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**Working Paper**

## Leveraging SME finance through value chains in the CAREC landlocked economies

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**ADB Working Paper Series**

**LEVERAGING SME FINANCE  
THROUGH VALUE CHAINS IN THE  
CAREC LANDLOCKED ECONOMIES**

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**Asian Development Bank Institute**

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**Abstract**

This paper analyzes the situation of SMEs in Mongolia, especially their financial situation and financing mechanisms, the business environment, the existing policies, and value chain analysis, and makes suggestions for enhancing their development. Value chains that have their potential developed further are the cashmere, tourism, fruit, and berry sectors. Key factors in the development of SMEs in Mongolia are discussed along with factors hindering their development. There is no unified database on SMEs and different organizations are responsible for gathering data on them. Thus the statistics on SMEs are inconsistent and fragmented. Therefore, it is difficult to present a clear picture of SMEs and make sound policies based on reliable, coherent analysis and data in favor of SMEs. Due to the sparse population, traditional banking services are costly, especially outside of the residential areas. A lack of sound credit infrastructure and governmental regulations are the main problems in the credit market for SMEs. Financial institutions offer only a few available financial products, due to the underdeveloped Mongolian financial sectors, insufficient government support, and the lack of a regulatory framework. The paper concludes by emphasizing the need to: (i) improve the quality of data on SMEs and establish the relevance of in-depth study of financial literacy to obtain a clear picture of them and develop effective policies; (ii) improve the regulatory framework for business, especially the fair competitiveness regulations; (iii) develop the regulatory framework for other sources of funding; (iv) develop a long-term national program for SMEs.

**Keywords:** SME sector, financial literacy, financing, global value chain, value chain financing, agriculture

**JEL Classification:** D53, G23, L26, Q13, Q14, Q17

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## 1. INTRODUCTION

Mongolia transitioned to a market economy in 1990 and became one of the fastest-growing economies due to the double-digit growth for three consecutive years in early 2010. With the slowdown of commodity prices the economic growth started to decline. The latest reports from the NSO and the World Bank show that the poverty rate is 35.5% in the countryside, compared to 23.2% in urban areas.

Administratively, Mongolia is divided into 21 aimags and the capital city of Ulaanbaatar, which is not part of a province. While up to 65% of GDP is produced in Ulaanbaatar city and 10% is produced in Orkhon province where the Erdenet Mining Corporation has been active since 1978, the remaining 25% is divided amongst the other 20 provinces. GDP per capita is three times lower in the countryside than in the city. There is a lower level of job opportunity and the business environment is unfavorable, due to poor infrastructure and low market potential, amongst other problems.

The research question of this paper is: “Are business environment and financing mechanisms favorable for SMEs?”

### 1.1 Analytical Framework

SMEs are the main drivers of an economy because they create most of the jobs and contribute to reducing poverty and inclusive economic growth. Thus, support of SMEs through effective policies and financing mechanisms remains the primary goal of countries across the world. Today, SMEs in developing countries are facing many difficulties. The objective of this paper is to identify the bottlenecks and drivers of economic growth as well as value chains with high growth potential.

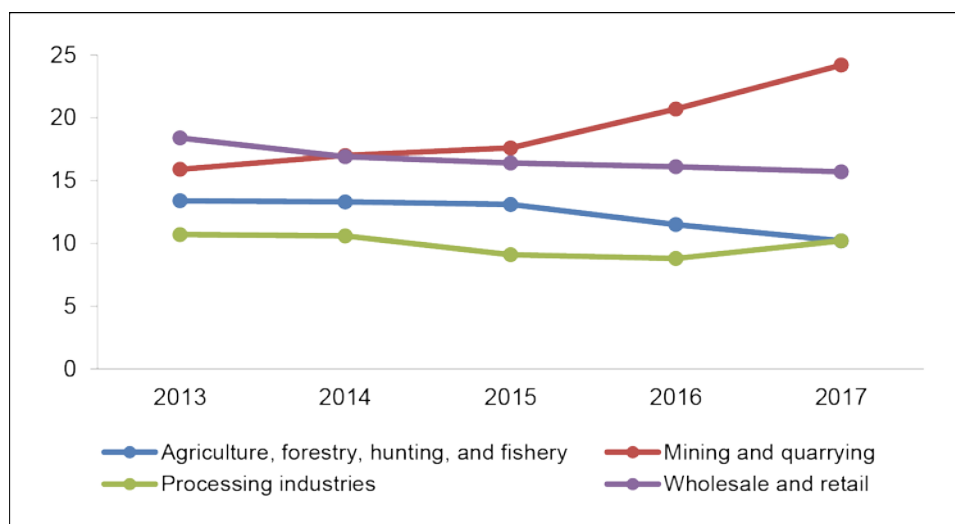
In general, the share of SMEs in GDP, business environment, financing mechanisms, government policies, and inclusion of SMEs in the value chain of a country are the important factors that have to be studied.

## 2. ECONOMIC SITUATION

Mongolia is landlocked and one of the world's most sparsely populated countries. The economic growth of Mongolia was very volatile in the last decade. Due to large projects in mining and infrastructure, the economic growth of Mongolia in the period from 2010 to 2014 was high. A sharp slowdown of growth occurred when the commodity prices fell in 2016, which highlighted again the need for economic diversification and high dependency on mining. In recent years, migration in Mongolia has continued the trend of rural to urban flows, particularly in Ulaanbaatar. The present urban population is above 1.3 million or almost half of the population of Mongolia. Despite significant economic opportunities, poverty and inequality continue to be serious problems and inequalities are widening between regions and between rural and urban areas.

The main driver of economic growth is mining and quarrying (24.5% of GDP as of 2017), while the second largest sector is wholesale and retail (15.7% of GDP as of 2017), followed by agriculture (10.2% of GDP as of 2017) and manufacturing (10.5% of GDP as of 2017). The real estate sector makes up 6.0% of GDP, financial and insurance activities 5.1%, transportation and storage 4.8%, and construction 4.1% as of 2017 (Figure 1).

**Figure 1: GDP Breakdown by Sectors**



Source: NSO (2019a).

According to the statistical information from the General Taxation Department, there are 78,585 legal entities active in Mongolia. Almost 70% of enterprises are located in Ulaanbaatar, and about 86% or 67,612 of those are SMEs.

The SME Law was first introduced in 2007 in which SMEs are defined as legally registered business entities with 199 or fewer employees with an annual turnover of up to MNT1.5 billion (approx. \$833,000), and the sectors in which they are active are also defined (Table 1).

**Table 1: Definition of SMEs in Mongolia**

Enterprise Category	Sector	Number of Employees	Annual Turnover in MNT
Small	All sectors	≤ 19 employees	≤ MNT250 million
	Services	≤ 49 employees	≤ MNT1.0 billion
Medium-sized	Wholesale	≤ 149 employees	≤ MNT1.5 billion
	Retail/Manufacturing	≤ 199 employees	≤ MNT1.5 billion

Source: SME Law of Mongolia (2007).

The National Statistical Office (NSO) uses different employee number categorization for the business register database and commercial banks use different definitions for their client segmentation.

The business register of the NSO divides enterprises according to the number of employees they have (Table 2). The NSO’s classification of enterprises is as follows:

**Table 2: Number of Active Companies**

<b>Number of Active Establishment by Employment Size</b>	<b>