MNT/USD on a regular basis based on an interest rate formula with maturities ranging from 1 year to 8 years.

The forward price used in the fair valuation technique is estimated by the BOM Monetary Policy Department, using the econometric method. There is no readily available market information on pricing of such long-term instruments. Management believes that forward rate estimated using the econometric method gives a more accurate rate than formula-based approach using interest rate parity theory. Information about fair values of instruments valued using assumptions that are not based on observable market data is disclosed in Notes 33.

Management has considered whether gains or losses should arise on initial recognition of such instruments. As the transactions were entered into by willing market participants, management's judgement is that these instruments are at market rates and no initial recognition gains or losses should arise. In making this judgement management also considers that these instruments are a principal market segment.

Initial recognition of loans to local banks. Starting from November 2012 the Bank has issued loans in MNT to local banks for further lending to local companies under Price Stabilization Program (PSP). These loans were issued under terms and conditions defined by Government joint resolutions and the Bank has no discretion in defining the terms of these loans. In addition, decisions on participation of particular companies in the program are also taken by the Government, and the entities selected are entitled to obtain loans, which are refinanced by the BOM, from any local bank. As a result, the Bank is able to advance funds to local banks as determined by the Government of Mongolia, at advantageous rates at 0.89% per annum to 4% per annum. Management has considered whether gains or losses should arise on initial recognition of such instruments. As the transactions are in accordance with the main function of the central bank to formulate and to implement monetary policy by money supply in the economy and to stabilize inflation, management's judgement is that these loans represent the principal market. The loans to local banks under PSP amounted to MNT 852,376 million as at 31 December 2021 (2020: MNT 383,799 million) and are disclosed in Note 9. For related accounting policy, refer to Note 3.

Initial recognition and impairment provision of loans and financial support to Deposit Insurance Corporation (DICOM). In 2013, the Bank issued a loan to DICOM in the amount of MNT 119,900 million with 0.5% interest p.a with maturity of 10 years with the sole purpose of ensuring stability of Mongolian banking. Based on contractual terms, this loan is due for repayment on 30 September 2023 and interest repayments are made on an annual basis. Based on the agreement, the loan is arranged to be repaid from (1) collection of claim rights contract of Savings Bank; (2) proceeds of the privatization of State Bank LLC; (3) dividend income of State Bank; and (4) other income of DICOM.

4. CRITICAL ACCOUNTING ESTIMATES, AND JUDGEMENTS IN APPLYING ACCOUNTING (CONTINUED)

On the same day, the Bank had additionally issued a short-term financial support to DICOM in the amount of MNT 85,000 million in support of the Government's decision to acquire shares in State Bank LLC. As a result, DICOM owns 75% of State Bank LLC. Based on the agreement, the financial support is arranged to be repaid from proceeds of the privatization of State Bank LLC.

As related lending was provided in accordance with the Bank's main function to ensure stability of Mongolian banking sector, act as a lender of the last resort for banks and to organize a system of refinancing, management's judgement is that related lending represents the principal market. The carrying value of loans to DICOM as at 31 December 2021 is MNT 57,576 million (2020: MNT 54,230 million) and is disclosed in Note 17.

Impairment provision for financial support to Deposit Insurance Corporation (DICOM). Although the counterparty of above-explained financial support and loan is DICOM, the repayment of each arrangement are specifically stated in the contracts. Therefore, the impairment provision for these lendings are assessed differently with consideration of the repayment methods contracted in the arrangements.

Initial recognition of other financial instruments below market rate. IFRS 9 requires initial recognition of financial instruments based on their fair values. Judgement is applied in determining if transactions are priced at market or non-market interest rates, where there is no active market for such transactions. The basis for judgement is pricing for similar types of transactions with unrelated parties and effective interest rate analysis. Further, in accordance with its accounting policy (Note 3), management assessed that recognition of loss on initial recognition is necessary in case of the following transactions, as their nature (substance) do not represent functions of the Central Bank:

- On 23 September 2015, the Bank purchased the Development Bank securities in the total nominal amount of MNT 60,000 million with an interest rate of 4% per annum, which is below market rate. The fair value of these securities at initial recognition was MNT 31,397 million. The difference between nominal value of the Development Bank securities and their fair value totalling MNT 28,603 million was recognized as a loss on initial recognition in profit or loss for the year ended 31 December 2015. The carrying value of the securities was MNT 55,650 million as at 31 December 2020, and it had been fully repaid in 2021. For related accounting policy, refer to Note 3 and for more information, refer to Note 10.
- During 2016, the Bank obtained government securities in par value of MNT 453,712 million at coupon rate of 1.0% per annum to 3.0% per annum in order to finance "Sain" program. Management has recognized these financial assets at fair value of MNT 123,668 million with initial loss of MNT 330,044 million. The loss was recognized in profit or loss for the year ended 31 December 2016. Government securities are carried at FVOCI. As at 31 December 2021, carrying value of the securities related to
- "Sain" program is MNT 231,778 million (2020: MNT 227,407 million). For related accounting policy, refer to Note 3 and for more information, refer to Note 16.
- The Bank entered into reverse repurchase arrangement with local banks in 2016. The arrangement bears floating interest rate at policy rate minus 3% per annum until 30 September 2016 and 11 October 2016 when the rate became fixed at 7.5% per annum and management has considered these are below market. The fair value of related lending at initial recognition was MNT 150,000 million and loss on initial recognition is MNT 23,426 million as at 31 December 2016. Carrying value of the agreements was MNT 62,327 as at 31 December 2020, and it had been fully repaid in 2021. For related accounting policy, refer to Note 3 and for more information, refer to Note 12.

4. CRITICAL ACCOUNTING ESTIMATES, AND JUDGEMENTS IN APPLYING ACCOUNTING (CONTINUED)

All above-mentioned losses on initial recognition are recognized as losses on initial recognition of assets at rates below market in profit or loss for the respective reporting periods.

When determining the amounts of loss on initial recognition in relation to abovementioned transactions, management made the following judgements based on available information on comparable transactions:

- the policy rate of the BOM represents reasonable approximation of market interest rate on MNT funding in case of credit (counterparty) risk related to the Government of Mongolia.
- the policy rate of the BOM increased by margin of 2% per annum represents reasonable approximation of market rate on MNT funding in case of credit (counterparty) risk related to corporate entities in relation to promissory notes (Note 17), given the nature and size of their operations, their reputation, likely support by related parties, and collateral.

Fair value of promissory notes. The Bank provided lending to corporate clients through the purchase of their promissory notes for the amount of MNT 350,000 million in 2014 and MNT 465,000 million in 2016 at interest rates at 21% p.a which have had an option to be decreased to 7-8% per annum in case specified performance conditions were met.

Management assessed at the origination of these assets the appropriate effective interest rate for these loans, taking into consideration the contractual terms and conditions, and the likelihood of specific performance conditions to be met based on available information. Management concluded that the borrowers had high probability of meeting specified conditions. Therefore, these reduced interest rates do not represent the market rate for similar financial instruments in Mongolia, management estimated the loss on initial recognition. As a result, fair value of related receivables at initial recognition was MNT 265,426 million and related loss on initial recognition in 2014 was MNT 84,574 million. The fair value of related lending at initial recognition was MNT 371,722 million and MNT 93,278 million was recognized as losses on initial recognition of assets at rates below market in profit or loss for the year ended 31 December 2016. These receivables were reclassified as FVTPL (mandatory) as per SPPI test from the date of initial application of IFRS 9. Therefore, fair value of the related receivables was estimated as at the transition date.

Management estimates fair value of the promissory notes using discounted cashflow model. In the fair value estimation, following judgements have been applied based on available information:

- Probability of the future cashflow: Management has assessed the probability of the future cashflows based on counterparties' historical financial information and believes repayment of the promissory notes are able to be fully collected on time for some of the promissory notes.
- Discount rate: The policy rate of the Bank increased by the counterparty's credit risk. The counterparty's credit risk is determined based on the credit ratings as referenced from their interest coverage ratio. Management believes that it represents the reasonable approximation of market rate on MNT funding in case of credit risk related to these corporate entities.

Information about fair values of these promissory notes using assumptions that are not based on observable market data is disclosed in Notes 33.

Control over Deposit Insurance Corporation (DICOM). Management applies judgement to determine whether the substance of the relationship between BOM and DICOM indicates whether DICOM is controlled by the BOM or not. In making this judgement, management considers the following:

4. CRITICAL ACCOUNTING ESTIMATES, AND JUDGEMENTS IN APPLYING ACCOUNTING (CONTINUED)

- power over the DICOM.
- exposure, or rights, to variable returns from its involvement with the DICOM; and ability to use its power over the DICOM to affect the amount of the BOM' s returns. The BOM has power over DICOM if it can direct the relevant activities of DICOM. According to the Charter of DICOM, the National Committee has seven members, and is chaired by the First Deputy Governor of BOM. The remaining six members comprise of the following:
    - State Secretary in charge of finance and budget issues.
    - Standing Commissioner of the Mongolian Financial Regulatory Commission.
    - Executive Director of DICOM.
    - Three members to be nominated by the Governor of BOM, Minister of Finance and Mongolian Bankers Association (an independent Association made up of local banks and financial institutions and does not include BOM) and to be appointed by the joint decisions of the Governor of BOM and Minister of Finance.

All decisions concerning the activities of DICOM must be approved by vote from each of the seven members of the National Committee and no member has any unilateral power to direct the activities of DICOM. Despite the BOM having its First Deputy Governor chairing the National Committee, the fact that the Chairman does not have any unilateral power to direct the activities of DICOM and that the BOM has limited influence in the appointment of the remaining three members of the National Committee sufficiently demonstrates that the BOM does not have control over DICOM. Therefore, management concluded that DICOM should not be consolidated into these financial statements.

Control over banks under receivership. Management applies judgement to determine whether the substance of the relationship between BOM and banks under receivership indicates whether these banks are controlled by the BOM or not. In making this judgement, management considers the following:

- the receiver is appointed by the BOM following the requirements of the Law.
- the receiver effectively acts in a fiduciary capacity and has narrow objective to wind up the bank and there are not any strategic decisions to be made.
- the receiver acts within the prescribed legal framework and the order of priority of liabilities is also set by the legislation, therefore the receiver cannot use its power specifically with the aim to influence benefits attributable to the BOM.
- further benefits received from receivership are limited with low variability.

Based on above, although the BOM has power to govern activities of banks under receivership, it cannot use that power to influence its own benefits as those benefits are independent from performance of banks under receivership. Therefore, management believes that these banks should not be consolidated into these financial statements.

Revaluation of buildings. The Bank measures its buildings at revalued amounts with changes in fair value being recognized in other comprehensive income (OCI). In 2018, the Bank engaged an independent valuation specialist to assess the fair value of the buildings. Buildings were valued by reference to market-based evidence, using comparable prices adjusted for specific market factors such as nature, location, and condition of the buildings.

4. CRITICAL ACCOUNTING ESTIMATES, AND JUDGEMENTS IN APPLYING ACCOUNTING (CONTINUED)

As at 31 December 2021, and 31 December 2020, management has assessed that the fair values of buildings has not changed significantly from the carrying amounts. This assessment requires exercise of judgement from management based on their experience on those properties as well as other assumptions described in Note 18.

Treasury Fund

Recognition. The Bank is a sole body, which is entitled to run day to day operation of the Treasury Fund according to the Law on the State Treasury Fund. Treasury Fund is comprised of heritage assets including historical, cultural, and inherited valuables and coins issued in 1925. These are exhibited in the museum to the public, and the proceeds from tickets are recognized as other operating income in the profit or loss of the Bank. Reserve Management Financial Markets Department is responsible for management of the Fund's operation, maintenance, safeguard, and security. Therefore, management believes that the Treasury Fund should be recognized as an asset in the statement of financial position of the Bank as economic benefit from the Fund flows to the Bank and the Fund is controlled by the Bank based on the Law on the State Treasury Fund. The coins were withdrawn from the circulation in 1938. The management is of the opinion that these coins, despite the fact that they were produced by the legal predecessor bank of the BOM, should be recognized as an asset as in the Management's understanding they were donated to the Treasury Fund by the Government.

Management of the Bank believes that Mongolian coins from 1925 meet recognition criteria based on following factors:

- Mongolian coins issued in 1925 have been withdrawn from the circulation in 1938 based on decision of the Ministry of Finance of Mongolia. Those coins have been replaced with newly issued banknotes.
- Following the decision of the Government to establish the Treasury Fund, these coins were donated to the Fund by the Government with the objective for the BOM to control and safeguard them as part of the BOM's responsibility to manage the Fund.
- The Bank has a right to accumulate gains or incur losses from sales/transfers of those coins to the third parties, based on sales or transfers pre-approved by the Government.
- Statement letter is received from the Mongolian National Centre for Cultural Heritage, which states that the coins from 1925 are the first coins issued after the establishment of the People's Republic of Mongolia, evidence of the establishment of the national currency in Togrogs, important items representing the history of the BOM and belong to the "cultural heritage" in accordance with the Article 3.1.1 of the Law on Protection of Cultural Heritage.

Measurement. The Bank measures the treasury fund at revalued amounts with changes in the fair value being recognized in other comprehensive income ("OCI"). Fair value is to be determined by internationally recognised valuation company as per International Valuation Standards. As at 31 December 2021, the treasury fund amounted to MNT 1,115,085 million (2020: MNT 1,071,665 million). The fair value hierarchy of the treasury assets are categorized as level 3 in which the valuations are based on unobservable market data which involves significant judgement. Refer to Note 33 for details of fair value measurement.

BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

4. CRITICAL ACCOUNTING ESTIMATES, AND JUDGEMENTS IN APPLYING ACCOUNTING (CONTINUED)

Changes in presentation. During the year, the Bank has changed its classification within the statement of profit or loss and statement of cash flows for presentation purposes. The Bank believes that the change provides reliable and more relevant information.

The effect of reclassifications for presentation purposes was as follows on amounts for the year ended 31 December 2020:

In millions of Mongolian Togrogs	**Note**	**2020 (as previously reported)**	**Reclassification**	**2020 (reclassified)**
Interest income calculated using the effective interest method	26	694,862	(460,500)	234,362
Other similar income	26	-	42,810	42,810
Interest expense	26	(1,095,830)	279,419	(816,411)
Losses less gains from derivative financial instruments		(381,196)	138,271	(242,925)
Losses less gains from trading of gold bullion and precious metals	27	879,608	(151,293)	728,315
Gold bullion and precious metals translation losses less gains		-	151,293	151,293
Losses less gains from trading in foreign currencies		-	(1,356)	(1,356)
Foreign exchange translation losses less gains		(459,090)	1,356	(457,734)
LOSS FOR THE YEAR		**(361,646)**	**-**	**(361,646)**

BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

4. CRITICAL ACCOUNTING ESTIMATES, AND JUDGEMENTS IN APPLYING ACCOUNTING (CONTINUED)

In millions of Mongolian Togrogs	Note	2020 (as previously reported)	Reclassification	2020 (reclassified)
Cash flows from operating activities				
Losses from disposal in debt securities at fair value through other comprehensive income		-	(3,262)	(3,262)
Gains/(loss) from disposal of financial investments in debt securities		-	6	6
Losses less gains from derivative financial instruments		(138,813)	381,738	242,925
Other similar income		(460,500)	417,690	(42,810)
Interest expense		1,095,830	(279,419)	816,411
Net (increase) in treasury fund		(2,805)	2,805	-
Net (Increase) in debt securities		(680,150)	680,150	-
Net decrease/(increase) in due from foreign financial institution		-	(1,698)	(1,698)
Net decrease in other assets		20,295	421,829	442,124
Net (decrease)/increase in other liabilities		331,892	(801,934)	(470,042)
Interest received		637,014	(421,829)	215,185
Interest paid		(1,097,097)	281,926	(815,171)
Cash flows from investing activities				
Acquisition of Treasury fund	14	-	(2,805)	(2,805)
Acquisition of debt securities at fair value through other comprehensive income		(1,589,766)	(292,273)	(1,882,039)
Acquisition of investment in debt securities carried at amortised cost		-	(751,163)	(751,163)
Proceeds from redemption of debt securities at fair value through other comprehensive income		933,596	122,662	1,056,258
Proceeds from redemption of debt securities carried at amortised cost		-	243,880	243,880
Cash flows from financing activities				
Proceeds from liabilities due to foreign parties	23	238,598	45,766	284,364
Repayment of liabilities due to foreign parties	23	-	(45,766)	(45,766)
Cash and cash equivalents at the end of the year		**4,752,271**	**(1,698)**	**4,750,573**

5. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS

The following amendments became effective from 1 January 2021:

COVID-19-Related Rent Concessions Amendment to IFRS 16 (issued on 28 May 2020 and effective for annual periods beginning on or after 1 June 2020). The amendment provides lessees with relief in the form of an optional exemption from assessing whether a rent concession related to COVID-19 is a lease modification. Lessees can elect to account for rent concessions in the same way as if they were not lease modifications. The practical expedient only applies to rent concessions occurring as a direct consequence of the COVID-19 pandemic and only if all of the following conditions are met: the change in lease payments results in revised consideration for the lease that is substantially the same as, or less than, the consideration for the lease immediately preceding the change; any reduction in lease payments affects only payments due on or before 30 June 2021; and there is no substantive change to other terms and conditions of the lease. At 31 March 2021, in light of the on-going pandemic, the IASB published additional amendment to extend the date for the concessions from 30 June 2021 to 30 June 2022 (effective for annual periods beginning on or after 1 April 2021). The amendment is not expected to have any material impact on the Bank's financial statements.

Interest rate benchmark (IBOR) reform – phase 2 amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16 (issued on 27 August 2020 and effective for annual periods beginning on or after 1 January 2021). The Phase 2 amendments address issues that arise from the implementation of the reforms, including the replacement of one benchmark with an alternative one. The amendments cover the following areas:

- *Accounting for changes in the basis for determining contractual cash flows as a result of IBOR reform:* For instruments to which the amortised cost measurement applies, the amendments require entities, as a practical expedient, to account for a change in the basis for determining the contractual cash flows as a result of IBOR reform by updating the effective interest rate using the guidance in paragraph B5.4.5 of IFRS 9. As a result, no immediate gain or loss is recognised. This practical expedient applies only to such a change and only to the extent it is necessary as a direct consequence of IBOR reform, and the new basis is economically equivalent to the previous basis.

  Insurers applying the temporary exemption from IFRS 9 are also required to apply the same practical expedient. IFRS 16 was also amended to require lessees to use a similar practical expedient when accounting for lease modifications that change the basis for determining future lease payments as a result of IBOR reform.

- *End date for Phase 1 relief for non-contractually specified risk components in hedging relationships:* The Phase 2 amendments require an entity to prospectively cease to apply the Phase 1 reliefs to a non-contractually specified risk component at the earlier of when changes are made to the non-contractually specified risk component, or when the hedging relationship is discontinued. No end date was provided in the Phase 1 amendments for risk components.

- *Additional temporary exceptions from applying specific hedge accounting requirements:* The Phase 2 amendments provide some additional temporary reliefs from applying specific IAS 39 and IFRS 9 hedge accounting requirements to hedging relationships directly affected by IBOR reform.

- Additional IFRS 7 disclosures related to IBOR reform: The amendments require disclosure of: (i) how the entity is managing the transition to alternative benchmark rates, its progress and the risks arising from the transition; (ii) quantitative information about derivatives and non-derivatives that have yet to transition, disaggregated by significant interest rate benchmark; and (iii) a description of any changes to the risk management strategy as a result of IBOR reform.

5. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS (CONTINUED)

Effect of IBOR reform. Reform and replacement of various inter-bank offered rates ('IBORs') has become a priority for regulators. Many IBOR rates stopped being published at 31 December 2021, while certain USD LIBOR rates would stop being published by 30 June 2023.

The table below discloses amounts of non-derivative financial liabilities and derivative contracts at 31 December 2021 that would be transitioned to alternative interest rate benchmarks:

In millions of Mongolian Togrogs	**USD LIBOR**	**Total**
NON-DERIVATIVE FINANCIAL LIABILITIES		
Liabilities due to foreign parties	570,417	**570,417**
TOTAL NON-DERIVATIVE FINANCIAL LIABILITIES	**570,417**	**570,417**
DERIVATIVE FINANCIAL INSTRUMENTS		
Interest rate swaps: notional amounts	4,348,663	**4,348,663**
TOTAL DERIVATIVE FINANCIAL INSTRUMENTS	**4,348,663**	**4,348,663**

The Bank is exposed to a risk that the liquidity of the above financial instruments would start to decrease, as the volume of operations with traditional IBOR-based financial instruments is shrinking. The Bank is also exposed to a risk of the potential arbitrage differences between IBOR interest rates and the applicable alternative rates.

The Bank established a working group including members from the Mongolian Bankers Association to study international best practices regarding IBOR reform and to perform the transition of legacy IBOR-based financial instruments to alternative benchmark interest rates including secured overnight financing rate ("SOFR").

The Bank has financing from the People's Bank of China with amount of MNT 5,463,574 million as at 31 December 2021. Interest rate is based on SHIBOR+200 bps per annum. Management is of the opinion that SHIBOR rate will not be ceased. Refer to Note 23.

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6. NEW ACCOUNTING PRONOUNCEMENTS

Certain new standards and interpretations have been issued that are mandatory for the annual periods beginning on or after 1 January 2022 or later, and which the Bank has not early adopted.

New standards or amendments	Effective date
IFRS 17 "Insurance Contracts" (issued on 18 May 2017 and effective for annual periods beginning on or after 1 January 2023)	1 January 2023
Amendments to IFRS 17 and an amendment to IFRS 4 (issued on 25 June 2020 and effective for annual periods beginning on or after 1 January 2023)	1 January 2023
Sale or Contribution of Assets between an Investor and its Associate or Joint Venture – Amendments to IFRS 10 and IAS 28 (issued on 11 September 2014 and effective for annual periods beginning on or after a date to be determined by the IASB)	to be determined by the IASB
Classification of liabilities as current or non-current – Amendments to IAS 1 (issued on 23 January 2020 and effective for annual periods beginning on or after 1 January 2022)	1 January 2022
Classification of liabilities as current or non-current, deferral of effective date – Amendments to IAS 1 (issued on 15 July 2020 and effective for annual periods beginning on or after 1 January 2023)	1 January 2023
Proceeds before intended use, Onerous contracts – cost of fulfilling a contract, Reference to the Conceptual Framework – narrow scope amendments to IAS 16, IAS 37 and IFRS 3, and Annual Improvements to IFRSs 2018-2020 – amendments to IFRS 1, IFRS 9, IFRS 16 and IAS 41 (issued on 14 May 2020 and effective for annual periods beginning on or after 1 January 2022)	1 January 2022
Amendments to IAS 8: Definition of Accounting Estimates (issued on 12 February 2021 and effective for annual periods beginning on or after 1 January 2023)	1 January 2023
Deferred tax related to assets and liabilities arising from a single transaction – Amendments to IAS 12 (issued on 7 May 2021 and effective for annual periods beginning on or after 1 January 2023)	1 January 2023

Unless otherwise described above, the new standards and interpretations are not expected to significantly affect the Bank's financial statements.

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7. CASH AND CASH EQUIVALENTS

In millions of Mongolian Togrogs	Note	31 December 2021	31 December 2020
Cash on hand		177,591	233,373
Due from foreign financial institutions:			
- Short term deposits in foreign currency	8	3,297,154	3,509,327
- Demand deposits	8	789,202	878,068
- Special drawing rights holdings	8	387,299	131,503
Less credit loss allowance		(56)	(1,698)
Total cash and cash equivalents		**4,651,190**	**4,750,573**

The above balances are presented as cash and cash equivalents for the purposes of the Statement of Cash Flows. Refer to Note 32 for the ECL measurement approach.

The table below discloses the credit quality of cash and cash equivalents balances based on credit risk grades at 31 December 2021. Refer to Note 32 for the description of the Bank's credit risk grading system.

In millions of Mongolian Togrogs	Short term deposits in foreign currency	Demand deposits	Special drawing rights holdings	Total
- Excellent	3,297,154	789,202	387,299	4,473,655
Total due from foreign financial institutions included in cash and cash equivalents, excluding cash on hand	**3,297,154**	**789,202**	**387,299**	**4,473,655**
Less: Credit loss allowance	**(1)**	**(55)**	**-**	**(56)**
Carrying amount	**3,297,153**	**789,147**	**387,299**	**4,473,599**

The credit quality of cash and cash equivalents balances based on credit risk grades at 31 December 2020 is as follows.

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NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

7. CASH AND CASH EQUIVALENTS (CONTINUED)

In millions of Mongolian Togrogs	**Short term deposits in foreign currency**	**Demand deposits**	**Special drawing rights holdings**	**Total**
- Excellent	3,509,327	878,068	131,503	4,518,898
Total due from foreign financial institutions included in cash and cash equivalents, excluding cash on hand	**3,509,327**	**878,068**	**131,503**	**4,518,898**
Less: Credit loss allowance	**(9)**	**(1,689)**	**-**	**(1,698)**
Net due from foreign financial institutions included in cash and cash equivalents, excluding cash on hand	**3,509,318**	**876,379**	**131,503**	**4,517,200**

To ECL measurement cash and cash equivalents balances are included in Stage 1. When counterparty is a central bank or international financial institution, which is not rated (such as Bank of England), its rating is equivalent to the country credit rating. Cash on hand and special drawing rights holdings in IMF do not expose the Bank to credit risk. Refer to Note 32 for the ECL measurement approach.

8. DUE FROM FOREIGN FINANCIAL INSTITUTIONS

In millions of Mongolian Togrogs	**31 December 2021**	**31 December 2020**
Short term deposits in foreign currency	3,297,154	3,509,327
Demand deposits	789,202	878,068
Special drawing rights holdings	387,299	131,503
World Bank subscription	179	179
Other subscriptions	12	13
Less: Credit loss allowance	(57)	(1,698)
Total due from foreign financial institutions	**4,473,789**	**4,517,392**

Short term deposits in foreign currency. This balance represents short-term time deposits with foreign central banks and other financial institutions, which are denominated in USD and CNY with initial maturity periods up to 65 days (2020: 29 days).

Demand deposits. This balance represents current account deposits with foreign central banks and other financial institutions.

Special Drawing Rights Holdings. This balance represents Mongolia's holding of special drawing rights to supplement existing reserve assets related to the International Monetary Fund. As at 31 December 2021, the balance is SDR 97.1 million (2020: SDR 35.8 million) and is interest bearing.

World Bank subscription. This balance represents the deposits and quota at the World Bank, as part of the condition to be a member of the World Bank group. This amount is matched by a corresponding liability (see Note 23) and is non-interest bearing. This asset will never be impaired as it is placed in the central banks of OECD countries and other reputable international institutions.

Other subscriptions. This balance represents the subscription amount when Mongolia joined SWIFT network.

The following table contains an analysis of due from foreign financial institutions balances by credit quality at 31 December 2021 based on credit risk grades for the purpose of ECL measurement. All balances are included in Stage 1 as funds are placed in the central banks of OECD countries and other reputable international institutions. Refer to Note 32 for the description of credit risk grading system used by the Bank and the approach to ECL measurement, including the definition of default and SICR as applicable to due from other banks balances. The carrying amount of due from foreign financial institutions balances at 31 December 2021 and 31 December 2020 below also represents the Bank's maximum exposure to credit risk on these assets:

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8. DUE FROM FOREIGN FINANCIAL INSTITUTIONS (CONTINUED)

In millions of Mongolian Togrogs	**31 December 2021 Stage 1 (12-months ECL)**	**31 December 2020 Stage 1 (12-months ECL)**
- Excellent	4,473,846	4,519,090
Gross carrying amount	**4,473,846**	**4,519,090**
Less: Credit loss allowance	(57)	(1,698)
Carrying amount	**4,473,789**	**4,517,392**

Special drawing rights holdings in IMF, World Bank subscription and other subscriptions do not expose the Bank to credit risk as these are placed in the central banks of OECD countries and other reputable international institutions.

None of these balances are collateralized. Refer to Note 33 for the estimated fair value of each class of amounts due from foreign financial institutions. Interest rate analysis of due from foreign financial institutions is disclosed in Note 32.

The following tables explain the changes in the credit loss allowance between the beginning and the end of the annual period.

In millions of Mongolian Togrogs	**31 December 2021**	**31 December 2020**
1 January	**1,698**	**11**
Credit loss (reversal)/expense	(1,641)	1,687
At 31 December	**57**	**1,698**

9. LOANS TO LOCAL BANKS

Loans to Local Banks

In millions of Mongolian Togrogs	31 December 2021	31 December 2020
Loans issued under Price Stabilization Program	852,376	383,799
Other loans	669,803	93,960
Gross carrying amount of loans to local banks before credit loss allowance	**1,522,179**	**477,759**
Less credit loss allowance	(34,871)	(16,445)
Total loans to local banks at AC	**1,487,308**	**461,314**

Gross carrying amount and credit loss allowance amount for loans to local banks at amortised cost by classes at 31 December 2021 and 31 December 2020 are disclosed in the table below:

	31-Dec-21			31-Dec-20		
In millions of Mongolian Togrogs	Gross carrying amount	Credit loss allowance	Carrying amount	Gross carrying amount	Credit loss allowance	Carrying amount
Loans to local banks						
Loans under Price Stabilization Program	852,376	(27,310)	**825,066**	383,799	(14,960)	**368,839**
Other loans	669,803	(7,561)	**662,242**	93,960	(1,485)	**92,475**
Total loans and advances to customers at AC	**1,522,179**	**(34,871)**	**1,487,308**	**477,759**	**(16,445)**	**461,314**

Loans issued under Price Stabilization Program

Starting from November 2012, the Bank has issued loans to local banks for the purposes of further lending to local companies from selected industries as part of the Government Price Stabilization Program. These loans were issued under terms and conditions defined by a Government joint resolution and the Bank has no discretion in defining the terms. In addition, decisions on participation of particular companies in the program are also approved by the Government and the companies selected are entitled to obtain loans, which are refinanced by the Bank, from any local bank.

Interest rate at which the loans have been granted to local banks varies between 0.89% to 4% per annum varied by subprograms. Management has concluded that no loss on initial recognition of these loans should be recognised in its financial statements, in case of Price Stabilization Program. Please refer to related accounting policy in Note 3 and management judgement in Note 4.

9. LOANS TO LOCAL BANKS (CONTINUED)

Under the Apartment Mortgage Funding Agreement signed by the Bank, the Government of Mongolia, Mongolian Mortgage Corporation (MIK) and local banks, the Bank receives Senior Residential Mortgage-Backed Securities (Senior RMBS) bonds in settlement of the loans to local banks issued under the Price Stabilization Program.

In 2021 and 2020, the Bank issued only mortgage loan financing under the framework of the Price Stabilization Program. Outstanding balance as at 31 December 2021 in the amount of MNT 852,376 million (2020: MNT 383,799 million) represents mortgage loan financing under the framework of the Price Stabilization Program and loans bear interest rate of 1%, 2% and 4% per annum with maturity of 1 years to 6 years.

In implementing measures against impact of Covid-19 pandemic under "Law to prevention, combat, and reduction of social and economic impacts of the COVID-19" enacted in 2020, the Bank has provided six-months payment holidays on the mortgage loan financing provided to local banks starting from 25 November 2020 until 1 July 2021 to reduce the financial burden on the individual borrowers.

The "Law to prevention, combat, and reduction of social and economic impacts of the COVID-19" was amended at 31 January 2022, which extended the payment holiday on the mortgage loan financing provided to local banks until 31 December 2022. As this has been considered as a modification in the loan agreement, the management has calculated modification loss for the period during payment holidays and resulted in an insignificant amount of losses to the financial statement. Therefore, the modification losses have not been adjusted to the carrying amount of the loans.

Other loans

Loans in local currency. The loans in local currency included in "Other loans", consist of loans related to the programs of ADB in the amount of MNT 1,811 million (2020: MNT 2,350 million), Government of Germany through KFW in the amount of MNT 8,358 million (2020: MNT 11,944 million), Gold-2 project in the amount of MNT 347,640 million (2020: MNT 72,828 million), secured loan in the amount of MNT 14,318 million (2020: MNT 6,100 million) and Fuel Stability Program in the amount of MNT 297,005 million (2020: nil).

Loans related to ADB programs were disbursed to various local banks in Mongolia, for further lending to Mongolian enterprises. This funding was made available by Asian Development Bank to create more job opportunities for the people of Mongolia. The loans bear interest at a rate of 7% per annum (2020: 7% per annum) and the repayment terms due in 2022 for each disbursed loan vary according to the date of disbursement.

Loans disbursed to local banks for further lending to Mongolian enterprises to promote small and medium scale companies were made available under two separate I and II programs by the Government of Germany through KfW. As per loan agreement, the BOM has the right to automatically withdraw funds from the accounts of the local banks with the BOM when repayments are due from 2022 to 2025.

Under a framework of Gold-2 project approved by Parliament order 32 issued in 2020 and Government of Mongolia order 167 issued in 2017 as well as in relation to "Law to reduce the social and economic impact of the coronavirus pandemic" enacted in 2020, the Bank has started financing domestic gold mining entities through commercial banks since 2020 for a purpose to increase foreign exchange reserves of Mongolia by supporting the gold miners' working capital. The loan bears interest rate of policy rate plus 3% and has term up to 24-36 months. According to the financing agreement, the Bank has a right to withdraw the repayments from the current account of respective commercial banks at the BOM upon repayment date.

9. LOANS TO LOCAL BANKS (CONTINUED)

Starting from December 2021, the Bank has issued loans to local banks for the purposes of further lending to local petroleum companies in order to stabilize fuel price according to the "Law to reduce the social and economic impact of the coronavirus pandemic" enacted in 2020. The loan bears interest rate of policy rate and has term up to 12 months. According to the financing agreement, the Bank has a right to withdraw the repayments from the current account of respective commercial banks at the BOM upon repayment date.

Loans in foreign currency. The loans in foreign currency, included as part of "Other loans", consist of loans for improving the local banks' systems and enhancing the capability of banking specialists under the program of ADB in the amount of MNT 671 million (2020: MNT 738 million).

Loans for improving the local banks' software and enhancing the capability of banking specialists are provided by the Bank to local banks to finance the training conducted by DAI (Thailand) Limited Company in accordance with the agreement signed between Mongolia and the Asian Development Bank. Repayment period of this loan is 14 years.

As disclosed in Note 32, the largest Mongolian local banks are rated by international rating agencies. In case of unrated Mongolian local banks, the Bank considers financial conditions of related local bank based on the recent financial information, compliance with prudential ratios, and other information available for assessing credit quality of related assets.

The credit loss allowance for loans to local banks recognised in the period is impacted by a variety of factors, details of ECL measurement are provided in Note 32. The main movements in the table are described below:

- Transfers between Stage 1, 2 and 3 due to balances experiencing significant increases (or decreases) of credit risk or becoming credit-impaired in the period, and the consequent "step up" (or "step down") between 12-month and Lifetime ECL.
- Additional allowances for new financial instruments recognised during the period, as well as releases for financial instruments derecognised in the period.

The following tables disclose the changes in the credit loss allowance and gross carrying amount for loans and advances to customers carried at amortised cost between the beginning and the end of the reporting and comparative periods. Movements in the credit loss allowances and gross carrying amount of other loans to local banks during 2021 are as follows:

9. LOANS TO LOCAL BANKS (CONTINUED)

In millions of Mongolian Togrogs	Credit loss allowance				Gross carrying amount			
	Stage 1 (12-months ECL)	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**
At 31 December 2020	**8,707**	**-**	**7,738**	**16,445**	**458,819**	**6,100**	**12,840**	**477,759**
Movements with impact on credit loss allowance charge for the period:								
Transfers:								
- to lifetime (from Stage 1 to Stage 2)	(1,943)	1,943	-	-	(14,313)	14,313	-	-
- to credit-impaired (from Stage 1 and Stage 2 to Stage 3)	-	-	-	**-**	-	(6,100)	6,100*	**-**
New originated or purchased	15,135	-	-	**15,135**	1,255,189	-	-	**1,255,189**
Changes to ECL measurement model assumptions	-	5,102	-	**5,102**	-	-	-	**-**
Derecognised during the period	(1,811)	-	-	**(1,811)**	(210,363)	-	(6,100)	**(216,463)**
Changes in accrued interest	-	-	-	**-**	5,691	3	-	**5,694**
Total movements with impact on credit loss allowance charge for the period	**11,381**	**7,045**	**-**	**18,426**	**1,036,204**	**8,216**	**-**	**1,044,420**
At 31 December 2021	**20,088**	**7,045**	**7,738**	**34,871**	**1,495,023**	**14,316**	**12,840**	**1,522,179**

* Following loan on stage 3 is over-collateralized.

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9. LOANS TO LOCAL BANKS (CONTINUED)

Movements in the credit loss allowances and gross carrying amount of other loans to local banks during 2020 are as follows:

	Credit loss allowance				Gross carrying amount			
In millions of Mongolian Togrogs	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**
At 31 December 2019	**3,059**	**-**	**4,707**	**7,766**	**437,453**	**-**	**13,231**	**450,684**
Movements with impact on credit loss allowance charge for the period:								
Transfers:								
- to lifetime (from Stage 1 to Stage 2)	-	-	-	**-**	(6,100)	6,100*	-	**-**
New originated or purchased	12,319	-	-	**12,319**	288,675	-	-	**288,675**
Derecognised during the period	(6,671)	-	-	**(6,671)**	(261,261)	-	(339)	**(261,600)**
Changes to ECL measurement model assumptions	-	-	3,031	**3,031**	-	-	-	**-**
Total movements with impact on credit loss allowance charge for the period	**5,648**	**-**	**3,031**	**8,679**	**21,314**	**6,100**	**(339)**	**27,075**
At 31 December 2020	**8,707**	**-**	**7,738**	**16,445**	**458,767**	**6,100**	**12,892**	**477,759**

* Following loan on stage 2 is over-collateralized.

Analysis of loans by credit quality at 31 December 2021 based on credit risk grades (Note 32) is disclosed as follows:

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NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

9. LOANS TO LOCAL BANKS (CONTINUED)

In millions of Mongolian Togrogs	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit impaired)**	**Total**
Loans to local banks				
- Good	1,495,023	-	-	**1,495,023**
- Satisfactory	-	14,316	-	**14,316**
- Default	-	-	12,840	**12,840**
Gross carrying amount	**1,495,023**	**14,316**	**12,840**	**1,522,179**
Less: Credit loss allowance	(20,088)	(1,943)	(12,840)	(34,871)
Carrying amount	**1,474,935**	**12,373**	**-**	**1,407,308**

Analysis of loans by credit quality at 31 December 2020 based on credit risk grades (Note 32) is disclosed as follows:

In millions of Mongolian Togrogs	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit impaired)**	**Total**
Loans to local banks				
- Good	458,767	-	-	**464,867**
- Satisfactory	-	6,100	-	**6,100**
- Default	-	-	12,892	**12,892**
Gross carrying amount	**458,767**	**6,100**	**12,892**	**477,759**
Less: Credit loss allowance	(8,707)	-	(7,738)	(16,445)
Carrying amount	**450,060**	**6,100**	**5,154**	**461,314**

None of the loans to local banks are collateralized as at 31 December 2021. Secured loans to local banks in the amount of MNT 13,670 million were collateralized by performing loan portfolio of the debtor as at 31 December 2020.

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NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

10. INVESTMENT IN DEBT SECURITIES

In millions of Mongolian Togrogs	31 December 2021	31 December 2020
Debt securities at FVOCI	3,080,813	2,350,220
Debt securities at AC	3,313,009	2,924,909
Total investments in debt securities	**6,393,822**	**5,275,129**

The table below discloses investments in debt securities at 31 December 2021 by measurement categories and classes:

In millions of Mongolian Togrogs	Debt securities at FVOCI	Debt securities at AC	Total
Investment in debt securities:			
Bonds issued by Bank for International Settlements	1,647,228	-	**1,647,228**
RAMP Investment Account Assets	928,574	-	**928,574**
US treasury bills	244,529	-	**244,529**
BIS Investments	146,463	-	**146,463**
IBRD Bonds	52,694	-	**52,694**
KfW bonds	30,085	-	**30,085**
China government bonds	22,670	-	**22,670**
European Investment Bank bond	8,570	-	**8,570**
Senior RMBS Bonds	-	2,203,680	**2,203,680**
Erdenes bonds	-	780,615	**780,615**
Erdenes Tavan Tolgoi bonds	-	320,045	**320,045**
Lease backed bonds	-	101,556	**101,556**
Total investments in debt securities at 31 December 2021 (fair value or gross carrying value)	**3,080,813**	**3,405,896**	**6,486,709**
Credit loss allowance	-	(92,887)	**(92,887)**
Total investments in debt securities at 31 December 2021 (carrying value)	**3,080,813**	**3,313,009**	**6,393,822**

10. INVESTMENTS IN DEBT SECURITIES (CONTINUED)

The table below discloses investments in debt securities at 31 December 2020 by measurement categories and classes:

In millions of Mongolian Togrogs	Debt securities at FVOCI	Debt securities at AC	Total
Investment in debt securities:			
RAMP Investment Account Assets	930,566	-	**930,566**
Bonds issued by Bank for International Settlements	898,352	-	**898,352**
US treasury bills	278,804	-	**278,804**
BIS Investments	146,569	-	**146,569**
IBRD bonds	47,800	-	**47,800**
KfW bonds	30,554	-	**30,554**
European Investment Bank bond	17,575	-	**17,575**
Senior RMBS bonds	-	2,324,824	**2,324,824**
Erdenes bonds	-	547,155	**547,155**
Development Bank securities	-	55,650	**55,650**
Lease backed bonds	-	34,694	**34,694**
Total investments in debt securities at 31 December 2020 (fair value or gross carrying value)	**2,350,220**	**2,962,323**	**5,312,543**
Credit loss allowance	-	(37,414)	**(37,414)**
Total investments in debt securities at 31 December 2020 (carrying value)	**2,350,220**	**2,924,909**	**5,275,129**

(a) Debt securities at FVOCI

Debt securities at FVOCI are included in Stage 1 and credit risk exposure based on credit risk grades were "excellent". Refer to Note 32 for the description of credit risk grading system used by the Bank and the approach to ECL measurement, including the definition of default and SICR as applicable to debt securities at FVOCI.

Bonds issued by Bank for International Settlements (BIS) represent quoted debt securities and thus are measured at fair value, which is based on market price of the bonds. At the end of financial year, the balance consists of USD 578.2 million equivalent to MNT 1,647,228 million (2020: USD 315.3 million equivalent to MNT 898,352 million). Maturity of these bonds is 30 days to 94 days (2020: 117 days) and bear interest rate and yield of 0.1% to 2.96% per annum (2020: 0.1% to 2.4% per annum). The Bank invests into these securities due to their low credit risk and high reputation of the BIS. Bonds are not collateralized. For more information, refer to Note 32.

Reserves Advisory and Management Program (RAMP) Investment Account Assets In order to improve and strengthen foreign currency management the BOM has been implementing World Bank's "Resource management improvement consulting and resource management" project since 2011.

10. INVESTMENTS IN DEBT SECURITIES (CONTINUED)

As at 31 December 2021, the Investment Account Assets consist of cash balance in the amount of USD 0.3 million equivalent to MNT 917 million (2020: USD 0.3 million equivalent to MNT 956 million), and securities in the amount of USD 326 million equivalent to MNT 927,657 million (2020: USD 326 million equivalent to MNT 929,610 million). The custodian of the Investment Account Assets is the Federal Reserve Bank of New York.

The securities representing a major part of investment account assets mainly include US Treasury bills and securities issued by other governmental agencies. Credit risk grade of debt securities included in Investment Account Assets are excellent and credit rating ranged from Aa3 to Aaa based on Moody's ratings or equivalents of Standard and Poor's and/or Fitch ratings. For more information, refer to Note 32.

US treasury bills At the end of the financial year, the balance of bonds consists of USD 85.9 million equivalent to MNT 244,607 million (2020: USD 97.9 million equivalent to MNT 279,071). Maturity of these bonds is 1 year to 3 years (2020: 1 to 3 years) and interest rate and yield of 0.13% to 2% per annum (2020: 1.125% to 2.75% per annum). These are not collateralized. For more information, refer to Note 32.

BIS Investment In order to improve foreign currency reserve management, the BOM has implemented BIS's resource management improvement consulting and resource management project since 2019. As at 31 December 2021, the Investment account in the amount of USD 51.4 million equivalent to MNT 146,463 million (2020: USD 51 million equivalent to MNT 146,569 million).

The securities representing a major part of investment account assets mainly include US Treasury bills and securities issued by other governmental agencies. Credit risk grade of debt securities included in Investment Account Assets are excellent and credit rating ranged from Aa3 to Aaa based on Moody's ratings or equivalents of Standard and Poor's and/or Fitch ratings. For more information, refer to Note 32.

According to the financing agreement made with BIS dated on 3 December 2021, the Bank pledged BIS investments and obtained financing of USD 43 million from the BIS. Refer to Note 23 for the details of the BIS investment.

IBRD bonds The BOM invested in the IBRD bonds denominated in USD issued by the International Bank for Reconstruction and Development. At the end of financial year, the balance consists of USD 18.5 million equivalent to MNT 52,703 million (2020: USD 18.5 million equivalent to MNT 47,864 million). Maturity years of the bonds ranges from 3 years to 5 years (2020: 3 years) with average rate of interest rate of 0.1% to 2.13% per annum (2020: 0.1% to 2.13% per annum). These bonds are not collateralized.

KfW bonds At the end of financial year, the balance of bonds consists of USD 10.7 million equivalent to MNT 30,097 million (2020: USD 10.7 million equivalent to MNT 30,642 million). Maturity of these bonds is 3 years (2020: 3 years) and interest rate and yield of 1.38% per annum (2020: 1.38% per annum). These are not collateralized. For more information, refer to Note 32.

China Government bond The BOM invested in China Government bond denominated in CNY issued by People's Bank of China (PBC) in 2021. At the end of financial year, the balance consists of CNY 50.7 million equivalent to MNT 22,681 million (2020: nil). Maturity of these bond is 1 year and interest rate and yield of 2.24% per annum. These are not collateralized. For more information, refer to Note 32.

European Investment Bank bond at the end of financial year, the balance of bonds consists of USD 3 million equivalent to MNT 8,572 million (2020: USD 6 million equivalent to MNT 17,578). Maturity of these bonds is 3 years (2020: 3 years) and interest rate and yield of 1.75% per annum (2020: 1.75% per annum). These are not collateralized. For more information, refer to Note 32.

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10. INVESTMENTS IN DEBT SECURITIES (CONTINUED)

Movements in the credit loss allowance and in the gross amortised cost amount of investments in debt securities at FVTOCI were as follows as at 31 December 2021.

	Credit loss allowance		Gross carrying amount	
In millions of Mongolian Togrogs	**Stage 1 (12-months ECL)**	**Total**	**Stage 1 (12-months ECL)**	**Total**
Investments in debt securities at FVTOCI				
At 31 December 2020	**421**	**421**	**2,350,641**	**2,350,641**
Movements with impact on credit loss allowance charge for the period:				
New originated or purchased	72	72	4,986,979	4,986,979
Derecognised during the period	(380)	(380)	(4,262,051)	(4,262,051)
Changes in accrued interest	-	-	99	99
Other movements	-	-	(589)	(589)
Total movements with impact on credit loss allowance charge for the period	**(308)**	**(308)**	**724,438**	**724,438**
Movements without impact on credit loss allowance charge for the period:				
FX and other movements	-	-	5,847	5,847
At 31 December 2021	**113**	**113**	**3,080,926**	**3,080,926**

Movements in the credit loss allowance and in the gross amortised cost amount of investments in debt securities at FVTOCI were as follows as at 31 December 2020.

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10. INVESTMENTS IN DEBT SECURITIES (CONTINUED)

In millions of Mongolian Togrogs	Credit loss allowance Stage 1 (12-months ECL)	Credit loss allowance Total	Gross carrying amount Stage 1 (12-months ECL)	Gross carrying amount Total
Investments in debt securities at FVTOCI				
At 31 December 2019	**80**	**80**	**1,449,923**	**1,449,923**
Movements with impact on credit loss allowance charge for the period:				
New originated or purchased	381	381	1,590,147	1,590,147
Derecognised during the period	(40)	(40)	(758,933)	(758,933)
Changes in accrued interest	-	-	2,478	2,478
Other movements	-	-	4,854	4,854
Total movements with impact on credit loss allowance charge for the period	**341**	**341**	**838,546**	**838,546**
Movements without impact on credit loss allowance charge for the period:				
FX and other movements	-	-	62,172	62,172
At 31 December 2020	**421**	**421**	**2,350,641**	**2,350,641**

(b) Debt securities at AC

Senior Residential Mortgage-Backed Securities (Senior RMBS) Bonds issued by MMC JSC subsidiaries
The Bank signed the Residential Mortgage Funding Agreement - a three-way agreement with MMC and the local banks in Mongolia on 13 June 2013. Starting from 2016, agreement was renewed, and government of Mongolia included in this arrangement. The Bank receives the RMBS Senior Bonds issued by MMC to the local banks in settlement of its soft loans granted to the local banks under Price Stabilization Program disclosed in Note 9. These bonds earn interest rate of 4.5% and 1% per annum and have a maturity up to 30 years.

Erdenes bonds. According to the Law on "One-time forgiveness of pension-secured loans" issued in January 2020, Erdenes Mongol LLC issued 929,861 bonds ("Erdenes bond") with par value of MNT 1 million each, at 6% interest rate per annum, whose principle is repayable after 5 years, to local commercial banks in exchange for the eligible outstanding pension backed loans, and the BOM is obligated to purchase certain bonds.

The bonds shall be repaid from the operation of "Salkhit" silver and gold deposit owned by one of the subsidiaries of Erdenes Mongol LLC, which is 100% state owned company. The Development Bank of Mongolia independently issued a guarantee with amount of MNT 550 billion in accordance with the Law on "One-time forgiveness of pension-secured loans". In case the BOM's equity decreases due to the possession of Erdenes bonds, the Government shall compensate by issuing government securities to the BOM.

10. INVESTMENTS IN DEBT SECURITIES (CONTINUED)

Erdenes Tavan Tolgoi bonds. According to the "Law on prevention, combat, and reduction of social and economic impacts of the COVID-19" enacted in 2020, the BOM purchased 3,110,000 quantity of the Erdenes Tavan Tolgoi bonds with par value of MNT 100,000 per bond from commercial banks with interest rate of 10% per annum with 2 years of maturity in order to support significant sector of economy.

Lease Backed Bonds Starting from 7 October 2020, the Bank started purchasing into the bonds issued by City Housing Corporation ("NOSK") JSC to support and provide affordable housing to the civil service employees. The Bank purchased 983,162 bonds (2020: 343,556) with a maturity of 15 years (2020: 15 years) and an interest rate of 8% and 6% per annum (2020: 8% per annum), par valued at MNT 100,000 each the bond is collateralized by the rental income from leased property owned by NOSK JSC or the residential apartments.

Development Bank securities on 23 September 2015, the Bank purchased the Development Bank securities at total nominal amount of MNT 60,000 million with 6 years of maturity and 4% coupon rate and management has considered these were below market rate. The fair value of these securities at initial recognition was MNT 31,397 million. The difference between the nominal value of the Development Bank securities and their fair value totalling MNT 28,603 million was recognised as losses on initial recognition in profit or loss for the year ended 31 December 2015. Coupon payments are paid semi-annually. The carrying value of the securities was MNT 55,650 million as at 31 December 2020, and it had been fully repaid in 2021.

For ECL measurement, investment at AC balances are included in stage 1 under "good" credit rating. Refer to Note 32 for the description of credit risk grading system used by the Bank and the approach to ECL measurement, including the definition of default and SICR as applicable to debt securities at AC.

Movements in the credit loss allowance and in the gross amortised cost amount of investments in debt securities at AC were as follows as at 31 December 2021

	Credit loss allowance		Gross carrying amount	
In millions of Mongolian Togrogs	**Stage 1 (12-months ECL)**	**Total**	**Stage 1 (12-months ECL)**	**Total**
At 31 December 2020	**37,414**	**37,414**	**2,962,323**	**2,962,323**
Movements with impact on credit loss allowance charge for the period:				
New originated or purchased	43,873	43,873	791,994	791,994
Derecognised during the period	(4,903)	(4,903)	(342,890)	(342,890)
Changes to ECL measurement model assumptions	16,503	16,503	-	-
Other movements	-	-	(5,531)	(5,531)
Total movements with impact on credit loss allowance charge for the period	**55,473**	**55,473**	**443,573**	**443,573**
At 31 December 2021	**92,887**	**92,887**	**3,405,896**	**3,405,896**

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10. INVESTMENTS IN DEBT SECURITIES (CONTINUED)

Movements in the credit loss allowance and in the gross amortised cost amount of investments in debt securities at AC were as follows as at 31 December 2020.

	Credit loss allowance		Gross carrying amount	
In millions of Mongolian Togrogs	**Stage 1 (12-months ECL)**	**Total**	**Stage 1 (12-months ECL)**	**Total**
At 31 December 2019	**6,627**	**6,627**	**2,436,048**	**2,436,048**
Movements with impact on credit loss allowance charge for the period:				
New originated or purchased	34,010	34,010	1,714,725	1,714,725
Derecognised during the period	(3,223)	(3,223)	(1,044,900)	(1,044,900)
Other movements	-	-	(143,550)	(143,550)
Total movements with impact on credit loss allowance charge for the period	**30,787**	**30,787**	**526,275**	**526,275**
At 31 December 2020	**37,414**	**37,414**	**2,962,323**	**2,962,323**

11. INVESTMENTS IN EQUITY SECURITIES

In millions of Mongolian Togrogs	**31 December 2021**	**31 December 2020**
Equity investments at FVOCI	6,533	6,595
Total investments in equity securities	**6,533**	**6,595**

Equity investments represent unquoted investments in International Investment Bank, International Bank of Economic Co-operation (2020: International Investment Bank, International Bank of Economic Co-operation, and Mongolian Banking Association) that are recorded at fair value which management considers to be approximate to its cost.

12. REVERSE REPURCHASE AGREEMENTS

In millions of Mongolian Togrogs	**31 December 2021**	**31 December 2020**
Federal Reserve Bank of New York	3,091,233	4,393,375
Local banks – in local currency	1,430,989	422,706
Total reverse repurchase agreements measured at AC (gross carrying amount)	**4,522,222**	**4,816,081**
Credit loss allowance	(2)	(13)
Total reverse repurchase agreements measured at AC (carrying value)	**4,522,220**	**4,816,068**

Federal Reserve Bank of New York The Bank entered into Automatic Investment Program arrangement in respect of its deposit account held with Federal Reserve Bank of New York. Under this program, amounts exceeding minimum balance of USD 250,000 are to be invested in Repurchase Agreement Pool ("repo pool") of Federal Reserve Bank of New York.

As at 31 December 2021, the funds invested in repo pool amounted to USD 1,085.1 million equivalent to MNT 3,091,233 million (2020: USD 1,541.8 million equivalent to MNT 4,393,375 million). This investment has 1 day maturity (2020: 4 days) and carries interest rate from 0% to 0.5% per annum (2020: 0% per annum). Though related investments are effectively collateralized, there is no clear identification of securities purchased based on the investment program.

Local banks Reverse repurchase agreements denominated in MNT represents long term and short-term loans to local banks secured by Central bank bills (2020: Central bank bills and Development Bank bonds).

As at 31 December 2021, overnight reverse repurchases agreements with local banks denominated in MNT amounted to MNT 330,191 million with 4 days of maturity and interest rate of 7% per annum is included in reverse repurchase agreement in local currency (2020: MNT 129,141 million with 4 days of maturity at interest rate of 7% per annum). This agreement is secured by Central bank bills.

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12. REVERSE REPURCHASE AGREEMENTS (CONTINUED)

The reverse repurchases agreements with par value of MNT 65,000 million with maturity of 6 years and bears interest rate of 7.5% per annum are secured by bonds issued by Development Bank of Mongolia. Carrying value of the agreements was MNT 62,327 as at 31 December 2020, and it had been fully repaid in 2021. The difference between the par value and the fair value totalling to MNT 23,426 million was recognized as an initial recognition loss in profit or loss for 2016.

As at December 2021, remaining long term repo agreements with local banks denominated in MNT amounted to MNT 1,054,984 million (2020: MNT 230,000 million) with maturity of 2 years (2020: 2 years) and bear annual interest rate of 6% and 6.5% (2020: 6.5%) and those are secured by Central Bank Bills purchased by local banks. Carrying value of the agreements as at 31 December 2021 is MNT 1,100,798 (2020: MNT 231,238 million).

Analysis by credit quality of reverse repurchase agreements of Federal Reserve Bank of New York measured at AC is as follows at 31 December 2021 and 31 December 2020.

In millions of Mongolian Togrogs	**31 December 2021 Stage 1 (12-months ECL)**	**31 December 2020 Stage 1 (12-months ECL)**
Federal Reserve Bank of New York		
- Excellent	3,091,233	4,393,375
Gross carrying amount	**3,091,233**	**4,393,375**
Less: Credit loss allowance	(2)	(13)
Carrying amount	**3,091,231**	**4,393,362**

Analysis by credit quality of reverse repurchase agreements of local banks measured at AC is as follows at 31 December 2021 and 31 December 2020. These assets are fully collateralized by Central bank bills (2020: Central bank bills, Development Bank bonds, and government securities).

In millions of Mongolian Togrogs	**31 December 2021 Stage 1 (12-months ECL)**	**31 December 2020 Stage 1 (12-months ECL)**
Local Banks		
- Good	1,430,989	422,706
Gross carrying amount	**1,430,989**	**422,706**
Less: Credit loss allowance	-*	-*
Carrying amount	**1,430,989**	**422,706**

* Following local banks' reverse repurchase agreements are fully collateralized.

12. REVERSE REPURCHASE AGREEMENTS (CONTINUED)

The following table discloses the changes in the credit loss allowance and gross carrying amount for reverse repurchase agreements carried at amortised cost between the beginning and the end of the reporting period:

In millions of Mongolian Togrogs	Credit loss allowance		Gross carrying amount	
	Stage 1 (12-months ECL)	**Total**	**Stage 1 (12-months ECL)**	**Total**
Reverse repurchases agreements				
At 31 December 2020	**13**	**13**	**4,816,081**	**4,816,081**
Movements with impact on credit loss allowance charge for the period:				
New originated or purchased	2	2	654,733,442	654,733,442
Derecognised during the period	(13)	(13)	(655,029,987)	(655,029,987)
Other movement	-	-	2,686	2,686
Total movements with impact on credit loss allowance charge for the period	**(11)**	**(11)**	**(293,859)**	**(293,859)**
At 31 December 2021	**2**	**2**	**4,522,222**	**4,522,222**

The following table discloses the changes in the credit loss allowance and gross carrying amount for reverse repurchase agreements carried at amortised cost between the beginning and the end of the prior period:

In millions of Mongolian Togrogs	Credit loss allowance		Gross carrying amount	
	Stage 1 (12-months ECL)	**Total**	**Stage 1 (12-months ECL)**	**Total**
Reverse repurchases agreements				
At 31 December 2019	**74**	**74**	**3,254,511**	**3,254,511**
Movements with impact on credit loss allowance charge for the period:				
New originated or purchased	-	-	763,680,353	763,680,353
Derecognised during the period	(61)	(61)	(762,118,783)	(762,118,783)
Total movements with impact on credit loss allowance charge for the period	**(61)**	**(61)**	**(1,561,570)**	**(1,561,570)**
At 31 December 2020	**13**	**13**	**4,816,081**	**4,816,081**

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13. GOLD BULLION AND PRECIOUS METALS

In millions of Mongolian Togrogs	31 December 2021	31 December 2020
At valuation		
Gold bullion	1,594,121	1,404,034
Silver	555	1,853
At cost		
Gold and silver purchased from miners	77,745	353,458
Gold in transit for refining	9,668	24,309
Commemorative coins	3,544	2,203
Total gold bullion and precious metals	**1,685,633**	**1,785,857**

Monetary gold and silver are mainly placed at the Bank of England and JP Morgan Chase Bank.

Gold and silver purchased from miners represent unrefined non-monetary gold and silver that is purchased from local gold miners. Other precious metals including commemorative coins are recognized as inventory and carried at lower of cost and net realizable value.

14. TREASURY FUND

In millions of Mongolian Togrogs	31 December 2021	31 December 2020
Main fund	175,342	145,701
Operational fund	939,743	925,964
Total treasury fund	**1,115,085**	**1,071,665**

Below table shows the movement of the Treasury fund based on nature of the treasuries as at 31 December 2021 and 2020:

In millions of Mongolian Togrogs	Coins	Cultural valuables	Total
Carrying amount at 1 January 2020	917,548	151,312	**1,068,860**
Additions	37	2,768	**2,805**
Carrying amount at 31 December 2020	**917,585**	**154,080**	**1,071,665**
Additions	115	43,305	**43,420**
Carrying amount at 31 December 2021	**917,700**	**197,385**	**1,115,085**

14. TREASURY FUND (CONTINUED)

Treasury Fund is comprised of heritage assets including historical, cultural, inherited valuables, silver and copper coins issued in 1925. These items are exhibited in the museum to the public, and the proceeds from tickets are recognized as other operating income in the profit or loss of the Bank as economic benefit from the Fund flows to the Bank and the Fund is controlled by the Bank based on the Law on the State Treasury Fund. The coins were withdrawn from the circulation in 1938. The management is of the opinion that these coins, despite the fact that they were produced by the legal predecessor bank of the BOM, should be recognized as an asset as in the Management's understanding they were donated to the Treasury Fund by the Government.

Included in the coins as at 31 December 2021 are primarily silver and copper coins originally issued in 1925 by the central bank of which the BOM is a successor with carrying amount of MNT 908,476 million (2020: MNT 908,476 million).

Starting from 2018, management changed its accounting policy to fair value its treasury assets and engaged with external valuation company "Make Difference" LLC to revalue the treasury fund items as per International Valuation Standards. Treasury fund items were valued using direct comparable method and replication method. Direct comparable method is used by reference to market-based evidence including public and online auction houses, using comparable prices adjusted for specific market factors such as origin, condition, symbolical prestige, current possessor, and uniqueness of the items. Replication method is a cost approach, which provides value based on estimated current costs to reproduce property of equal quality, utility, and marketability as near as possible to the original items of nature, quality, and age of material. Information about fair values of items valued using assumptions that are not based on observable market data is disclosed in Note 33.

15. DERIVATIVE FINANCIAL INSTRUMENTS

Financial derivatives represent the fair value of the long-term cross currency interest rate swaps made with local banks and international financial institution. Derivatives have potentially favourable (assets) or unfavourable (liabilities) conditions because of fluctuations in market interest rates, foreign exchange rates or other variables relative to their terms. The aggregate fair values of derivative financial assets and liabilities can fluctuate significantly from time to time. The table below shows the fair values of financial derivatives recorded as assets and liabilities.

In millions of Mongolian Togrogs	**31 December 2021**	**31 December 2020**
Interest rate swaps: fair values, at the end of the reporting period, of		
- Financial assets at fair value through profit or loss	77,103	156,419
- Financial liabilities at fair value through profit or loss	(469,758)	(303,501)
Financial assets at fair value through profit or loss, net	**(392,655)**	**(147,082)**

The table below sets out fair values, at the end of the reporting period, of currencies receivable or payable under long-term cross currency interest rate swaps contracts entered into by the Bank. The table reflects gross positions before netting of any counterparty positions (and payments) and covers the contracts with settlement dates after the end of the respective reporting period.

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15. DERIVATIVE FINANCIAL INSTRUMENTS (CONTINUED)

In millions of Mongolian Togrogs	2021		2020	
	Contracts with positive fair value	**Contracts with negative fair value**	**Contracts with positive fair value**	**Contracts with negative fair value**
Interest rate swaps: fair values, at the end of the reporting period, of				
- USD payable on settlement (-)	(370,632)	(741,393)	(271,928)	(810,556)
- MNT receivable on settlement (+)	447,735	271,635	428,347	507,055
Net fair value of interest rate swaps	**77,103**	**(469,758)**	**156,419**	**(303,501)**

16. GOVERNMENT SECURITIES

In millions of Mongolian Togrogs	**31 December 2021**	**31 December 2020**
Government securities	231,778	227,407

Government securities at below market rate. Bank purchased government securities in accordance with the Government conducted “Sain” program with par value of MNT 453,712 million at a coupon rate of 1.0% per annum to 3.0% per annum and maturity from 1 to 15 years in 2016. The fair value of these securities at initial recognition was MNT 123,668 million and the difference between the par value and the fair value totalling MNT 330,044 million was recognized to profit or loss for 2016 as loss on initial recognition. Par value of outstanding government securities as at 31 December 2021 amounted to MNT 374,000 million at coupon rate of 1.0 % per annum and have maturity of 15 years. (2020: MNT 374,000 million at coupon rate of 1.0% per annum, maturity of 15 years). For the fair value disclosure, refer to Note 33.

Government securities are carried at FVOCI. As at 31 December 2021, the carrying value of the securities related to “Sain” program is MNT 231,778 million (2020: MNT 227,407 million). For related accounting policy and management’s judgement, refer to Note 3 and 4.

ECL allowances for the government securities measured at FVOCI amounting to MNT 5,842 million (2020: MNT 3,635 million) has been included in movement of the respective other comprehensive income during the year.

All the outstanding balance which represents the maximum exposure to credit risk as at 31 December 2021 and 31 December 2020. Refer to Note 32 for the description of the credit risk grading system used by the Bank and the approach to ECL measurement.

16. GOVERNMENT SECURITIES (CONTINUED)

The following table discloses Government securities measured at FVTOCI:

In millions of Mongolian Togrogs	31 December 2021 Stage 1 (12-months ECL)	31 December 2020 Stage 1 (12-months ECL)
Government securities		
- Good	93,917	82,726
Total AC gross carrying amount	**93,917**	**82,726**
Less: Credit loss allowance	(9,800)	(3,958)
Add: Fair value adjustment from AC to FV	147,661	148,639
Carrying value (fair value)	**231,778**	**227,407**

The following tables disclose the changes in the credit loss allowance and gross carrying amount for government securities carried at fair value through other comprehensive income between the beginning and the end of the reporting and comparative periods.

In millions of Mongolian Togrogs	Credit loss allowance Stage 1 (12-months ECL)	Gross carrying amount Stage 1 (12-months ECL)
Government Securities at FVTOCI		
At 1 January 2021	**3,958**	**82,726**
Movements with impact on credit loss allowance charge for the period:		
Changes to ECL measurement model assumptions	5,842	-
Changes in accrued interest	-	3
Unwinding of discount	-	11,188
At 31 December 2021	**9,800**	**93,917**
Government Securities at FVTOCI		
At 1 January 2020	**323**	**73,257**
Movements with impact on credit loss allowance charge for the period:		
Changes to ECL measurement model assumptions	3,635	-
Changes in accrued interest	-	(3)
Unwinding of discount	-	9,472
At 31 December 2020	**3,958**	**82,726**

None of the government securities are collateralized as at 31 December 2021 and 31 December 2020. For more information on related party transactions, refer to Note 31.

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17. OTHER ASSETS

In millions of Mongolian Togrogs	**31 December 2021**	**31 December 2020**
Other financial assets at AC		
Receivables from Deposit Insurance Corporation	148,958	148,958
Receivables from companies	60,346	60,360
Asset received from Anod Bank	58,534	58,839
Receivables from receivership of Capital bank	54,480	55,271
Promissory notes from receivership of Capital bank	40,040	47,732
Claims on foreign financial institutions	24,906	24,912
Other financial assets	5,140	-
Less: Allowance for credit losses	(318,863)	(305,127)
Total other financial assets at AC	**73,541**	**90,945**
Other non-financial assets		
Prepaid expenses	19,461	31,425
Other	2,232	18,758
Total other non-financial assets	**21,693**	**50,183**
Other assets measured at FVTPL		
Promissory notes	224,487	282,545
Total other assets at FVTPL	**224,487**	**282,545**
Total other assets	**319,721**	**423,673**

Receivables from Deposit Insurance Corporation (DICOM). Receivables from DICOM include an initial disbursement of loan amounts in MNT 119,900 million with 0.5% interest per annum with maturity of 10 years and financial support of MNT 85,000 million with zero percent interest per annum. The purpose of the loan to DICOM of MNT 119,900 million was to ensure the stability of Mongolian banking sector. Based on the contractual terms, this loan is due for repayment on 30 September 2023.

The financial support of MNT 85,000 million had to be repaid by 25 December 2014 from the proceeds of planned privatization of State Bank LLC. However, the privatization of State Bank LLC did not happen, and the financial support has not been repaid. Management has concluded that no loss on initial recognition of these loans should be recognised in its financial statements. Please refer to related accounting policy in Note 3 and management judgement in Note 4.

The loan and financial support are staged at 3 as at 31 December 2021 as the financial support of MNT 85,000 million overdue since 2014. ECL measurement of the loan and the financial support are separately assessed with consideration of the arrangements of repayments for each asset. Please refer to management judgement in Note 4. The carrying value of loans to DICOM as at 31 December 2021 is MNT 57,576 million (2020: MNT 54,230 million).

17. OTHER ASSETS (CONTINUED)

Receivables from companies. Receivables from companies include receivables due from gold producing companies that have not fulfilled their obligations under the gold option contracts entered with the Bank in prior years. These receivables amount to MNT 40,075 million (2020: MNT 40,085 million). All of these receivables have been fully provisioned in prior years and are considered at Stage 3, with 100% of PD and LGD as at 31 December 2021 and 31 December 2020.

Remaining balances consist of receivables from non-banking institutions amounting MNT 20,271 million as at 31 December 2021 (2020: MNT 20,275 million). All of these receivables have been fully provisioned in prior years and are considered at Stage 3, with 100% of PD and LGD as at 31 December 2021 and 31 December 2020.

Assets received from Anod Bank. The Bank received assets with carrying amount of MNT 73,662 million when Anod receivership was terminated in 2015 out of which, MNT 305 million and MNT 126 million were recovered in 2021 and 2020, respectively. The assets after recovery of MNT 58,534 million (2020: MNT 58,839 million) are fully provisioned. Under IFRS 9, the assets are assessed at Stage 3 with 100% of PD and LGD.

Receivables from receivership of Capital bank. Receivables from Capital bank receivership is composed of MNT 5,215 million clearing account receivable, MNT 4,602 million Mandatory reserve penalty receivable and MNT 44,663 million receivables in relation to DICOM and MNT 791 million on penalty interest on promissory note acquired by Bank in 2020. In 2021, MNT 791 million on penalty interest on promissory note acquired by the Bank is written off.

Promissory note from receivership of Capital bank. In June 2020, the Bank received promissory note issued by Capital bank receivership as a repayment of receivables related to promissory notes measured at FVTPL from one of local companies as noted below. The promissory note from receivership of Capital bank has par value of MNT 41 billion and MNT 5.7 billion of interest receivable totalling to MNT 46.7 billion, with remaining maturity of one month. As the promissory note was not repaid in July 2020 when it was due, it is categorized at Stage 3 in the ECL assessment with 100% of PD. In 2020, ECL charge of MNT 29,474 million has been recognized in profit or loss for the year.

Claims on foreign financial institutions. Claims on foreign financial institutions is a receivable from Eastern Gates and considered to be non-recoverable and thus fully provisioned since the related foreign institutions were no longer operating. As at 31 December 2021 and 2020, the Bank has assessed this asset at Stage 3 with 100% of PD and LGD.

Receivables related to promissory notes. Promissory notes represent promissory notes issued by local companies with details as follows:

As at 31 December 2021, the Bank holds promissory notes issued by two (2) local companies and a local bank, which have a nominal value of MNT 255,500 million (2020: MNT 367,426 million). These notes have a maturity of 5 years to 7 years (2020: 5 years to 7 years) and earn interest at interest rates defined in related contracts. Most of these contracts specify higher initial interest rate, which can be reduced to below market level, if certain conditions are met. The Bank's management as well as their internal legal departments are of the view that these transactions do not violate any provisions under the Law on Central Bank and other related laws in Mongolia.

Maturity of two of the receivables related to promissory notes were extended to another year in 2021. In terms of the remaining promissory note, the Bank reached an agreement to collect the outstanding receivables through fixed assets and financial assets in 2022 and it was overdue since November 2019.

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Promissory notes are measured at FVTPL and the fair value is estimated using the Discounted Cash Flows. Refer to Note 33 for the disclosure of fair value measurement.

Other non-financial assets. Other non-financial assets consist of the Bank's prepayments, advances to staff, consumable materials, and stationery supplies. Receivables from ADB amounts to MNT 4,500 million (2020: MNT 4,875 million) and project investment amounts MNT 13,729 million (2020: MNT 8,191 million) as at 31 December 2021.

As at 31 December 2020, other non-financial assets include gold received from engaged refining entity to enrich its museum collection which is to be transferred to Treasury fund once cost computation is completed. The non-monetary refined gold and silver is measured at lower of cost and net realizable value and amounted to MNT 29,020 million as at 31 December 2020. These assets are fully transferred to the Treasury Fund in 2021.

Credit loss allowances. Tables below contain an analysis of the credit risk exposure of other financial assets at AC at 31 December 2021.

In millions of Mongolian Togrogs	**Stage 1 (12-months ECL)**	**Stage 2 (lifetime ECL for SICR)**	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**
Other financial assets				
-Satisfactory	-	4,231	-	**4,231**
-Special monitoring	909	-	-	**909**
-Default	-	-	387,264	**387,264**
Gross carrying amount at AC	**909**	**4,231**	**387,264**	**392,404**
Credit loss allowance	(281)	(1,454)	(317,128)	**(318,863)**
Total carrying amount at AC	**628**	**2,777**	**70,136**	**73,541**

Tables below contain an analysis of the credit risk exposure of other financial assets at AC of 31 December 2020.

In millions of Mongolian Togrogs	**Stage 3 (lifetime ECL for credit im-paired)**	**Total**
Other financial assets		
- Default	396,072	**396,072**
Gross carrying amount at AC	**396,072**	**396,072**
Credit loss allowance	(305,127)	**(305,127)**
Total carrying amount at AC	**90,945**	**90,945**

17. OTHER ASSETS (CONTINUED)

Movements in the provision for impairment of other financial and non-financial assets during 2021 are as follows:

	Stage 1	Stage 2	Stage 3						
In thousands of Mongolian Togrogs	Other financial assets (stage 1)	Other financial assets (stage 2)	Asset received from Anod Bank (stage 3)	Promissory notes from receivership of Capital bank (stage 3)	Receivables from Deposit Insurance Corporation (stage 3)	Receiva-bles from receivership of Capital bank (stage 3)	Claims on foreign financial institution (stage 3)	Receivables from other companies (stage 3)	**Total**
Gross carrying amount									
At 1 January 2021	**-**	**-**	**58,839**	**47,732**	**148,958**	**55,271**	**24,912**	**60,360**	**396,072**
Movements with impact on credit loss allowance charge for the period:									
Derecognised during the period	-	-	(305)	(547)	-	-	-	-	**(852)**
Changes in accrued interest	909	4,231	-	-	-	-	-	-	**5,140**
Other movement	-	-	-	(4,354)	-	-	-	-	**(4,354)**
Total movements with impact on credit loss allowance charge for the period	**909**	**4,231**	**(305)**	**(4,901)**	**-**	**-**	**-**	**-**	**(66)**
Movements without impact on credit loss allowance charge for the period:									
FX and other movements	**-**	**-**	**-**	**-**	**-**	**-**	**(6)**	**(14)**	**(20)**
Write-offs	**-**	**-**	**-**	**(2,791)**	**-**	**(791)**	**-**	**-**	**(3,582)**
At 31 December 2021	**909**	**4,231**	**58,534**	**40,040**	**148,958**	**54,480**	**24,906**	**60,346**	**392,404**
Credit loss allowances									
On 1 January 2021	**-**	**-**	**58,839**	**29,474**	**94,728**	**36,814**	**24,912**	**60,360**	**305,127**
Movements with impact on credit loss allowance charge for the period:									
New originated or purchased	281	1,454	-	-	-	-	-	-	**1,735**
Changes to ECL measurement model assumptions	-	-	-	-	-	18,457	-	-	**18,457**
Derecognised during the period	-	-	(305)	(547)	(3,346)	-	-	-	**(4,198)**
Changes in accrued interest	-	-	-	-	-	-	-	-	**-**
Other movements	-	-	-	-	-	-	-	-	**-**

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17. OTHER ASSETS (CONTINUED)

Total movements with impact on credit loss allowance charge for the period	**281**	**1,454**	**(305)**	**(547)**	**(3,346)**	**18,457**	**-**	**-**	**15,994**
Movements without impact on credit loss allowance charge for the period:									
FX and other movements	-	-	-	-	-	-	-	-	-
Write-offs	-	-	-	**(1,447)**	-	**(791)**	**(6)**	**(14)**	**(2,258)**
At 31 December 2021	**281**	**1,454**	**58,534**	**27,480**	**91,382**	**54,480**	**24,906**	**60,346**	**318,863**

Movements in the provision for impairment of other financial and non-financial assets during 2020 are as follows:

	Stage 1	**Stage 3**						
In thousands of Mongolian Togrogs	Other financial assets (stage 1)	Asset received from Anod Bank (stage 3)	Promissory notes from receivership of Capital bank (stage 3)	Receivables from Deposit Insurance Corporation (stage 3)	Receivables from receivership of Capital bank (stage 3)	Claims on foreign financial institutions (stage 3)	Receivables from other companies (stage 3)	**Total**
Gross carrying amount								
At 1 January 2020	-	58,965	-	149,092	54,480	23,898	58,111	**344,546**
Movements with impact on credit loss allowance charge for the period:								
- to credit-impaired (from Stage 1 and Stage 2 to Stage 3)	(49,532)	-	49,532	-	-	-	-	**-**
New originated or purchased	49,532	-	-	-	791	-	-	**50,323**
Derecognised during the period	-	(126)	(1,800)	(134)	-	-	-	**(2,060)**
Other movements	-	-	-	-	-	1,014	2,249	**3,263**
Total movements with impact on credit loss allowance charge for the period	**-**	**(126)**	**47,732**	**(134)**	**791**	**1,014**	**2,249**	**51,526**
At 31 December 2020	**-**	**58,839**	**47,732**	**148,958**	**55,271**	**24,912**	**60,360**	**396,072**
Credit loss allowances								
At 1 January 2020	-	58,965	**-**	105,907	18,696	23,898	58,111	**265,577**

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17. OTHER ASSETS (CONTINUED)

Movements with impact on credit loss allowance charge for the period:								
- to 12-months ECL (from Stage 2 and Stage 3 to Stage 1)	(7,531)	-	7,531	-	-	-	-	-
New originated or purchased	7,531	-	21,943	-	18,118	-	-	**47,592**
Derecognised during the period	-	-	-	(11,179)	-	-	-	**(11,179)**
Changes in accrued interest	-	(126)	-	-	-	-	-	**(126)**
Other movements	-	-	-	-	-	1,014	2,249	**3,263**
Total movements with impact on credit loss allowance charge for the period	**-**	**(126)**	**29,474**	**(11,179)**	**18,118**	**1,014**	**2,249**	**39,550**
At 31 December 2020	**-**	**58,839**	**29,474**	**94,728**	**36,814**	**24,912**	**60,360**	**305,127**

18. PREMISES, EQUIPMENT AND INTANGIBLE ASSETS

In millions of Mongolian Togrogs	Buildings/ premises	Const-ruction in progress	Office and computer equipment	Premises and equipment	Intangible assets	Total
Cost or valuation on 1 January 2020	87,549	38,495	16,740	**142,784**	2,603	**145,387**
Accumulated depreciation/ amortization	(43,778)	-	(6,845)	**(50,623)**	(614)	**(51,237)**
Carrying amount at 1 January 2020	**43,771**	**38,495**	**9,895**	**92,160**	**1989**	**94,150**
Additions	2,125	29,505	10,592	**42,222**	1,958	**44,180**
Disposals - cost	(270)	(11,727)	(2,004)	**(14,001)**	(118)	**(14,119)**
Reclassification	50,781	(53,925)	-	**(3,144)**	3,144	**-**
Transfer to asset held for sale	(5,277)	-	-	**(5,277)**	-	**(5,277)**
Write-offs - cost	-	-	(37)	**(37)**	-	**(37)**
Depreciation/amortization charge	(1,639)	-	(3,123)	**(4,762)**	(1,328)	**(6,090)**
Disposals - accumulated depreciation	254	-	1,991	**2,245**	118	**2,363**
Write-offs - accumulated depreciation	-	-	32	**32**	-	**32**

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18. PREMISES, EQUIPMENT AND INTANGIBLE ASSETS (CONTINUED)

Cost or valuation at 31 December 2020	134,908	2,348	25,291	**162,547**	7,587	**170,134**
Accumulated depreciation/ amortization	(45,163)	-	(7,945)	**(53,108)**	(1,824)	**(54,932)**
Carrying amount at 31 December 2020	**89,745**	**2,348**	**17,346**	**109,439**	**5,763**	**115,202**
Additions	2,526	4,020	6,202	**12,748**	1,330	**14,078**
Disposals - cost	(930)	(4,849)	(1,513)	**(7,292)**	(16)	**(7,308)**
Write-offs - cost	-	-	(29)	**(29)**	-	**(29)**
Depreciation/amortization charge	(2,381)	-	(4,231)	**(6,612)**	(956)	**(7,568)**
Disposals - accumulated depreciation	110	-	1,498	**1,608**	16	**1,624**
Write-offs - accumulated depreciation	-	-	26	**26**	-	26
Cost or valuation at 31 December 2021	136,503	1,519	29,951	**167,973**	8,900	**176,873**
Accumulated depreciation/ amortization	(47,433)	-	(10,651)	**(58,084)**	(2,765)	**(60,849)**
Carrying amount at 31 December 2021	**89,070**	**1,519**	**19,299**	**109,888**	**6,137**	**116,024**

The Bank's premises have been revalued at fair value at 31 December 2018. The valuation was carried out by an independent firm of valuers, Growth Finance Audit LLC, who hold a recognised and relevant professional qualification and who have recent experience in the valuation of assets in similar locations and in a similar category. The basis used for the appraisal was market value, replacement cost and income approach. Fair values were estimated using appropriate valuation techniques and using the following assumptions: For majority of the premises, market approach was assumed to be appropriate as there are sufficient information on comparable assets in the principal market.

For the premises of 2 branches in rural area, cost approach and income approach were used due to the fact that there are insufficient data of similar and comparable assets in their location areas and data obtained had significant difference. Information about fair values of items valued using assumptions that are not based on observable market data and sensitivity analysis are disclosed in Note 33.

Management believes that an overall decrease in value of the Bank’s building is unlikely under the current economic conditions, while any potential increase in value of buildings (leading to increase in property, equipment and intangible assets and equity) would not have material impact on the financial statements from the perspective of users of financial information.

At 31 December 2021, the carrying amount of premises would have been MNT 58,739 million (2020: MNT 59,414 million) had the assets been carried at cost less depreciation. The amount reconciles to the carrying value of the premises as follows:

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18. PREMISES, EQUIPMENT AND INTANGIBLE ASSETS (CONTINUED)

In millions of Mongolian Togrogs	31 December 2021	31 December 2020
Premises at revalued amount in the statement of financial position	89,070	89,745
Revaluation reserve presented in equity	(30,331)	(30,331)
Premises at cost less accumulated depreciation	**58,739**	**59,414**

None of the property, equipment and intangible assets have been pledged as security for borrowings as at 31 December 2021 and 31 December 2020.

19. CASH IN CIRCULATION

In millions of Mongolian Togrogs	31 December 2021	31 December 2020
Banknotes issued to circulation	1,116,970	1,151,315
Uncounted banknotes	(11,403)	(159,867)
Coins issued into circulation	22	22
Cash in circulation	**1,105,589**	**991,470**

Cash issued into circulation as at 31 December 2021 and 31 December 2020:

In millions of Mongolian Togrogs	Beginning balance	Increase	Decrease	Ending balance
Issued Banknotes	1,151,315	1,491,824	(1,526,169)	1,116,970
Uncounted banknotes	(159,867)	(1,365,176)	1,513,640	(11,403)
Issued Coins	22	-	-	22
Cash in circulation	**991,470**	**(518,008)**	**632,127**	**1,105,589**

Uncounted banknotes represent excess cash transferred from local banks for safeguarding purposes that are kept by the BOM and will be transferred back to respective local bank upon their request.

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20. CENTRAL BANK BILLS

In millions of Mongolian Togrogs	31 December 2021	31 December 2020
Central Bank bills issued	8,622,184	7,952,438
Total Central Bank bills	**8,622,184**	**7,952,438**

Central bank bills are bills issued by the BOM, which are issued to local banks. Such bills have maturities of 28 days (2020: 7 days to 184 days) and bear interest rates ranging from 6% per annum as at 31 December 2021 (2020: 7% to 11% per annum).

21. LIABILITIES DUE TO GOVERNMENT ORGANIZATIONS

In millions of Mongolian Togrogs	31 December 2021	31 December 2020
Current accounts of Ministry of Finance	1,079,704	1,452,764
Liabilities to the Ministry of Finance related to borrowings:		
- International Monetary Fund (IMF)	618,751	646,516
- Asian Development Bank (ADB)	32,267	27,936
- International Development Association (IDA)	3,394	4,809
Total liabilities due to government organizations	**1,734,116**	**2,132,025**

Current accounts of Ministry of Finance. This relates to various current accounts that the Ministry of Finance maintains with the BOM. These current accounts are on demand and do not bear any interest except for one account which bears an interest of 2.5% per annum as at 31 December 2021 (2020: 3.5% per annum).

Liabilities due to the Ministry of Finance related to borrowings from international organizations. These liabilities relate to the borrowing agreements signed by the Government of Mongolia with IMF, Asian Development Bank (ADB), and International Development Association (IDA). The Ministry of Finance of Mongolia (MOF) acts as the fiscal agent with regard to these agreements, while the BOM acts as the project executing agency.

International Monetary Fund (IMF). The Executive Board of the IMF approved a three-year extended arrangement under Extended Fund Facility (EFF) for Mongolia in a total amount of SDR 315 million to support the country's economic reform program on 24 May 2017. The EFF arrangement represent loans granted to Government of Mongolia by IMF under the EFF and bear interest ranging from 1.53% p.a. to 1.59% p.a.

The funding was further transferred to the Bank according to memorandum of understanding between BOM and Ministry of Finance of Mongolia (MOF) dated 25 May 2017. These loans represent obligation of the Ministry of Finance. Given that the Ministry of Finance acts as a fiscal agent of Mongolia, it has signed promissory notes issued to IMF in respect of repayments of loans granted by IMF under EFF arrangement, the Ministry of Finance has the obligation toward IMF with regard to these loans granted by IMF.

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21. LIABILITIES DUE TO GOVERNMENT SECURITIES (CONTINUED)

The loans and repayments are denominated in Special Drawing Rights ("SDR") and the repayment is done by the BOM on behalf of MOF to IMF according to repayment schedule, which is expected to be paid within 2026. As at 31 December 2021, liabilities due to MOF under EFF arrangement were SDR 155.2 million, which is equivalent to MNT 618,751 million (2020: SDR 157.5 million, which is equivalent to MNT 646,516 million).

Asian Development Bank (ADB). The loans received from the ADB are mainly for purpose of reducing poverty in Mongolia by developing and promoting private enterprises and providing training and consultancy to the Government, non-government organizations and local banks. The loans bear interest of 1% and 2.5% per annum with maturity ranging from 17 to 27 years.

The Bank's obligations are to the Ministry of Finance of Mongolia and it has no direct obligations toward IMF and ADB, as the MOF acts as the fiscal agent of the Government of Mongolia. However, the Bank, as project executing agency, is responsible for channelling funds to the local banks, which further channelled the funds to final customers (borrowers) who meet criteria specified by IMF and ADB.

Based on the arrangement between MOF and BOM, the BOM has borrowed related funds from MOF under the same conditions, as MOF has borrowed under the agreement with IMF and ADB. The BOM also acts as a depository, and it is responsible for settling payments from the accounts of the MOF with regards to IMF and ADB. Loans issued to local banks from these funds are disclosed in Note 9. For management's judgement related to these liabilities to MOF and loans to local banks, refer to Note 4.

International Development Association (IDA). Proceeds of the borrowings received by the MOF on behalf of the Government of Mongolia from International Development Association are for the private sector development project and the financial capacity development project and are lent by MOF with interest rates of 1% and 3% per annum with maturity ranging from 14 to 15 years.

There were no breaches of covenant as at 31 December 2021 and 31 December 2020.

22. DEPOSITS FROM LOCAL BANKS

In millions of Mongolian Togrogs	**31 December 2021**	**31 December 2020**
Correspondent accounts:		
- in foreign currency	2,148,313	2,316,318
- in national currency	1,817,495	1,249,089
Overnight deposits in national currency	506,069	106,515
Foreign currency time deposits	-	199,475
Total deposits from local banks	**4,471,877**	**3,871,397**

Correspondent accounts mainly consist of various deposit accounts and the obligatory reserves of local banks maintained with the Bank, calculated as a percentage of their eligible liabilities to deposit holders.

Overnight deposits in national currency as at 31 December 2021 represent MNT overnight deposits placed by local banks at an interest rate of 5% per annum with maturity of 3 days (2020: interest rate of 5% per annum with maturity of 4 days).

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23. LIABILITIES DUE TO FOREIGN PARTIES

In millions of Mongolian Togrogs	31 December 2021	31 December 2020
Financing from People's Bank of China	5,463,574	5,332,233
Financing from Cargill Financial Services International	570,417	-
Allocation of Special Drawing Rights of IMF	470,698	200,102
Financing from MUFG Bank Ltd	284,905	255,613
Financing from Bank of International Settlements	122,512	-
Current account of World Bank	1,620	1,281
Subscription to World Bank	179	179
Subscription to IDA	39	39
Current account of ADB	61	61
Total liabilities to foreign parties	**6,914,005**	**5,789,508**

Below table shows the movement of the liabilities due to foreign parties as at 31 December 2021 and 2020:

	Liabilities from financing activities	
In thousands of Mongolian Togrogs	31 December 2021	31 December 2020
Liabilities from financing activities at 1 January	**5,789,508**	**4,969,684**
Cash transactions:		
Cash inflows	2,237,184	284,364
Cash outflows	(1,231,344)	(45,766)
Interest paid	(263,496)	-
Non-cash transactions:		
Interest accrued	262,992	-
Foreign exchange adjustments	119,161	581,226
Liabilities from financing activities at 31 December	**6,914,005**	**5,789,508**

Financing from People's Bank of China. This balance represents 12 months (2020: 12 months) financing denominated in CNY from the People's Bank of China that was used by the BOM for CNY funding to local banks. Interest rate is based on SHIBOR+200 bps per annum.

Financing from Cargill Financial Services International. On 15 December 2021, Bank entered into gold purchase financing agreement with amount of USD 200 million with Cargill Financial Services International for a purpose to finance local gold companies and to increase the gold supply to the BOM. As at 31 December 2021, financing from Cargill Financial Services International liabilities was USD 200.12 million equivalent to MNT 570,417 million (2020: nil) with interest rate of LIBOR 3M plus margin of 2.75% per annum and maturity of 1 year.

23. LIABILITIES DUE TO FOREIGN PARTIES (CONTINUED)

Allocations of Special Drawing Rights. *("SDR")* IMF member countries are allocated SDR in proportion to their subscription to the IMF. The allocations represent a dormant liability of the Bank to the IMF, against which assets are received in the SDR Holdings account from the IMF as referred in Note 8. The net accumulation of the allocation was SDR 118,053 million equivalent to MNT 470,698 million as at 31 December 2021 (2020: SDR 48,757 million equivalent to MNT 200,102 million).

Loan from MUFG Bank Ltd. On 12 June 2020, the Bank entered into a facility agreement with MUFG Bank LTD as financier, coordinator bank and agent and Sumitomo Mitsui Banking Corporation, as financier to receive fund of JPY 10,800 million for a purpose to finance local gold companies and to increase the gold supply to the BOM where the gold will be refined at Samsung. The interest rate is LIBOR3MJPY plus 2.5% per annum. The shipment quantity per contract is designated to be higher than the quantity to close the principal repayment and the remaining will be deposited to the banks account. In circumstances, the Bank deficit the agreed quantity to be shipped, default interest is to be paid on each deficit ounce. The Bank fully repaid the loan by 31 December 2021 with 7 separate gold shipment to Samsung by using London Bullion Market fix price per ounce.

On 24 December 2021, the Bank entered into a facility agreement with MUFG Bank LTD to receive fund of USD 100 million for a purpose to finance local gold companies and to increase the gold supply to the BOM where the gold will be refined at Samsung. As at 31 December 2021, loan from the MUFG Bank LTD was USD 100.01 million equivalent to MNT 284,905 million with interest rate of 3.2% per annum and maturity of 1.6 year.

Financing from Bank of International Settlements ("BIS"). On 3 December 2021, the Bank entered into a financing agreement with the Bank of International Settlements in order to increase foreign currency reserve. According to the agreement, the Bank pledged BIS investments and obtained a financing of USD 43 million, which is aggregate amount of not exceeding 86% of market value of pledged assets. As at 31 December 2021, financing from the BIS was USD 43.01 million equivalent to MNT 122,513 million with interest rate of 1.05% per annum and maturity of 1 year. Refer to Note 10 for the details of the BIS investment.

Subscription to World Bank and IDA This balance represents the Bank's subscription obligation to World Band and IDA.

There were no breaches of covenant as at 31 December 2021 and 31 December 2020.

24. OTHER LIABILITIES

In millions of Mongolian Togrogs	**31 December 2021**	**31 December 2020**
Other financial liabilities		
Deposits by non-banking entities	505,468	324,941
Other payables	159,703	38,216
Other liabilities		
Social development fund	2,060	2,160
Total other liabilities	**667,231**	**365,317**

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24. OTHER LIABILITIES (CONTINUED)

Deposits non-banking entities. Deposits by non-banking entities relate to deposits from government organizations, Securities Clearing House Central Depository and Deposit Insurance Corporation.

Social development fund. Based on its internal regulations, the Bank allocates certain funds to the Social development fund, which is used for improving living and working conditions of the Bank's employees. These funds are used for payment of benefits, reimbursements, work performance remunerations of the Bank's employees, purchasing apartments to guarantee social welfare of employees and to help employees in need etc. Management believes that allocated funds in social development fund are sufficient as at financial year-end to cover outstanding obligations.

25. CHARTER CAPITAL AND OTHER RESERVES

In millions of Mongolian Togrogs	**31 December 2021**	**31 December 2020**
Charter capital	60,000	60,000

Other reserves comprise the following:

In millions of Mongolian Togrogs	**Revaluation reserve for investment securities at FVOCI**	**Revaluation reserve for Premises and Equipment**	**Revaluation reserve for gold bullion and foreign exchange**	**Revaluation reserve for Treasury Fund**	**Total**
At 1 January 2020	**74,792**	**30,331**	**572,739**	**1,061,764**	**1,739,626**
Gain on fair value changes of investments in debt securities at FVOCI	91,685	-	-	-	**91,685**
ECL movement as part of FV change	3,976	-	-	-	**3,976**
Transfer to profit or loss upon disposal	(3,262)	-	-	-	**(3,262)**
Transfer from/(to) accumulated deficit to other reserves	(4,624)	-	130,681	-	**126,057**
At 31 December 2020	**162,567**	**30,331**	**703,420**	**1,061,764**	**1,958,082**
Loss on fair value changes of investments in debt securities at FVOCI	(25,570)	-	-	-	**(25,570)**
ECL movement as part of FV change	5,534	-	-	-	**5,534**
Transfer to profit or loss upon disposal	1,335	-	-	-	**1,335**
Transfer from/(to) accumulated deficit to other reserves	-	-	(12,432)	-	**(12,432)**
At 31 December 2021	**143,866**	**30,331**	**690,988**	**1,061,764**	**1,926,949**

25. CHARTER CAPITAL AND OTHER RESERVES (CONTINUED)

Revaluation reserve for investment securities at FVOCI. This reserve comprises changes in fair value of investment securities at FVOCI. The ECL movement compromises ECL of government securities at FVOCI and investment in debt securities at FVOCI. During the year ended 31 December 2020, fair value reserve of MIK shares amounting to MNT 4,624 million were transferred to the accumulated deficit upon disposal of the investment.

Revaluation Reserve for Premises and Equipment. The revaluation reserve is used to record the surplus arising from the revaluation of the Bank's building. Refer to Note 18 for more information.

Revaluation Reserve for Gold Bullion and Foreign exchange. Revaluation reserve is used to record the number of unrealized gains or losses arising from fair value changes of gold bullion and foreign currency translation of monetary assets and liabilities denominated in foreign currency.

Revaluation Reserve for Treasury Fund. The revaluation reserve is used to record the surplus arising from the revaluation of the Treasury Fund. Refer to Notes 4 for more information.

26. INTEREST INCOME AND EXPENSE

In millions of Mongolian Togrogs	**2021**	**2020**
Interest income calculated using the effective interest method		
Debt securities at AC	159,487	129,420
Reverse repurchase agreement at AC	52,854	19,041
Debt securities at FVTOCI	25,263	32,141
Due from foreign financial institutions at AC	18,690	27,474
Loans to local banks at AC	15,006	13,063
Government securities at FVOCI	14,928	13,223
Total interest income calculated using the effective interest method	**286,228**	**234,362**
Other similar income		
Other assets at FVTPL	22,165	42,810
Total other similar income	**22,165**	**42,810**
Total interest income	**308,393**	**277,172**
Interest expense		
Central bank bills	(532,079)	(465,875)
Liabilities due to foreign parties	(262,992)	(253,217)
Liabilities due to government organization	(36,384)	(27,297)
Fulfilment on mandatory reserve requirement to local banks	(23,954)	(52,378)
Deposits from local banks	(9,367)	(15,377)
Other interest expense	(21,486)	(2,267)
Total interest expense	(886,262)	(816,411)
Net interest expense	**(577,869)**	**(539,240)**

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27. LOSSES/(GAINS) FROM TRADING IN GOLD BULLION AND PRECIOUS METALS

In millions of Mongolian Togrogs	2021	2020
Losses on trading of gold bullion and precious metals	(1,559)	(7,099)
Realized (losses)/ gains from disposal of gold bullion and precious metals	(6,018)	695,442
(Losses)/gains from refining of gold bullion and precious metals	(60,961)	39,971
(Losses)/Gains from trading in gold bullion and precious metals	**(68,539)**	**728,315**

28. OTHER OPERATING INCOME

In millions of Mongolian Togrogs	2021	2020
Commission income	22,536	17,472
Penalty income from local banks	4,231	9,917
Rental income from property and equipment	666	575
Other operating income	1,935	1,659
Total other operating income	**29,368**	**29,623**

The Bank obtains mandatory reserves from local banks as a regulatory body of the banking sector in accordance with the requirements of the Bank. The balances are set at percentages based on a 14-day period. (Refer to Note 22). As at 31 December 2021, penalty income received from the mandatory reserve held with the local banks was MNT 4,231 million (2020: MNT 9,917 million).

Commission income comprises from commissions on interbank transactions with high and low amounts, cards, and foreign currency transactions. Other operating income includes income from banknotes and coin sales.

29. ADMINISTRATIVE AND OTHER OPERATING EXPENSES

In millions of Mongolian Togrogs	2021	2020
Staff cost	25,472	23,310
Cost of printing banknotes	9,928	15,549
Depreciation and amortisation of premises, equipment, and intangible assets	7,568	6,090
Gold transportation and shipping expense	5,434	2,596
Facility and arrangement fees	3,275	5,501
Telecommunication and utility expense	2,366	2,034
Security expense	1,766	1,657
Loss on fixed asset disposal	1,217	5
System repair fees	884	1,008
Membership and professional fees	783	787
Fixed asset repair and maintenance fee	756	684
Advertisement expenses	690	864
Transportation and trip expenses	565	629
Training expenses	112	209
Legal and professional fees	-	56
Other expenses	5,201	4,485
Total administrative and other operating expenses	**66,017**	**65,464**

30. CONTINGENCIES AND COMMITMENTS

Legal proceedings. Management is not aware of any legal proceedings as at 31 December 2021 and 31 December 2020, in which the Bank acts as defendant and which could result in material losses to the Bank. Thus, management believes that no provision is necessary in these financial statements.

Credit related commitments. The Bank enters into certain credit related commitments, which are deemed to be of importance for the country (e.g. exporting goods and/or services) and/or when such arrangements are requested by the Government of Mongolia or its institutions. The primary purpose of these instruments is to ensure that funds are available to the Government or other relevant parties in these arrangements as required.

Issued letters of credit represent unused portions of authorizations to extend credit in the form of loans or letters of credit, refer to information below. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss in an amount equal to the total unused commitments.

However, the likely amount of loss is less than the total unused commitments due to low counterparty risk, as outlined below.

In millions of Mongolian Togrogs	**31 December 2021**	**31 December 2020**
Contingent Liabilities		
Import letters of credit	22,475	35,898
Commitments		
Undrawn credit line of People's Bank of China	6,000,000	6,000,000
Total credit related commitments	**6,022,475**	**6,035,898**

An analysis of credit related commitments by credit quality based on credit risk grades at 31 December 2021 is as follows.

In millions of Mongolian Togrogs	**31 December 2021 Stage 1 (12-months ECL)**	**31 December 2020 Stage 1 (12-months ECL)**
Import letters of credit		
- Satisfactory	22,475	35,898
Unrecognised gross amount	**22,475**	**35,898**
Commitments		
- Excellent	6,000,000	6,000,000
Unrecognised gross amount	**6,000,000**	**6,000,000**

30. CONTINGENCIES AND COMMITMENTS (CONTINUED)

For the purpose of ECL measurement, contingent liabilities and commitment balances are included in Stage 1. The ECL for these balances represents an insignificant amount, therefore the Bank did not recognise any credit loss allowance for contingencies and commitments as at 31 December 2021 and 31 December 2020.

Import letters of credit. Import letters of credit are mainly issued to the Government of Mongolia with regard to import arrangements. Through issued letters of credit, the Bank is obliged to make payment on behalf of the Government or its institutions to foreign legal entities, which provided services or delivered goods to the Government, its institutions, or other entities at the Government's request.

SWAP Agreement with People's Bank of China. **T**he Bank entered into "Chinese Yuan/Mongolian Togrogs Bilateral Currency Swap Arrangement" with the People's Bank of China (PBC) in May 2011. The agreement was renewed in August 2014, July 2017, and July 2020. Central banks can use this money for financing trade between the two countries, for providing short-term liquidity for stabilisation of financial markets, and for other purposes agreed upon by both parties.

Based on the agreement, the PBC and the Bank may, from time to time, conduct transactions involving the purchase and sale, and subsequent repurchase and resale, of CNY (Chinese Yuan) against MNT and of MNT against CNY. According to the agreement, the period of use of funds (i.e. usage period) can be up to twelve months. Each usage is made upon the request of one bank and approval of another bank. The maximum amounts requested for use are limited to the open limit of CNY 15,000 million (2020: CNY 15,000 million) when the BOM is the requesting party and MNT 6,000,000 million (2020: MNT 6,000,000 million) when PBC is the requesting party.

The bank using funds is obliged to pay interest for the used amount on the date of repayment at interest rates specified in the agreement. In the case of the BOM requesting to use CNY, the interest rate is equivalent to 200 basis points plus the Shanghai Interbank Offered Rate (SHIBOR) for CNY deposits with corresponding usage period. In the case of PBC requests for use of MNT, the interest rate is equivalent to the Interbank MNT Weighted Rate with corresponding usage period.

As at 31 December 2021, the Bank has used amount of CNY 12,000 million equal to MNT 5,365,800 million (2020: CNY 12,000 million equal to MNT 5,233,560 million) and the unused amount of CNY 3,000 million equivalent to MNT 1,341,450 million (2020: CNY 3,000 million equivalent to MNT 1,308,390 million).

The Bank's management believes that fair value of letters of credit and credit line commitments are not material. The total outstanding contractual amount of undrawn credit lines and letters of credit does not necessarily represent future cash requirements, as these financial instruments may expire or terminate without being funded. ECL measurement was assessed using the credit conversion factor and ECL for these balances represent an insignificant amount. Therefore, the Bank did not recognise any credit loss allowance for these credit commitments.

Capital commitment. At 31 December 2021, the Bank had commitments of MNT 2,029 million (2020: MNT 2,388 million) relating to the main completion of purchase of new database infrastructure.

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31. RELATED PARTY TRANSACTIONS

Parties are generally considered to be related if the parties are under common control, or one party has the ability to control the other party or can exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

As at 31 December 2021 and 31 December 2020, the Bank has disclosed balances and transactions with the following related parties:

- Government which includes organizations, such as Ministry of Finance, which management is appointed by the Government of Mongolia.
- A local bank State Bank, which is fully owned by Ministry of Finance and management appointed by the Parliament.
- Development Bank of Mongolia, which is owned by Government of Mongolia and the management is appointed by the government; and
- DICOM, which is fully owned by the government and all decisions concerning the activities of DICOM must be approved by vote from each of the seven members of the National Committee chaired by the First Deputy Governor of BOM. Refer to Note 4 for the management judgement of control over Deposit Insurance Corporation (DICOM).
- Erdenes Mongol LLC which is 100% owned by Government.
- Erdenes Tavan Tolgoi LC which is 81.5% owned by Erdenes Mongol LLC; and
- City Housing Corporation (“NOSK”) JSC which is 100% owned by Government.

The Bank utilized the exemption in IAS 24 from the disclosure requirement for government-related entities. Thus, individually immaterial transactions with government-related entities are not disclosed in these financial statements.

The income and expense items with related parties for 2021 were as follows:

In millions of Mongolian Togrogs	**Government**	**State Bank**	**Development Bank of Mongolia**	**DICOM**	**Erdenes Mongol LLC**	**Erdenes Tavan Tolgoi LC**	**City Housing Corporation JSC**	**Total**
Interest income	14,928	1,070	6,744	320	44,036	15,716	5,054	**87,868**
Interest expense	(36,384)	(64,149)	(5,541)	(11,695)	-	-	-	**(117,769)**
Commission income	1,253	182	-	-	-	-	-	**1,435**
Total	**(20,203)**	**(62,897)**	**1,203**	**(11,375)**	**44,036**	**15,716**	**5,054**	**(28,466)**

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31. RELATED PARTY TRANSACTIONS (CONTINUED)

At 31 December 2021, the outstanding balances after ECL with related parties were as follows:

In millions of Mongolian Togrogs	Government	State Bank	Development Bank of Mongolia	DICOM	Erdenes Mongol LLC	Erdenes Tavan Tolgoi LC	City Housing Corporation JSC	Total
Government securities	231,778	-	-	-	-	-	-	**231,778**
Reverse repurchases agreements	-	87,863	-	-	-	-	-	**87,863**
Loans to local banks	-	83,330	-	-	-	-	-	**83,330**
Loans to non-financial entities	-	-	-	57,576	-	-	-	**57,576**
Erdenes bonds	-	-	-	-	715,209	-	-	**715,209**
Erdenes Tavan Tolgoi bonds	-	-	-	-	-	297,659	-	**297,659**
Lease backed bonds	-	-	-	-	-	-	100,487	**100,487**
Financial derivatives	-	(2,857)	(131,191)	-	-	-	-	**(134,048)**
Central bank bills	-	(855,367)	-	-	-	-	-	**(855,367)**
Deposits from local banks	-	(200,562)	(263,639)	-	-	-	-	**(464,201)**
Deposits from non-financial entities	-	-	-	(495,649)	-	-	-	**(495,649)**
Liabilities due to the government organisations	(1,734,116)	-	-	-	-	-	-	**(1,734,116)**
Other payables	(10,725)	-	-	-	-	-	-	**(10,725)**
Total	**(1,513,063)**	**(887,593)**	**(394,830)**	**(438,073)**	**715,209**	**297,659**	**100,487**	**(2,120,204)**

The income and expense items with related parties for 2020 were as follows:

In millions of Mongolian Togrogs	Government	State Bank	Development Bank of Mongolia	DICOM	Erdenes Mongol LLC	City Housing Corporation JSC	Total
Interest income	13,223	4,135	90,512	321	11,743	339	**120,273**
Interest expense	(27,297)	(62,723)	(73,334)	(31,326)	-	-	**(194,680)**
Commission income	73	2,128	-	-	-	-	**2,201**
Total	**(14,001)**	**(56,460)**	**17,178**	**(31,005)**	**11,743**	**339**	**(72,206)**

31. RELATED PARTY TRANSACTIONS (CONTINUED)

At 31 December 2020, the outstanding balances after ECL with related parties were as follows:

In millions of Mongolian Togrogs	Government	State Bank	Development Bank of Mongolia	DICOM	Erdenes Mongol LLC	City Housing Corporation JSC	Total
Government securities	227,408	-	-	-	-	-	**227,408**
Reverse repurchases agreements	-	5,028	-	-	-	-	**5,028**
Loans to local banks	-	38,158	-	-	-	-	**38,158**
Loans to non-financial entities	-	-	-	54,230	-	-	**54,230**
Development Bank securities	-	-	55,650	-	-	-	**55,650**
Erdenes bonds	-	-	-	-	515,811	-	**515,811**
Lease backed bonds	-	-	-	-	-	34,096	**34,096**
Financial derivatives	-	(710)	(52,435)	-	-	-	**(53,145)**
Central bank bills	-	(921,758)	(98,936)	(169,453)	-	-	**(1,190,147)**
Deposit from local banks	-	(184,959)	(40,874)	-	-	-	**(225,833)**
Non-financial institution assets	-	-	-	(320,436)	-	-	**(320,436)**
Liabilities due to government organizations	(2,132,025)	-	-	-	-	-	**(2,132,025)**
Other payables	(6,410)	-	-	-	-	-	**(6,410)**
Total	**(1,911,027)**	**(1,064,241)**	**(136,595)**	**(435,659)**	**515,811**	**34,096**	**(2,997,615)**

The transactions with related parties arose from the ordinary course of the Bank's operation. Management considers whether gains/losses should arise on initial recognition of transactions with related parties. In making this judgement, management also considers these transactions as a principal market segment. Refer to Notes 4 for details.

Outstanding balances to related parties at year-end are unsecured except reverse repurchases agreements, Erdenes bonds, and Lease backed bonds. There have been no guarantees provided or received for any related party receivables and payables.

Import Letter of Credit Commitments. As at 31 December 2021, the Bank has MNT 22,475 million (2020: MNT 35,898 million) of import letter of credits commitments to related parties. Refer to Note 30 for more information.

Key management compensation is presented below:

In millions of Mongolian Togrogs	2021	2020
Salary and wages	764	1,406
Social and pension fund contribution	113	207
Benefits in-kind	110	249
Other compensation	5	189
Total	**992**	**2,051**

32. FINANCIAL RISK MANAGEMENT

Risk is inherent in the Bank's activity; however, it is managed through a process of ongoing identification, measurement, and monitoring, subject to risk limits and other controls. This process of risk management is critical to the Bank's management to pursue its monetary policy (including control of inflation), financial stability and business continuity of Mongolian banking operations. At certain times, the Bank may be overly exposed to certain risks and/or take disadvantageous positions of fulfilling its primary objectives and responsibilities, which are typical for central banks and consequently the Bank may incur unexpected financial losses, e.g. losses from translation of foreign currency balances. Such financial losses could be incurred with regard to all financial risks.

From the financial point of view, the Bank is exposed to credit risk, liquidity risk and market risk. In addition, it is also subject to operational, reputation and legal risks. Currently, the Bank has a decentralized risk management process. Each department is responsible for the independent control of risks, including monitoring the risk of exposures against their activities. Those risks, which are unique to the Bank as the central bank of Mongolia, are monitored through the Bank's strategic planning process. In addition, the Bank actively explores the possibility of setting up a Risk Committee. Committee, which would have the overall responsivity for the development of the risk strategy, and implementing principles, frameworks, policies, and limits, as well as for making relevant decisions related to monitoring and managing risks.

At present, the Investment Committee is responsible for development of risk strategy and making decisions on relevant limits, while the Risk Management Unit and Reserve Management Financial Markets Department are in charge of implementing principles, frameworks, policies, and limits.

Risk Management Structure. The Board of Directors is ultimately responsible for identifying and controlling risks; however, there are separate independent bodies responsible for managing and monitoring risks.

Board of Directors. The Board of Directors is responsible for the overall risk management approach. Further, it provides recommendations on risk management related issues to the Governor and the First Deputy Governor of the Bank.

Supervisory Board. The Supervisory Board has been established outside of the Bank's internal organization in order to maintain an external supervisory role and has the responsibility to monitor the overall risk process within the Bank.

Investment Committee. The Investment Committee is a key body responsible for risk management in the Bank. As such, the Committee is responsible for offering recommendations on the area of risk management policy to the Governor and the Board of Directors. It consists of the First Deputy Governor, Deputy Governor, Director of Risk Management Unit, Director of Reserve Management Financial Markets Department and Director of Financial Reporting and Accounting Department.

The Investment Committee issues the "Annual Investment Policy" and determines acceptable levels of risk. Based on the acceptable risk, the Investment Committee proposes the structure of the international reserve for the Governor's approval. The Committee's proposal defines the currency composition of international reserves and its acceptable variation, asset allocation and its acceptable variance, duration of investments, eligible instruments, counterparties, and the counterparty limits. Limits over the foreign currency reserve are approved by the Governor on a quarterly basis and represent the key method used in managing international risk, as well as credit risk, liquidity risk and interest rate risk.

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

The risks related to the Bank's foreign currency assets (reserves) are a key area of focus, given the proportion of international reserves in the Bank's total assets. Thus, the activities of the Investment Committees and departments involved in the risk management process are mainly focused on monitoring and managing risks related to international reserves. However, the Investment Committee is also responsible for monitoring the activities of the Risk Management Unit and other responsible departments, which address financial risks, related to the Bank's financial assets and liabilities, and overall compliance with the Bank's investment policy. The methods used in managing financial risks are further outlined below.

Risk management unit. The Risk Management Unit ("RMU") is responsible for implementing and maintaining international reserves and other risk related procedures to ensure an independent control process. RMU is responsible for monitoring compliance with strategic benchmark for international reserves, risk principles, policies and limits. In addition, RMU also ensures the complete capture of risk measures related to the international reserves and reporting system.

According to the Regulation on International Reserve Management, the objectives of reserve management are subordinated to the Bank's monetary and foreign exchange policies. The main objectives in holding foreign reserves are to:

- Support monetary policy.
- Manage excessive volatility of the foreign exchange market.
- Guarantee payment of government foreign exchange debt.
- Use as a liquidity buffer in the event of national disaster or emergency.

Risk management of international reserves contributes to these objectives by strategically managing and controlling the exposure to financial and operational risks. The Bank determines strategy for asset selection and allocation to control exposures to external risks. This involves establishing parameters for the currency holding and composition necessary to maintain the ready availability of convertible currencies, the permissible range of investment instruments that meet liquidity and security requirements, and duration requirements for limiting exposure to interest rate risk.

Reserve Management Financial Markets Department. Reserve Management Financial Markets Department is responsible for general implementation of the investment policy through its specific units. The Director of Reserve Management Financial Markets Department monitors and manages the general structure of the asset portfolio, including asset composition, instruments, counterparties, maturity, as well as limits over the international reserves.

Internal Audit Department. The Bank's internal control mission is to examine and evaluate the adequacy and effectiveness of the risk management system in its activities toward the accomplishment of the Bank's objectives, and fulfilment of policies and plans. Internal Audit Department ("IAD") charter determines its duties to examine the effectiveness of all levels of risk management in planning, organization, coordination and controlling the implementation of the policies and procedures adopted by the Bank, examining the compliance of operations and systems with laws, regulations as well as integrity, and security of financial and operational information. IAD carries out general risk assessment and further assessment focused on specific issues. General risk assessment is undertaken during the development of long-term and annual audit plans to ensure proper allocation of audit resources according to the degree of risk, while assessment focuses on issues at the specific level. IAD of the Bank has carried out activities in accordance with the audit program and annual audit plan for 2021.

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

Priorities for audits are determined by applying criteria, which reflect potential and actual degree of risk to which each area of operation is exposed. For these purposes certain criteria are developed and appropriate weights are assigned to each type of criteria in relation to the activities audited. The weighted scores are totalled for each operational area and the degree of risk is classified as high, medium and low accordingly.

The evaluation of internal control system is also a very important aspect of internal audit work. The evaluation is aimed at ensuring the existence of adequate procedures and competent performance, as well as reliability of financial reporting system and compliance of all activities with applicable laws and regulations. IAD reports about findings and its recommendations administratively to the Governor, and functionally to the Supervisory Board. After each assessment, IAD discusses the results with management of the Bank, as well as undertaking follow-up reviews on the actions taken by management.

Credit Risk. Credit risk is the risk that the Bank will incur a loss because its customers, clients or counterparties failed to discharge their contractual obligations. Exposure to credit risk results from the Bank's lending and other transactions with counterparties, which give rise to financial assets and off-balance sheet credit-related commitments.

The Bank's maximum exposure to credit risk is reflected in the carrying amounts of financial assets in the statement of financial position. For financial guarantees issued, undrawn credit lines and import letters of credit, the maximum exposure to credit risk is the amount of the commitment.

Credit risk management. Credit risk is managed and controlled through proper selection of investment assets, credit quality of investment assets and setting limits on the amount of investment per investment asset. Limits on the level of credit risk by type of investment and counterparty are approved regularly by management.

Such risks are monitored on a revolving basis and subject to an annual or more frequent review.

To minimize credit risk, international reserves are invested in securities issued by the "Aaa" to "Aa3"rated governments (or central banks), and "Aaa" rated international institutions and agencies. The credit risk on foreign currency deposits and money market instruments is limited by transacting with counterparties rated "A3" or above by internationally recognised rating agencies. The minimum rating is taken when a counterparty has ratings from more than one rating agency.

For domestic monetary policy operations, the Bank actively uses collateral to reduce its exposure to credit risk. According to the Regulation on Central Bank Refinancing, the main types of collateral used when financial instruments are issued to Mongolian local banks are as follows:

1. Central Bank bills.
2. Government securities.
3. Development Bank securities; and
4. Loans issued by financial institution

The eligible borrowing banks have to meet all prudential ratios set by the Bank. If the borrowing local bank breaches one of the prudential ratios, the Bank terminates the refinancing operation in order to limit total exposure to the borrowing bank.

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

Credit limits in respect to international reserves, all counterparties have credit limits, which are set taking into consideration their ratings, capital, and other factors. The credit limits are approved quarterly by the Governor and compliance with the limits is monitored daily by the Risk Management Unit. In order to monitor its credit risk, the Bank also monitors the aging of its financial assets, particularly loans to local banks and other financial assets (refer to Notes 9 and 17). Any significant exposures against counterparties with deteriorating creditworthiness are reported to and reviewed by the Board of Directors, which also makes decisions on necessary actions.

As disclosed in Note 30, the Bank enters into certain credit related commitments, which are deemed to be of importance for the country (e.g. exporting goods and/or services) and/or when such arrangements are requested by the Government of Mongolia or its institutions. The primary purpose of these instruments is to ensure that funds are available to the Government or other relevant parties in these arrangements as required. Issued letters of credit represent irrevocable assurances that the Bank will make payments in the event that the party requesting this arrangement cannot meet its obligations to third parties and expose the Bank to similar risks to loans, which are mitigated by the same control processes and policies. Commitments to extend credit represent unused portions of authorisations to extend credit and relate to the arrangement with the People's Bank of China (Note 30). Based on analysis performed, the management believes that counterparty risk in case of this arrangement is low.

The Bank's maximum exposure to credit risk is reflected in the carrying amounts of monetary financial assets in the statement of financial position. The credit risk for reserve repurchase agreement is mitigated by collateral as disclosed in Notes 12. For letters of credit and commitments to extend credit, the maximum exposure to credit risk is the amount of the commitment, see Note 30.

Impairment assessment

Expected credit loss (ECL) measurement. *ECL* is a probability-weighted estimate of the present value of future cash shortfalls (i.e., the weighted average of credit losses, with the respective risks of default occurring in a given time period used as weights). An ECL measurement is unbiased and is determined by evaluating a range of possible outcomes. ECL measurement is based on four components used by the Bank: Probability of Default ("PD"), Exposure at Default ("EAD"), Loss Given Default ("LGD") and Discount Rate.

EAD is an estimate of exposure at a future default date, considering expected changes in the exposure after the reporting period, including repayments of principal and interest, and expected drawdowns on committed facilities. The EAD on credit related commitments is estimated using Credit Conversion Factor ("CCF"). CCF is a coefficient that shows the probability of conversion of the committed amounts to an on-balance sheet exposure within a defined period. PD an estimate of the likelihood of default to occur over a given time period. LGD is an estimate of the loss arising on default. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, including from any collateral. It is usually expressed as a percentage of the EAD. The expected losses are discounted to present value at the end of the reporting period. The discount rate represents the effective interest rate ("EIR") for the financial instrument or an approximation thereof.

The ECLs that are estimated by management for the purposes of these financial statements are point-in-time estimates, rather than through-the-cycle estimates that are commonly used for regulatory purposes. The estimates consider *forward-looking information,* that is, ECLs reflect probability weighted development of key macroeconomic variables that have an impact on credit risk.

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

The ECL modelling does not differ for Purchased or Originated Credit Impaired ("POCI") financial assets, except that (a) gross carrying value and discount rate are based on cash flows that were recoverable at initial recognition of the asset, rather than based on contractual cash flows, and (b) the ECL is always a lifetime ECL. POCI assets are financial assets that are credit-impaired upon initial recognition, such as impaired loans acquired in a past business combination.

Definition of default, impaired and cure. The Bank considers exposure to be in default for ECL calculations in all cases when the borrower becomes 90 days past due on its contractual payments, or where the obligor is unlikely to repay the exposure fully without the Bank's realisation of collaterals.

As part of the qualitative assessment of whether an exposure is credit-impaired, the Bank also considers a variety of instances that may indicate unlikeliness to pay. When such events occur, the Bank carefully considers whether the event should result in treating the customer as defaulted and therefore assessed as Stage 3 for ECL calculations or whether Stage 2 is appropriate. Such events include:

- Internal rating of the borrower indicating default or near-default
- The borrower requesting emergency funding from the Bank
- Prudential ratio does not meet the requirements
- The borrower having past due liabilities to public creditors or employees
- The borrower is deceased
- A material decreases in the underlying collateral value where the recovery of the loan is expected from the sale of the collateral
- A material decreases in the borrower's turnover or the loss of a major customer
- A covenant breach not waived by the Bank
- The debtor (or any legal entity within the debtor's group) filing for bankruptcy application/protection
- Debtor's listed debt or equity suspended at the primary exchange because of rumours or facts about financial difficulties

It is the Bank's policy to consider a financial instrument as 'cured' and therefore re-classified out of Stage 3 when none of the default criteria have been present for at least six consecutive months. The decision whether to classify an asset as Stage 2 or Stage 1 once cured depends on the updated credit grade, at the time of the cure, and whether this indicates there has been a significant increase in credit risk compared to initial recognition.

Credit risk grading system. For measuring credit risk and grading financial instruments by the amount of credit risk, the Bank applies risk grades estimated by external international rating agencies (Moody's, Standard & Poor's - "S&P", Fitch). The Bank has fully suspended trading with certain parties without considering their ratings due to instability of international financial markets, which could lead to a system risk, if counterparty risk is not properly addressed.

External credit ratings are mapped on master scale with a specified range of probabilities of default as disclosed in the table below:

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

Master scale credit risk grade	Corresponding ratings of external international rating agencies S&P	Moody's
Excellent	AAA to A-	AAA to A3
Good	BBB + to B -	Baa1 to B3
Satisfactory	CCC + to CCC -	Caa1 to Caa3
Special monitoring	CC to C	Ca to C
Default	Default	Default

Each master scale credit risk grade is assigned a specific degree of creditworthiness:

- *Excellent* – strong credit quality with low expected credit risk.
- *Good* – adequate credit quality with a moderate credit risk.
- *Satisfactory* – moderate credit quality with a satisfactory credit risk.
- *Special monitoring* – facilities that require closer monitoring and remedial management; and
- *Default* – facilities in which a default has occurred.

Given that the biggest Mongolian local banks are rated by international rating agencies, financial assets due from local banks are also monitored on this basis. In case of unrated Mongolian local bank, the Bank references the credit rating of the similar sized local banks and considers financial conditions of related local bank based on the recent financial information, compliance with prudential ratios, and other information available by the Supervision Department and other relevant departments for assessing credit quality of related assets and benchmark proxies of comparable banks.

Definition of default and determination of staging The Bank defines default as a situation when the exposure meets one or more of the following criteria:

- the borrower is more than 90 days past due on its contractual payments.
- local banks' prudential ratios greater than the Bank's requirement.
- financial asset's loan to value ratio greater than 100%.
- the Altman Z-score for local banks and companies (Emerging markets) fall below 1.1 and 1.8 respectively.
- the borrower meets the unlikeliness-to-pay criteria listed below:
  - a missed or delayed disbursement of a contractually obligated interest or principal payment
  - a bankruptcy filing or legal receivership by the debt issuer or obligor that will likely cause a miss or delay in future contractually obligated debt service payments.
  - a distressed exchange whereby.
  - a change in the payment terms of a credit agreement or indenture imposed by the sovereign that results in a diminished financial obligation, such as a forced currency re-denomination (imposed by the debtor, or the debtor's sovereign) or a forced change in some other aspect of the original promise, such as indexation or maturity.

BANK OF MONGOLIA

NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

The Bank's management sets following criteria for determination of Stage of financial assets:

No.	Criteria	Stage 1	Stage 2	Stage 3
1	Past due days of contractual payment	Less than 30 days	30-90 days	More than 90 days
2	Prudential ratio analysis for local banks	satisfies minimum requirement set by the Bank	doesn't satisfy minimum requirement set by the Bank	Default/ bankrupted
3	Altman Z-score for local banks and companies	Banks: Z-score > 2.6 Companies: Z-score > 3	Banks: 1.1 <Z-score>2.6 Companies: 1.8<Z-score>3	Banks: Z-score < 1.1 Companies: Z-score < 1.8
4	Loan to value ratio (LTV)	Less than 70%	70%-100%	Greater 100%

In addition to the above criteria, the Bank monitors recent changes in the external rating of banks and companies. Staging of financial assets reflects the upgrade or downgrade of the credit rating estimated by the external international rating agencies.

Exposure at default. The exposure at default (EAD) represents the gross carrying amount of the financial instruments subject to the impairment calculation, addressing both the client's ability to increase its exposure while approaching default and potential early repayments too.

To calculate the EAD for a Stage 1 loan, the Bank assesses the possible default events within 12 months for the calculation of the 12mECL. For Stage 2 and Stage 3 financial assets, the exposure at default is considered for events over the lifetime of the instruments.

Loss given default. Loss given default (LGD) values are assessed annually by the Risk Management Unit. LGD represents the Bank's expectation of the extent of loss on defaulted exposure. LGD varies by type of counterparty, type and seniority of claim and availability of collateral or other credit support. LGD is expressed as a percentage loss per unit of exposures at the time of default. LGD is calculated on a 12-month or lifetime basis, where 12-month LGD is the percentage of loss expected to be made if the default occurs in the next 12 months and Lifetime LGD is the percentage of loss expected to be made if the default occurs over the remaining expected lifetime of the loan.

In the absence of collateral for the financial instrument and sufficient historical data on default, the Bank applies expert judgement.

The Bank continuously monitors all assets subject to ECL. In order to determine whether an instrument or a portfolio of instruments is subject to 12m ECL or LTECL, the Bank assesses whether there has been a significant increase in credit risk since initial recognition.

LGD is calculated by choosing appropriate methods shown below based on availability of quantitative data on loss:

- If there is sufficient information about loss to establish an internal model to estimate future loss using a simulation method by developing an internal model when there is sufficient quantitative data on macroeconomics, particular sector and losses.
- If there is a certain amount of information about the losses: to estimate future loss using a simulation method and portfolio method, which is to estimate the same loss rate for the collateralized and uncollateralized exposures.
- If there is lack of or missing information about the loss: to use loss rate information of similar financial assets or to use parameters established by the foreign regulatory body.

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

The Bank applies the recovery rates of corporate entities applicable to each rating and time to maturity generated from Thomson Reuters data terminal for its LGD due to the limited historical data.

The following table shows LGD determined for each financial asset class in 2021 and 2020:

	Due from financial institution Note (8)	Investment in debt securities Note (10)	Reverse repurchases agreements Note (12)	Government securities Note (16)	Loan to local banks Note (9)	Other financial assets Note (17)
2021	60%	18% - 77%	0%	64%	0% - 77.2%	64% - 100%
2020	60%	47% - 63%	0% - 60%	63%	63%	72%

Significant increase in credit risk (SICR). The Bank continuously monitors all assets subject to ECL. In order to determine whether an instrument or a portfolio of instruments is subject to 12mECL or LTECL, the Bank assesses whether there has been a significant increase in credit risk since initial recognition.

The Bank applies a qualitative method for triggering a significant increase in credit risk for an asset, such as the account becoming forborne. In certain cases, the Bank may also consider that events explained in “Definition of default” are a significant increase in credit risk as opposed to a default.

When estimating ECLs on a collective basis for a group of similar assets, the Bank applies the same principles for assessing whether there has been a significant increase in credit risk since initial recognition.

Analysis of inputs to ECL model – forward looking information The Bank has incorporated the effect of future macroeconomic developments into the ECL by applying forward looking information on the component of the ECL, the PD. The Bank calculates the PD for the allowance for ECL either on a collective or an individual basis based on the nature of the financial assets. In terms of the methodology, correlation analysis was conducted initially to preselect the suitable macroeconomic variables. Then coefficients were estimated applying simple regression analysis. From the estimated coefficients and forecasts, adjustment factors to incorporate forward-looking information into PD were derived as the ratio between the predicted default rate and historical average default rate. Below is the PD base and forward-looking variables the Bank used for the calculation. The Bank uses the historical default rates published by international rating agencies (Moody’s and S&P) and macroeconomic factors to come up with a forward-looking probability weighted PD:

- Due from local banks

The Bank uses the historical speculative grade default rates of published by international rating agency (S&P) and macroeconomic factors to come up with a forward-looking probability weighted PD:

- Annual GDP.
- Inflation rate lagged by one (1) year.
- Loan interest rate; lagged by one (1) year.
- Unemployment rate

The Bank has run a linear regression analysis on the annual PD for the last 20 years against those macro-economic variables which are considered as the statistically significant macroeconomic factors.

- Secured loans to local banks

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

The Bank uses the historical weakest link default rates published by international rating agency (S&P) and macroeconomic factors to come up with a forward-looking probability weighted PD:

- Annual GDP.
- Inflation rate lagged by one (1) year.

The Bank has run a linear regression analysis on the annual PD for the last 21 years against those macro-economic variables which are considered as the statistically significant macroeconomic factors.

- Residential mortgage-backed securities and Lease backed bonds

The Bank uses the historical weight of non-performing mortgage loan published by BoM and macroeconomic factors to come up with a forward-looking probability weighted PD:

- Quarterly GDP.
- Non-performing loan %, lagged by one (1) quarter.
- Unemployment rate

The Bank has run a linear regression analysis on the quarterly non-performing mortgage loan % (PD) for the last 10 years against those macro-economic variables which are considered as the statistically significant macroeconomic factors.

- Erdenes Mongol Bond

The Bank uses the historical weight of non-performing loan of mining sector published by BoM and macroeconomic factors to come up with a forward-looking probability weighted PD:

- Quarterly GDP lagged by two (2) quarter.
- Non-performing loan %, lagged by one (1) quarter

The Bank has run a linear regression analysis on the quarterly non-performing mining sector loan % (PD) for the last 10 years against those macro-economic variables which are considered as the statistically significant macroeconomic factors.

These adjustment factors and adjusted PD rates are considered as Base scenario for ECL model, as it represents the best prediction of the future economic development. The best and worst scenarios are derived from historical adjustment factors based on the model predicted default rates and selected as certain quantiles of the adjustment factor distribution.

Expected loss for different scenarios are calculated based on those estimated PD rates under the different scenarios, and the actual expected credit loss allowance is estimated as weights of 3 scenarios: 5% for Best and Worst case, and 90% for Base case scenario.

The following table below shows the value of the key forward looking macroeconomic assumptions used in each of the scenarios for the ECL calculations. Other variables were lagging variables and thus used actual statistics.

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

		31 December 2021		31 December 2020	
Key drivers	ECL scenario	Assigned weightings	Assumption for 2022	Assigned weightings	Assumption for 2021
	Best case	5%	14.40%	30%	8.30%
GDP growth %	Base case	90%	5.50%	40%	6.40%
	Worst case	5%	(2.60%)	30%	4.50%
	Best case	5%	(0.50%)	not applied	-
Inflation %	Base case	90%	6.70%	not applied	-
	Worst case	5%	14.40%	not applied	-
Unemployment rate	All case	100%	8.30%	100%	10.80%

The following table shows that PD base for each financial asset which are not based on counterparty's credit ratings:

Financial assets	PD Base
Loans to local banks	S&P default rate
Reverse repurchase agreement with local banks	S&P default rate
Investment in debt securities	
Senior RMBS bonds	NPL % of Mortgage loan
Lease backed bonds	NPL % of Residential loan
Erdenes bonds	NPL % of Mining loan
Erdenes Tavan Tolgoi bonds	NPL % of Mining loan

The multiplier as shown in the table below represents the forward-looking adjustment which is reflected into PD base with consideration of macro-economic variables into ECL model. The multiplier is estimated based on the regression of annual historical PD with the reference of above-mentioned macroeconomic variables. The following table below shows that multipliers and each assigned PDs used in the ECL model:

Scenario	Weight	Loans to local banks		Senior RMBS bonds		Lease backed bonds		Erdenes bonds and Erdenes Tavan Tolgoi Bonds	
		Multiplier	PD	Multiplier	PD	Multiplier	PD	Multiplier	PD
Best	5%	0.12	0.43%	0.73	0.85%	0.73	4.61%	1.08	15.57%
Base	90%	0.82	2.90%	0.83	0.97%	0.83	5.26%	1.14	16.42%
Worst	5%	1.04	3.67%	0.93	1.09%	0.93	5.87%	1.2	17.21%

In terms of financial assets held with foreign institutions, including Due from foreign institutions and Investment in debt securities from foreign banks, the management assumed that forward-looking information is implied in the credit rating of the counterparty based on Probability of Default Implied Rating Research on Bloomberg terminal. Accordingly, credit allowance for the next 12 months was estimated by providing default rates on each scenario by using the same weights as above-mentioned financial assets.

Market risk. Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates or foreign exchange rates. When assessing market risk, as well as liquidity risk, management's main considerations also include intervention needs, structure of the import and current liabilities to foreign parties. The Bank manages and monitors this risk element using sensitivity analyses. Except for the concentrations within foreign currencies, the Bank has no significant concentration of market risk. The Bank is not significantly exposed to other price risk.

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

Currency risk. Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. Currency risk is managed through diversification of foreign currency portfolio and determination of the below parameters:

- international reserve management.
- maximum share of the managed currency in related assets denominated in foreign currencies for foreign currency reserve and short-term and long-term investment portfolio.

The currency composition of the international reserves is approved by the Investment Committee on an annual basis.

The following table presents sensitivities of profit or loss and equity to reasonably possible changes in exchange rates of foreign currencies and SDRs applied at the end of the reporting period relative to the functional currency of the Bank, with all other variables held constant. A negative amount in the table reflects a potential net reduction in profit or loss while a positive amount reflects a net potential increase.

In millions of Mongolian Togrogs	**At 31 December 2021 Impact on profit or loss and equity**	**At 31 December 2020 Impact on profit or loss and equity**
USD strengthening by 10% (2020: 10%)	455,422	635,845
USD weakening by 10% (2020: 10%)	(455,422)	(635,845)
CNY strengthening by 10% (2020: 10%)	(455,114)	(479,091)
CNY weakening by 10% (2020: 10%)	455,114	479,091
EUR strengthening by 10% (2020: 10%)	(19,752)	(16,504)
EUR weakening by 10% (2020: 10%)	19,752	16,504
SDR strengthening by 10% (2020: 10%)	(70,215)	(71,512)
SDR weakening by 10% (2020: 10%)	70,215	71,512
XAU strengthening by 10% (2020: 10%)	159,468	140,589
XAU weakening by 10% (2020: 10%)	(159,468)	(140,589)
Other strengthening by 10% (2020: 10%)	28,434	17,169
Other weakening by 10% (2020: 10%)	(28,434)	(17,169)

The exposure was calculated only for monetary balances denominated in currencies other than the functional currency of the Bank and monetary balances denominated in SDRs.

The following table indicates the currencies, XAU and SDRs to which the Bank had significant exposure at 31 December 2021 on its monetary assets including gold bullion and precious metal and liabilities.

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

In millions of Mongolian Togrogs	MNT	USD	CNY	EUR	SDR	XAU	Other	Total
Cash on hand	38	72,542	51,136	35,712	-	-	18,163	**177,591**
Due from foreign financial institutions	-	2,996,207	702,108	65,600	387,299	-	322,575	**4,473,789**
Loans to local banks	1,486,637	671	-	-	-	-	-	**1,487,308**
Investments in debt securities	3,312,896	2,835,320	245,606	-	-	-	-	**6,393,822**
Investments in equity securities	6,533	-	-	-	-	-	-	**6,533**
Reverse repurchase agreements	1,430,987	3,091,233	-	-	-	-	-	**4,522,220**
Gold bullion and precious metals	-	-	-	-	-	1,594,676	-	**1,594,676**
Government securities	231,778	-	-	-	-	-	-	**231,778**
Other financial asset	298,108	(81)	-	-	-	-	-	**298,027**
Total financial assets	**6,766,977**	**8,995,892**	**998,850**	**101,312**	**387,299**	**1,594,676**	**340,738**	**19,185,744**
Cash in circulation	(1,105,589)	-	-	-	-	-	-	**(1,105,589)**
Central bank bills	(8,622,184)	-	-	-	-	-	-	**(8,622,184)**
Liabilities due to government organizations	(394,543)	(618,915)	(9)	(78,074)	(618,751)	-	(23,824)	**(1,734,116)**
Deposits from local banks	(2,323,564)	(1,812,787)	(86,407)	(220,754)	-	-	(28,365)	**(4,471,877)**
Liabilities due to foreign parties	(2,416)	(977,317)	(5,463,574)	-	(470,698)	-	-	**(6,914,005)**
Other financial liabilities	(650,000)	(13,025)	-	-	-	-	(4,206)	**(667,231)**
Total financial liabilities	**(13,098,296)**	**(3,422,044)**	**(5,549,990)**	**(298,828)**	**(1,089,449)**	**-**	**(56,395)**	**(23,515,002)**
Derivative financial instruments	719,370	(1,112,025)	-	-	-	-	-	**(392,655)**
Net balance sheet position	**(5,611,949)**	**4,461,823**	**(4,551,140)**	**(197,516)**	**(702,150)**	**1,594,676**	**284,343**	**(4,721,913)**

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

The following table indicates the currencies, XAU and SDRs to which the Bank had significant exposure at 31 December 2020 on its monetary assets including gold bullion and precious metal and liabilities.

In millions of Mongolian Togrogs	MNT	USD	CNY	EUR	SDR	XAU	Other	Total
Cash on hand	47	164,131	17,089	37,576	-	-	14,530	**233,373**
Due from foreign financial institutions	-	3,225,376	583,672	98,224	131,503	-	478,617	**4,517,392**
Loans to local banks	460,576	738	-	-	-	-	-	**461,314**
Investments in debt securities	2,924,909	2,306,627	43,593	-	-	-	-	**5,275,129**
Investments in equity securities	-	-	-	6,595	-	-	-	**6,595**
Reverse repurchase agreements	422,693	4,393,375	-	-	-	-	-	**4,816,068**
Gold bullion and precious metals	-	-	-	-	-	1,405,887	-	**1,405,887**
Government securities	227,407	-	-	-	-	-	-	**227,407**
Other financial asset	373,490	-	-	-	-	-	-	**373,490**
Total financial assets	**4,409,122**	**10,090,247**	**644,354**	**142,395**	**131,503**	**1,405,887**	**493,147**	**17,316,655**
Cash in circulation	(991,470)	-	-	-	-	-	-	**(991,470)**
Central bank bills	(7,952,438)	-	-	-	-	-	-	**(7,952,438)**
Liabilities due to government organizations	(888,930)	(479,219)	(9)	(94,288)	(646,516)	-	(23,063)	**(2,132,025)**
Deposits from local banks	(1,355,604)	(2,156,843)	(103,018)	(213,149)	-	-	(42,783)	**(3,871,397)**
Liabilities due to foreign parties	(1,381)	(179)	(5,332,233)	-	(200,102)	-	(255,613)	**(5,789,508)**
Other financial liabilities	(350,083)	(13,074)	-	-	-	-	-	**(363,157)**
Total financial liabilities	**(11,539,906)**	**(2,649,315)**	**(5,435,260)**	**(307,437)**	**(846,618)**	**-**	**(321,459)**	**(21,099,995)**
Derivative financial instruments	935,402	(1,082,484)	-	-	-	-	-	**(147,082)**
Net balance sheet position	**(6,195,382)**	**6,358,448**	**(4,790,906)**	**(165,042)**	**(715,115)**	**1,405,887**	**171,688**	**(3,930,422)**

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32. FINANCIAL RISK MANAGEMENT (CONTINUED)

Interest rate risk. Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments. The main objective when managing the interest rate risk is to maintain stable return on investments while not exceeding the risk levels that can be undertaken per investment policies.

Assets and liabilities of the Bank are predominantly fixed rate or non-interest bearing, which significantly reduces exposure to interest rate risk. Further, in strategic benchmark development process the Bank sets duration requirements for its foreign reserve portfolio in order to limit exposure to interest rate risk. The duration requirement is monitored on a daily basis. The duration of the investment is assessed through the application of horizon analysis. The Bank uses a one-year investment horizon, defined negative return as minimum return and up to 5% of acceptable variance of negative return for calculation of prudential duration.

The table below summarizes the Bank’s exposure to interest rate risks. The table presents the aggregated amounts of the Bank’s financial assets including gold bullion and precious metal and liabilities at carrying amounts, categorized by the earlier of contractual interest repricing or maturity dates:

In millions of Mongolian Togrogs	**Demand and less than one month**	**From 1 to 6 months**	**From 6 to 12 months**	**Over 12 months**	**Total interest bearing**	**Non-interest sensitive**	**Total**
31-Dec-21							
Total financial assets	9,583,810	55,820	1,141,763	6,598,300	17,379,693	1,883,155	**19,262,848**
Total financial liabilities	(16,354,976)	(124,529)	(6,676,453)	(791,524)	(23,947,482)	(162,501)	**(24,109,983)**
Net interest sensitivity gap at 31 December 2021	**(6,771,166)**	**(68,709)**	**(5,534,690)**	**5,806,776**	**(6,567,789)**	**1,720,654**	**(4,847,135)**
31-Dec-20							
Total financial assets	11,095,318	254,690	242,614	4,241,192	15,833,814	1,639,260	**17,473,074**
Total financial liabilities	(13,409,135)	(313,742)	(5,479,568)	(846,424)	(20,048,869)	(1,354,627)	**(21,403,496)**
Net interest sensitivity gap at 31 December 2020	**(2,313,817)**	**(59,052)**	**(5,236,954)**	**3,394,768**	**(4,215,055)**	**284,633**	**(3,930,422)**

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

Interest is accrued at floating rates on the following assets and liabilities: SDR holdings (note 8), SDR allocation, financing from People's Bank of China (note 23), and financing from Cargill Financial Services International (note 23). At 31 December 2021, if interest rates at reporting date had been 100 basis points lower with all other variables held constant, loss for the year would have been MNT 65,678 million lower (2020: MNT 42,151 million), mainly because of lower interest expense on variable interest liabilities, primarily loan from People's Bank of China. If interest rates had been 100 basis points higher, with all other variables held constant, loss would have been MNT 65,678 million higher (2020: MNT 42,151 million), mainly as a result of higher interest expense on variable interest liabilities.

The Bank monitors interest rates for its financial instruments. The table below summarizes interest rates at the respective reporting date based on reports reviewed by key management personnel. For quoted securities, the interest rates represent yields to maturity based on market quotations at the reporting date.

In % p.a.	2021				2020			
	MNT	**USD**	**CNY**	**Other**	**MNT**	**USD**	**CNY**	**Other**
Assets								
Due from foreign financial institutions	-	0.17%	2.86%	-	-	0.25%	2.50%	0.01%
Investments in debt securities	7.13%	0.93%	2.79%	-	7.13%	1.00%	2.38%	-
Reverse repurchases agreements	7.00%	-	-	-	7.00%	-	-	-
Government securities	1.00%	-	-	-	1.00%	-	-	-
Loans to local banks	3.74%	0.75%	-	-	5.50%	0.75%	-	-
Liabilities								
Central bank bills	6.00%	-	-	-	6.75%	-	-	-
Liabilities due to government organizations	-	2.17%	-	1.00%	3.50%	-	-	-
Deposits from local banks	5.00%	-	-	-	5.00%	0.19%	-	-
Liabilities due to foreign parties	-	2.41%	4.73%	-	-	-	4.87%	2.50%

The sign "- "in the table above means that the Bank does not have the respective assets or liabilities in the corresponding currency.

BANK OF MONGOLIA

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32. FINANCIAL RISK MANAGEMENT (CONTINUED)

Geographical risk concentrations. The geographical concentration of the Bank's financial assets and liabilities at 31 December 2021 is set out below:

In millions of Mongolian Togrogs	**Mongolia**	**OECD**	**IMF**	**Non-OECD**	**Total**
Assets					
Cash on hand	177,591	-	-	-	177,591
Due from foreign financial institutions	-	3,543,394	387,299	543,096	4,473,789
Loans to local banks	1,487,308	-	-	-	1,487,308
Investments in debt securities	3,313,009	3,058,132	-	22,681	6,393,822
Investments in equity securities	-	6,533	-	-	6,533
Reverse repurchases agreements	1,430,987	3,091,233	-	-	4,522,220
Gold and precious metals	-	1,594,676	-	-	1,594,676
Derivative financial instruments	77,103	-	-	-	77,103
Government securities	231,778	-	-	-	231,778
Another financial asset	298,027	-	-	-	298,027
Total financial assets	**7,015,803**	**11,293,968**	**387,299**	**565,777**	**19,262,847**
Liabilities					
Cash in circulation	(1,105,589)	-	-	-	(1,105,589)
Central bank bills	(8,622,184)	-	-	-	(8,622,184)
Liabilities due to government organizations	(1,734,116)	-	-	-	(1,734,116)
Deposits from local banks	(4,471,877)	-	-	-	(4,471,877)
Derivative financial instruments	(469,758)	-	-	-	(469,758)
Liabilities due to foreign parties	-	(979,733)	(470,698)	(5,463,574)	(6,914,005)
Other financial liabilities	(665,171)	-	-	-	(665,171)
Total financial liabilities	**(17,068,695)**	**(979,733)**	**(470,698)**	**(5,463,574)**	**(23,982,700)**
Net balance sheet position as 31 December 2021	**(10,052,892)**	**10,314,235**	**(83,399)**	**(4,897,797)**	**(4,719,853)**
Credit related commitments (Note 30)	**(22,475)**	**-**	**-**	**(6,000,000)**	**(6,022,475)**

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

The geographical concentration of the Bank's financial assets and liabilities at 31 December 2020 is set out below:

In millions of Mongolian Togrogs	Mongolia	OECD	IMF	Non-OECD	Total
Assets					
Cash on hand	233,373	-	-	-	233,373
Due from foreign financial institutions	-	3,802,217	131,503	583,672	4,517,392
Loans to local banks	461,314	-	-	-	461,314
Investments in debt securities	2,924,909	2,306,627	-	43,593	5,275,129
Investments in equity securities	6,595	-	-	-	6,595
Reverse repurchases agreements	422,693	4,393,375	-	-	4,816,068
Gold and precious metals	-	1,405,887	-	-	1,405,887
Derivative financial instruments	156,419	-	-	-	156,419
Government securities	227,407	-	-	-	227,407
Another financial asset	373,490	-	-	-	373,490
Total financial assets	**4,806,200**	**11,908,106**	**131,503**	**627,265**	**17,473,074**
Liabilities					
Cash in circulation	(991,470)	-	-	-	(991,470)
Central bank bills	(7,952,438)	-	-	-	(7,952,438)
Liabilities due to government organizations	(2,132,025)	-	-	-	(2,132,025)
Deposits from local banks	(3,871,397)	-	-	-	(3,871,397)
Derivative financial instruments	(303,501)	-	-	-	(303,501)
Liabilities due to foreign parties	-	(257,173)	(200,102)	(5,332,233)	(5,789,508)
Other financial liabilities	(363,157)	-	-	-	(363,157)
Total financial liabilities	**(15,613,988)**	**(257,173)**	**(200,102)**	**(5,332,233)**	**(21,403,496)**
Net balance sheet position as 31 December 2020	**(10,807,788)**	**11,650,933**	**(68,599)**	**(4,704,968)**	**(3,930,422)**
Credit related commitments (Note 30)	**(35,898)**	**-**	**-**	**(6,000,000)**	**(6,035,898)**

Other risk concentrations. Management monitors concentrations of credit risk through obtaining reports listing exposures to borrowers per counterparty limits, which are disclosed above. The Bank did not have any such significant risk concentrations as at 31 December 2021 and 31 December 2020.

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

Liquidity risk. Liquidity risk is the risk that the Bank will be unable to meet its payment obligations when they fall due under normal and stress circumstances. Liquidity risk of foreign currency is the main area of risk faced by the Bank. With respect to the classical investment triad (safety–liquidity-return), the investment policy of the Bank is maximizing returns, which ought to be considered only if all the liquidity and safety requirements are met. In circumstances of high import dependence, constant supply requirement of Government external debt servicing, volatility of demand and supply of foreign exchange in the domestic market, liquidity is the most important concern of foreign exchange reserve management. In order to manage liquidity risk, the Bank divided its foreign reserve portfolio into two sub-portfolios:

- The Short-term Investment Portfolio (including the cash management or liquidity portfolio): This portfolio is used for purposes of debt servicing and smooth functioning of the foreign exchange market. It consists of cash, overnights and demand deposits. It is also invested in time deposits, highly liquid money market instruments (commercial papers) and securities ranging from a week to twelve-month maturity and commodities (monetary gold).
- The Long-term Investment Portfolio: This portfolio is invested in medium to long-term high liquid instruments including government bonds and securities.

The Investment Committee proposes the limits for foreign exchange portfolio. In order to minimize the liquidity risk, the following asset structure is followed in accordance with the regulation on State Foreign Exchange Reserve Management:

- Not less than below limit defined as certain percentage of total assets with short-term maturity (i.e., maturity up to 1 year) shall be placed as current accounts and cash in foreign currency.
- Not less than below limit defined as percentage of total assets with short-term maturity (i.e. maturity up to 1 year) shall be placed as deposits with maturity up to 6 months.

Stop-loss limit of foreign trading is USD 400,000, while the limit of trading unit is USD 100,000 and the limit of one-off trading is USD 50,000, which also reduces liquidity risk.

The table below shows liabilities at 31 December 2021 by their remaining contractual maturity. The amounts of liabilities disclosed in the maturity table are the contractual undiscounted cash flows, including gross loan commitments and financial guarantees. Such undiscounted cash flows differ from the amount included in the statement of financial position because the amount in the statement of financial position is based on discounted cash flows. Financial derivatives are included at the contractual amounts to be paid or received i.e. payments in respect of gross settled forwards and swaps are accompanied by related cash inflows.

Liquidity requirements to support calls under issued letters of credit are considerably less than the amount of the commitment disclosed in the maturity analysis, because the Bank does not generally expect the third party to draw funds under the agreement. The total outstanding contractual amount of commitments to extend credit as included in the maturity table below does not necessarily represent future cash requirements, since these commitments may expire or terminate without being funded.

When the amount payable is not fixed, the amount disclosed is determined by reference to the conditions existing at the end of the reporting period. Foreign currency payments are translated, using the spot exchange rate at the end of the reporting period.

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32. FINANCIAL RISK MANAGEMENT (CONTINUED)

The maturity analysis of financial liabilities at 31 December 2021 is as follows:

In millions of Mongolian Togrogs	Demand and less than 1 month	From 1 to 6 months	From 6 to 12 months	Over 12 months	Total
Liabilities					
Cash in circulation	1,105,589	-	-	-	**1,105,589**
Central bank bills	8,644,994	-	-	-	**8,644,994**
Liabilities due to government organizations	1,080,844	835	6,363	655,937	**1,743,979**
Deposits from local banks	4,471,877	-	-	-	**4,471,877**
Liabilities due to foreign parties	472,596	-	6,504,011	-	**6,976,607**
Other financial liabilities	665,175	-	-	-	**665,175**
Gross settled swaps and forwards:					
- inflows	(13,844)	(186,156)	(240,873)	(671,152)	**(1,112,025)**
- outflows	15,393	75,802	74,806	553,369	**719,370**
Credit related commitments:					
-Undrawn credit line to PBC	6,000,000	-	-	-	**6,000,000**
-Other contingent liabilities	22,475	-	-	-	**22,475**
Total potential future payments for financial obligations	**22,465,099**	**(109,519)**	**6,344,307**	**538,154**	**29,238,041**

The maturity analysis of financial liabilities at 31 December 2020 is as follows:

In millions of Mongolian Togrogs	Demand and less than 1 month	From 1 to 6 months	From 6 to 12 months	Over 12 months	Total
Liabilities					
Cash in circulation	991,470	-	-	-	**991,470**
Central bank bills	7,777,935	-	266,799	-	**8,044,734**
Liabilities due to government organizations	1,483,042	1,339	-	685,731	**2,170,112**
Deposits from local banks	3,871,477	-	-	-	**3,871,477**
Liabilities due to foreign parties	300,636	214,249	5,435,870	-	**5,950,755**
Other financial liabilities	363,157	-	-	-	**363,157**
Gross settled swaps and forwards:					
- inflows	(19,153)	(188,867)	(124,978)	(749,486)	**(1,082,484)**
- outflows	12,751	179,781	96,025	646,845	**935,402**
Credit related commitments:					
-Undrawn credit line to PBC	6,000,000	-	-	-	**6,000,000**
-Other contingent liabilities	35,898	-	-	-	**35,898**
Total potential future payments for financial obligations	**20,817,212**	**206,502**	**5,673,716**	**583,091**	**27,280,521**

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

A significant portion of deposits from local banks and liabilities due to government organizations represent core deposits. Similarly, cash in circulation also represents a stable source of financing, although the Bank does not have unconditional contractual rights to delay payment. Refer to maturity analysis based on expected maturity below.

The Bank does not use the above maturity analysis based on undiscounted contractual maturities of liabilities to manage liquidity. Instead, the Bank monitors expected maturities of carrying amounts of financial assets and liabilities and the resulting expected liquidity gap. The table below shows the maturity analysis of financial assets and liabilities based on expected maturity.

Expected maturity of financial liabilities significantly differs from contractual maturity, due to a large amount of core deposits (consisting primarily from deposits from government organizations and local banks) and cash in circulation, as mentioned above. Financial assets that are readily saleable if it should be necessary to meet cash outflows on financial liabilities are included in the maturity analysis based on their expected date of disposal. Impaired loans are included at their carrying amounts net of impairment provisions and based on the expected timing of cash inflows.

The maturity analysis at 31 December 2021 is as follows:

In millions of Mongolian Togrogs	**Demand and less than 1 month**	**From 1 to 6 months**	**From 6 to 12 months**	**Over 12 months**	**Total**
Assets					
Cash on hand	177,591	-	-	-	**177,591**
Due from foreign financial institutions	4,473,789	-	-	-	**4,473,789**
Investments in debt securities	1,665,398	42,997	101,646	4,583,781	**6,393,822**
Investments in equity securities	-	-	-	6,533	**6,533**
Reverse repurchases agreements	3,467,428	-	-	1,054,792	**4,522,220**
Gold and precious metals	1,594,676	-	-	-	**1,594,676**
Derivative financial instruments	15,096	44,190	12	17,805	**77,103**
Government securities	672	-	-	231,106	**231,778**
Loans to local banks	11,264	12,823	879,002	584,219	**1,487,308**
Other financial assets	16,843	-	161,116	120,069	**298,028**
Total financial assets	**11,422,757**	**100,010**	**1,141,776**	**6,598,305**	**19,262,848**
Liabilities					
Cash in circulation	(1,105,589)	-	-	-	**(1,105,589)**
Central bank bills	(8,622,184)	-	-	-	**(8,622,184)**
Liabilities due to government organizations	(1,112,858)	(835)	(409)	(620,014)	**(1,734,116)**
Deposits from local banks	(4,471,877)	-	-	-	**(4,471,877)**
Derivative financial instruments	(13,547)	(154,545)	(166,079)	(135,587)	**(469,758)**
Liabilities due to foreign parties	(571,067)	-	(6,058,058)	(284,880)	**(6,914,005)**
Other financial liabilities	(665,171)	-	-	-	**(665,171)**
Total financial liabilities	**(16,562,293)**	**(155,380)**	**(6,224,546)**	**(1,040,481)**	**(23,982,700)**
Net liquidity gap	**(5,139,536)**	**(55,370)**	**(5,082,770)**	**5,557,824**	**(4,719,852)**

32. FINANCIAL RISK MANAGEMENT (CONTINUED)

The maturity analysis at 31 December 2020 is as follows:

In millions of Mongolian Togrogs	Demand and less than 1 month	From 1 to 6 months	From 6 to 12 months	Over 12 months	Total
Assets					
Cash on hand	233,373	-	-	-	**233,373**
Due from foreign financial institutions	4,517,392	-	-	-	**4,517,392**
Investments in debt securities	1,981,989	65,429	108,089	3,119,622	**5,275,129**
Investments in equity securities	-	-	-	6,595	**6,595**
Reverse repurchases agreements	4,522,516	-	62,314	231,238	**4,816,068**
Gold and precious metals	1,405,887	-	-	-	**1,405,887**
Derivative financial instruments	-	90,559	-	65,860	**156,419**
Government securities	-	-	-	227,407	**227,407**
Loans to local banks	443	966	51,378	408,527	**461,314**
Other financial assets	72,978	97,736	20,833	181,943	**373,490**
Total financial assets	**12,734,578**	**254,690**	**242,614**	**4,241,192**	**17,473,074**
Liabilities					
Cash in circulation	(991,470)	-	-	-	**(991,470)**
Central bank bills	(7,777,935)	-	(174,503)	-	**(7,952,438)**
Liabilities due to government organizations	(1,452,764)	(1,337)	-	(677,924)	**(2,132,025)**
Deposits from local banks	(3,871,397)	-	-	-	**(3,871,397)**
Derivative financial instruments	(6,403)	(99,645)	(28,953)	(168,500)	**(303,501)**
Liabilities due to foreign parties	(300,636)	(212,760)	(5,276,112)	-	**(5,789,508)**
Other financial liabilities	(363,157)	-	-	-	**(363,157)**
Total financial liabilities	**(14,763,762)**	**(313,742)**	**(5,479,568)**	**(846,424)**	**(21,403,496)**
Net liquidity gap	**(2,029,184)**	**(59,052)**	**(5,236,954)**	**3,394,768**	**(3,930,422)**

33. FAIR VALUE OF FINANCIAL INSTRUMENT

Fair value measurements are analysed by level in the fair value hierarchy as follows: (i) level one are measurements at quoted prices (unadjusted) in active markets for identical assets or liabilities, (ii) level two measurements are valuations techniques with all material inputs observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices), and (iii) level three measurements are valuations not based on observable market data (that is, unobservable inputs). Management applies judgement in categorizing financial instruments using the fair value hierarchy. If a fair value measurement uses observable inputs that require significant adjustment, that measurement is a Level 3 measurement. The significance of a valuation input is assessed against the fair value measurement in its entirety.

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33. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

(a) Recurring fair value measurements

Recurring fair value measurements are those that the accounting standards require or permit in the statement of financial position at the end of each reporting period. The level in the fair value hierarchy into which the recurring fair value measurements are categorized as at 31 December 2021 are, as follows:

	31 December 2021			
In millions of Mongolian Togrogs	**Level 1**	**Level 2**	**Level 3**	**Total**
ASSETS AT FAIR VALUE				
Financial assets and Gold bullion and precious metals at fair value				
- Bonds issued by Bank for International Settlements	1,647,228	-	-	1,647,228
- RAMP Investment Account Assets	928,574	-	-	928,574
- US treasury bills	244,529	-	-	244,529
- BIS Investments	146,463	-	-	146,463
- IBRD Bonds	52,694	-	-	52,694
- KfW bonds	30,085	-	-	30,085
- China government bonds	22,670	-	-	22,670
- European Investment Bank bond	8,570	-	-	8,570
- Other equity investments	-	-	6,533	6,533
- Gold Bullion and Precious Metals at fair value	1,594,676	-	-	1,594,676
- Government securities	-	231,778	-	231,778
- Receivables related to promissory notes	-	-	224,487	224,487
- Derivative financial assets	-	-	77,103	77,103
Non-financial assets				
- Buildings and premises	-	-	89,070	89,070
- Treasury fund	-	-	1,115,085	1,115,085
TOTAL ASSETS WITH RECURRING FAIR VALUE MEASUREMENTS	**4,675,489**	**231,778**	**1,512,278**	**6,419,545**
LIABILITIES CARRIED AT FAIR VALUE				
Financial liabilities				
- Derivative financial liabilities	-	-	(469,758)	(469,758)
TOTAL LIABILITIES WITH RECURRING FAIR VALUE MEASUREMENTS	**-**	**-**	**(469,758)**	**(469,758)**

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NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

33. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

The level in the fair value hierarchy into which the recurring fair value measurements are categorized as at 31 December 2020 are, as follows:

	31 December 2020			
In millions of Mongolian Togrogs	**Level 1**	**Level 2**	**Level 3**	**Total**
ASSETS AT FAIR VALUE				
Financial assets and Gold bullion and precious metals at fair value				
- RAMP Investment Account Assets	930,566	-	-	930,566
- Bonds issued by Bank for International Settlements	898,352	-	-	898,352
- US treasury bills	278,804	-	-	278,804
- BIS Investments	146,569	-	-	146,569
- IBRD bonds	47,800	-	-	47,800
- KfW bonds	30,554	-	-	30,554
- European Investment Bank bond	17,575	-	-	17,575
-Other equity investments	-	-	6,595	6,595
-Gold Bullion and Precious Metals at fair value	1,405,887	-	-	1,405,887
- Government securities	-	227,407	-	227,407
- Receivables related to promissory notes	-	-	282,545	282,545
- Derivative financial assets	-	-	156,419	156,419
Non-financial assets				
- Buildings and premises	-	-	89,745	89,745
- Treasury fund	-	-	1,071,665	1,071,665
TOTAL ASSETS WITH RECURRING FAIR VALUE MEASUREMENTS	**3,756,107**	**227,407**	**1,606,969**	**5,590,483**
LIABILITIES CARRIED AT FAIR VALUE				
Financial liabilities				
- Derivative financial liabilities	-	-	(303,501)	(303,501)
TOTAL LIABILITIES WITH RECURRING FAIR VALUE MEASUREMENTS	**-**	**-**	**(303,501)**	**(303,501)**

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33. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

The description of valuation technique and description of inputs used in the fair value measurement for level 2 measurements at 31 December 2021 and 31 December 2020:

In millions of Mongolian Togrogs	Fair value 2021	Fair value 2020	Valuation technique	Inputs used
ASSETS AT FAIR VALUE				
Financial assets				
- Government securities	231,778	227,407	Discounted Cash Flow	Discount rate based on policy rate and CF projection according to repayment schedule
TOTAL RECURRING FAIR VALUE MEASUREMENTS AT LEVEL 2	**231,778**	**227,407**		

The description of valuation technique and description of inputs used in the fair value measurement for level 3 measurements at 31 December 2021 and 31 December 2020:

In millions of Mongolian Togrogs	Fair value 2021	Fair value 2020	Valuation technique	Inputs used
ASSETS AT FAIR VALUE				
Financial assets				
- Financial derivatives	77,103	156,419	Discounted Cash Flow	US leg based on US LIBOR 3M / 6M / 12M, Z spread, and Most up-to-date weighted average interest of commercial banks' USD accounts, US discount rate based on US LIBOR 3M / 6M and Z spread, MNT leg based on policy rate, CBB 28-week rate and repo rate, MNT discount rate based on repo rate, Forward rate using GAP model
- Promissory notes	224,487	282,545	Discounted Cash Flow	Audited Financial Statements of promissory note issuers, discount rate based on policy rate and credit risk spread based on credit risk of counterparty, and CF projection according to repayment schedule
Non-financial assets				
- Buildings and premises	89,070	89,745	Market, Income, and Cost approach	Comparable market prices with appropriate adjustments/ discounts/haircuts, DCF from expected market rental income and estimated current costs to reproduce property of equal quality, utility, and marketability
- Treasury Fund:	1,115,085	1,071,665	Market and Cost approach	See below:
Coins	917,700	917,585	Market approach	Comparable market prices with appropriate adjustments/ discounts/haircuts
Historical items	197,385	154,080	Market and Cost approach	Comparable market prices with appropriate adjustments/ discounts/haircuts, and estimated current costs to reproduce property of equal quality, utility, and marketability

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33. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

LIABILITIES CARRIED AT FAIR VALUE				
Financial liabilities				
- Financial derivatives	(469,758)	(303,501)	Discounted Cash Flow	US leg based on US LIBOR 3M / 6M / 12M, Z spread, and Most up-to-date weighted average interest of commercial banks' USD accounts, US discount rate based on US LIBOR 3M / 6M and Z spread, MNT leg based on policy rate, CBB 28-week rate and repo rate, MNT discount rate based on repo rate, Forward rate using GAP model
TOTAL RECURRING FAIR VALUE MEASUREMENTS AT LEVEL 3	**1,035,987**	**1,296,873**		

The inputs used in the fair value measurement for level 3 measurements and related sensitivity to reasonably possible changes in those inputs are as follows at 31 December 2021:

In millions of Mongolian Togrogs	Fair value 2021	Inputs used	Range of inputs (weighted average)	Reasonable change	Sensitivity of fair value measurement
ASSETS AT FAIR VALUE					
Financial assets					
- Financial derivatives	77,103	US leg based on US LIBOR 3M / 6M / 12M, Z spread, and Most up-to-date weighted average interest of commercial banks' USD accounts	1.8%-3% (2.63%)	± 10 %	±2,105
		MNT leg based on policy rate, CBB 28-week rate and repo rate	6.36%	± 10 %	±9,426
		Forward rate	2,821.08 – 3,055.87 (2,972.34)	± 10 %	±32,056
- Promissory notes	224,487	Policy rate and credit risk spread	6.85% -7.71% (7.47%)	± 10 %	±2,035
Non-financial assets					
- Buildings and premises	89,070	Market prices with appropriate adjustments, discounts/haircuts	0.5-2.4	± 10 %	±8,907
- Treasury Fund	1,115,085			± 10 %	±111,509
Coins	917,700	Market prices with appropriate adjustments, discounts/haircuts	0.1–1.1	± 10 %	± 91,770
Historical items	197,385	Market prices with appropriate adjustments, discounts/haircuts	2-13,228	± 10 %	±19,739

33. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

LIABILITIES CARRIED AT FAIR VALUE					
Financial liabilities					
- Financial derivatives	(469,758)	US leg based on US LIBOR 3M / 6M / 12M, Z spread, and Most up-to-date weighted average interest of commercial banks' USD accounts	2% - 6.69% (5%)	± 10 %	±7,523
		MNT leg based on policy rate, CBB 28-week rate and repo rate	6% - 6.36% (6%)	± 10 %	±23,779
		Forward rate	2,434.74 – 3,055.87 (2,983.97)	± 10 %	±374,951

The inputs used in the fair value measurement for level 3 measurements and related sensitivity to reasonably possible changes in those inputs are as follows at 31 December 2020:

In millions of Mongolian Togrogs	Fair value 2020	Inputs used	Range of inputs (weighted average)	Reasonable change	Sensitivity of fair value measurement
ASSETS AT FAIR VALUE					
Financial assets					
- Financial derivatives	156,419	US leg based on US LIBOR 3M / 6M / 12M, Z spread, and Most up-to-date weighted average interest of commercial banks' USD accounts	1.8% - 5.37% (3.46%)	± 10 %	±2,772
		MNT leg based on policy rate, CBB 28-week rate and repo rate	6.5% - 9.5% (8.49%)	± 10 %	±19,732
		Forward rate	2,866.38 – 2,884.65 (2,877.1)	± 10 %	±45,935
- Promissory notes	282,545	Policy rate and credit risk spread	8% - 17.08% (9.85%)	± 10 %	±3,793
Non-financial assets					
- Buildings and premises	89,745	Market prices with appropriate adjustments, discounts/haircuts	0.5-2.4	± 10 %	±8,975
- Treasury Fund	1,071,665			± 10 %	±107,167
Coins	917,585	Market prices with appropriate adjustments, discounts/haircuts	0.1–1	± 10 %	±91,759
Historical items	154,080	Market prices with appropriate adjustments, discounts/haircuts	27-4,536	± 10 %	±15,408
LIABILITIES CARRIED AT FAIR VALUE					
Financial liabilities					

33. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

- Financial derivatives	(303,501)	US leg based on US LIBOR 3M / 6M / 12M, Z spread, and Most up-to-date weighted average interest of commercial banks' USD accounts	3.94% - 8.07% (5.25%)	± 10 %	±11,811
		MNT leg based on policy rate, CBB 28-week rate and repo rate	6% - 10% (8.17%)	± 10 %	±44,523
		Forward rate	2,863.46 – 2,965.39 (2,913.4)	± 10 %	±315,658

The above tables disclose sensitivity to valuation inputs for financial assets and financial liabilities, if changing one or more of the unobservable inputs to reflect reasonably possible alternative assumptions would change fair value significantly. For this purpose, significance was judged with respect to profit or loss, and total assets or total liabilities, or, when changes in fair value are recognised in other comprehensive income, total equity.

Reasonable possible changes in input (market price of equity instrument) would have impact on the Bank's equity and no impact on the Bank's financial result, as material impairment is considered unlikely. If the market price of investment in equity securities, classified as level 3 for fair value measurement purposes, would increase/(decrease) by 10%, the fair value of these investment would increase/(decrease) by MNT 653 million (2020: MNT 660 million).

There were no changes in valuation technique for level 3 recurring fair value measurements during the year ended 31 December 2021 (2020: none).

A reconciliation of movements in Level 3 of the fair value hierarchy by class of instruments for the year ended 31 December 2021 and 31 December 2020 is as follows:

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33. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

In millions of Mongolian Togrogs	**2021**	**2020**
Financial derivative assets and liabilities, net		
Fair value on 1 January	**(147,082)**	**(284,262)**
Gains or losses recognised in profit or loss for the year	(219,426)	(242,925)
Settlements	(26,147)	380,104
Fair value at 31 December	**(392,655)**	**(147,082)**
Unrealised revaluation gains less losses/(losses less gains) recognised in profit or loss for the year for assets held at 31 December	**230,779**	**(138,813)**

In millions of Mongolian Togrogs	**2021**	**2020**
Promissory notes		
Fair value on 1 January	**282,545**	**394,621**
Gains or losses recognised in profit or loss for the year	59,638	(27,707)
Settlements	(117,696)	(84,369)
Fair value at 31 December	**224,487**	**282,545**
Unrealised revaluation losses less gains recognised in profit or loss for the year for assets held at 31 December	**(39,180)**	**(166,682)**

33. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

(b) Assets and liabilities not measured at fair value but for which fair value is disclosed

Fair values analysed by level in the fair value hierarchy and carrying value of assets not measured at fair value as at 31 December 2021 are as follows:

	31 December 2021			
In millions of Mongolian Togrogs	**Level 1**	**Level 2**	**Level 3**	**Carrying amount**
FINANCIAL Assets				
Cash and cash equivalents				
-Cash on hand	177,591	-	-	177,591
Due from foreign financial institutions				
-Short term deposits in foreign currency	-	3,297,153	-	3,297,153
-Demand deposits	-	789,147	-	789,147
-Special drawing rights holdings	-	387,299	-	387,299
-World Bank subscriptions	-	179	-	179
-Other subscriptions	-	12	-	12
Loans to local banks				
- Loans issued under Price Stabilization Program	-	-	825,066	825,066
-Other loans	-	-	662,242	662,242
Investments in debt securities				
-Investments in debt securities	-	3,313,009	-	3,313,009
Reverse repurchases agreements				
-Federal Reserve Bank of New York	-	3,091,231	-	3,091,231
- Local banks	-	1,430,989	-	1,430,989
Other financial assets	-	73,822	-	73,822
Total financial assets carried at amortized cost	**177,591**	**12,382,841**	**1,487,308**	**14,047,740**

Fair values analysed by level in the fair value hierarchy and carrying value of assets not measured at fair value as at 31 December 2020 are as follows:

BANK OF MONGOLIA

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33. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

	31 December 2020			
In millions of Mongolian Togrogs	**Level 1**	**Level 2**	**Level 3**	**Carrying amount**
FINANCIAL Assets				
Cash and cash equivalents				
-Cash on hand	233,373	-	-	233,373
Due from foreign financial institutions				
-Short term deposits in foreign currency	-	3,507,650	-	3,507,650
-Demand deposits	-	878,047	-	878,047
-Special drawing rights holdings	-	131,503	-	131,503
-World Bank subscriptions	-	179	-	179
-Other subscriptions	-	13	-	13
Loans to local banks				
- Loans issued under Price Stabilization Program	-	-	368,839	368,839
-Other loans	-	-	92,475	92,475
Investments in debt securities				
-Investments in debt securities	-	2,924,909	-	2,924,909
Reverse repurchases agreements				
-Federal Reserve Bank of New York	-	4,393,375	-	4,393,375
- Local banks	-	422,693	-	422,693
Other financial assets	-	90,945	-	90,945
Total financial assets carried at amortized cost	**233,373**	**12,349,314**	**461,314**	**13,044,001**

Fair values analysed by level in the fair value hierarchy and carrying value of liabilities not measured at fair value as at 31 December 2021 are as follows:

	31 December 2021			
In millions of Mongolian Togrogs	**Level 1**	**Level 2**	**Level 3**	**Carrying amount**
FINANCIAL liabilities				
Cash in circulation	1,105,589	-	-	1,105,589
Central bank bills	-	8,622,184	-	8,622,184
Liabilities due to government organizations				
-Current accounts of Ministry of Finance	-	1,079,704	-	1,079,704
- Liabilities to the Ministry of Finance related to borrowings	-	654,412	-	654,412
Deposits from local banks				
-Correspondent accounts	-	3,965,808	-	3,965,808
-Overnight deposits in national currency	-	506,069	-	506,069
Liabilities due to foreign parties				
-Financing from People's Bank of China	-	5,463,574	-	5,463,574
-Financing from Cargill Financial Services International	-	570,417	-	570,417
-Allocation of Special Drawing Rights of IMF	-	470,698	-	470,698
-Financing from MUFG Bank Ltd	-	284,905	-	284,905
-Financing from Bank of International Settlements	-	122,513	-	122,513
-Current account of World Bank	-	1,620	-	1,620
-Subscription to World Bank	-	179	-	179
-Subscription to IDA	-	39	-	39
-Current account of ADB	-	61	-	61
Other financial liabilities	-	665,175	-	665,175
Total financial liabilities carried at amortized cost	**1,105,589**	**22,407,358**	**-**	**23,512,947**

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NOTES TO THE FINANCIAL STATEMENTS – 31 DECEMBER 2021

33. FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

Fair values analysed by level in the fair value hierarchy and carrying value of liabilities not measured at fair value as at 31 December 2020 are as follows:

	31-Dec-20			
In millions of Mongolian Togrogs	**Level 1**	**Level 2**	**Level 3**	**Carrying amount**
FINANCIAL liabilities				
Cash in circulation	991,470	-	-	991,470
Central bank bills	-	7,952,438	-	7,952,438
Liabilities due to government organizations				
-Current accounts of Ministry of Finance	-	1,452,764	-	1,452,764
- Liabilities to the Ministry of Finance related to borrowings	-	679,261	-	679,261
Deposits from local banks				
-Correspondent accounts	-	3,565,407	-	3,565,407
-Overnight deposits in national currency	-	106,515	-	106,515
-Foreign currency time deposits	-	199,475	-	199,475
Liabilities due to foreign parties				
-Financing from People's Bank of China	-	5,332,233	-	5,332,233
-Allocation of Special Drawing Rights of IMF	-	200,102	-	200,102
-Financing from MUFG Bank Ltd	-	255,613	-	255,613
-Current account of World Bank	-	1,281	-	1,281
-Subscription to World Bank	-	179	-	179
-Subscription to IDA	-	39	-	39
-Current account of ADB	-	61	-	61
Other financial liabilities	-	363,158	-	363,158
Total financial liabilities carried at amortized cost	**991,470**	**20,108,526**	**-**	**21,099,996**

34. PRESENTATION OF FINANCIAL INSTRUMENTS BY MEASUREMENT CATEGORY

For the purposes of measurement, IFRS 9 "Financial Instruments" classifies financial assets into the following categories: (a) financial assets at FVTPL; (b) debt instruments at FVOCI, (c) equity instruments at FVOCI and (c) financial assets at AC. Financial assets at FVTPL have two sub-categories: (i) assets mandatorily measured at FVTPL, and (ii) assets designated as such upon initial recognition or subsequently.

The following table provides a reconciliation of financial assets with these measurement categories as at 31 December 2021:

	31 December 2021					
In millions of Mongolian Tugriks	**AC**	**Debt instruments at FVOCI**	**Equity instruments at FVOCI**	**FVTPL (mandatory)**	**FVTPL (desig-nated)**	**Total**
Financial Assets and Gold bullion and precious metals at fair value						
Cash and cash equivalents						
-Cash on hand	177,591	-	-	-	-	177,591
Due from foreign financial institutions						
-Short term deposits in foreign currency	3,297,153	-	-	-	-	3,297,153
-Demand deposits	789,147	-	-	-	-	789,147
-Special drawing rights holdings	387,299	-	-	-	-	387,299
-World Bank subscriptions	179	-	-	-	-	179
-Other subscriptions	12	-	-	-	-	12
Loans to local banks						
- Loans issued under Price Stabilization Program	825,066	-	-	-	-	825,066
-Other loans	662,242	-	-	-	-	662,242
Gold and precious metal	-	-	-	-	1,594,676	1,594,676
Investments in debt securities	3,313,009	3,080,813	-	-	-	6,393,822
Investments in equity securities	-	-	6,533	-	-	6,533
Reverse repurchases agreements						
- Federal Reserve Bank of New York	3,091,231	-	-	-	-	3,091,231
- Local banks	1,430,989	-	-	-	-	1,430,989
Government securities	-	231,778	-	-	-	231,778
Derivative financial assets	-	-	-	77,103	-	77,103
Other financial assets	73,822	-	-	224,487	-	298,309
Total financial assets and Gold bullion and precious metals at fair value	**14,047,740**	**3,312,591**	**6,533**	**301,590**	**1,594,676**	**19,263,130**

34. PRESENTATION OF FINANCIAL INSTRUMENTS BY MEASUREMENT CATEGORY (CONTINUED)

The following table provides a reconciliation of financial assets with these measurement categories as at 31 December 2020:

	31 December 2021					
In millions of Mongolian Tugriks	AC	Debt instruments at FVOCI	Equity instruments at FVOCI	FVTPL (mandatory)	FVTPL (designated)	Total
Financial Assets and Gold bullion and precious metals at fair value						
Cash and cash equivalents						
-Cash on hand	233,373	-	-	-	-	233,373
Due from foreign financial institutions						
-Short term deposits in foreign currency	3,507,650	-	-	-	-	3,507,650
-Demand deposits	878,047	-	-	-	-	878,047
-Special drawing rights holdings	131,503	-	-	-	-	131,503
-World Bank subscriptions	179	-	-	-	-	179
-Other subscriptions	13	-	-	-	-	13
Loans to local banks						
- Loans issued under Price Stabilization Program	368,839	-	-	-	-	368,839
-Other loans	92,475	-	-	-	-	92,475
Gold and precious metal	-	-	-	-	1,405,887	1,405,887
Investments in debt securities	2,924,909	2,350,220	-	-	-	5,275,129
Investments in equity securities	-	-	6,595	-	-	6,595
Reverse repurchases agreements						
- Federal Reserve Bank of New York	4,393,375	-	-	-	-	4,393,375
- Local banks	422,693	-	-	-	-	422,693
Government securities	-	227,407	-	-	-	227,407
Derivative financial assets	-	-	-	156,419	-	156,419
Other financial assets	90,945	-	-	282,545	-	373,490
Total financial assets and Gold bullion and precious metals at fair value	**13,044,001**	**2,577,627**	**6,595**	**438,964**	**1,405,887**	**17,473,074**

As at 31 December 2021 and 31 December 2020, all of the Bank’s financial liabilities were carried at amortized cost except for derivatives, which belong to the fair value through profit or loss measurement category.

35. CAPITAL MANAGEMENT

The capital of the Bank comprises the residual value of the Bank's assets after deduction of all its liabilities. The Bank's objectives when managing capital are to maintain an appropriate level of capital to ensure economic independence of the Bank and ability to perform its functions. The Bank considers total capital under management to be equity shown in the statement of financial position as disclosed in these financial statements.

No external capital requirements exist for the Bank as the central bank. The Law on Central Bank (Bank of Mongolia) defines the minimum amount of statutory capital (charter fund) and minimum portion of annual net income, which needs to be allocated to the Bank's equity.

The statutory capital as at 31 December 2021 is MNT 60,000 million (2020: MNT 60,000 million), which is above the minimum amount MNT 5,000 million defined by the Law. The Law also states that at least 40% of the Bank's net income must be allocated to the Bank's equity, while the remaining amount (i.e., maximum 60% of net income) can be transferred to the State Budget account. No transfers were made to the State Budget during 2021 and 2020.

The Bank has earned loss of MNT 1,044,072 million in 2021 (2020: loss of MNT 503,378 million) and has negative equity position of MNT 3,372,056 million as at 31 December 2021 (2020: 2,309,283 million). Article 38 of the Law stipulates that if a deficit of the Central Bank arises, the Parliament shall decide whether the Government must issue securities to cover the difference in the amount of the net deficit. Thus, the Government has no obligation to fund a net deficit of the Bank. However, issuance of government bonds for covering a deficit is a possibility, which could be used by the Parliament, if covering a deficit is necessary to enable the Bank to perform its functions and continue its operations.

According to the Article 37 of the Law, the revaluation fund of the Bank should include the following:

- differences resulting from the foreign currency revaluation of assets and liabilities that are held in gold and in foreign currency due to fluctuations of foreign exchange rate of Mongolian Togrogs.
- differences resulting from the revaluation of fixed assets (i.e. buildings) and treasury fund.

According to the Article 37 of the Law, the differences resulting from the revaluation of foreign currency denominated assets and liabilities and gold should not be included in the determination of net distributable income of the Bank.

As a result, the Bank has established a revaluation reserve for foreign exchange and gold bullion, revaluation reserve for buildings and premises, revaluation reserve for treasury fund, and revaluation reserve for investments in debt securities, refer to Notes 4 and 25.

36. EVENTS AFTER THE END OF THE REPORTING PERIOD

Ukraine-Russia conflict

On 24 February 2022, Russia began a military invasion of Ukraine. Following the event, many countries began to impose sanctions on Russia's financial sector. Sanctions include freezing assets of Russian banks, politicians, and other related individuals, restricting access to securities. The most recent of these sanctions was the removal of some Russian banks from the SWIFT payment system. As a result, trade with Russia may be restricted and access to oil, natural gas and other exports could be limited. Mongolia might face a risk of increased fuel prices as the changes in world oil prices; however, uncertainty surrounding the war remains high. The Bank has no direct exposure to the sanctions imposed on Russia, but it could further impact the Bank's ability to do make transactions with Russian counterparties. It is not possible for management to predict with any degree of certainty the impact of this uncertainty on the future operations of the Bank.

On 28 March 2022, the Ministry of Finance repaid the government securities with par value of MNT 277,378 million at a coupon rate of 1% pa by the senior RMBS bonds. Carrying value of the government securities at derecognition date was MNT 140,122 million and the fair value of mortgage loans and Senior RMBS were MNT 140,122 million.

Management is not aware of any events that occurred after the end of reporting period, which would have an impact on these financial statements.

37. MONGOLIAN TRANSLATION

These financial statements are also prepared in Mongolian language. In the event of discrepancies or contradictions between the English version and the Mongolian version, the English version will prevail.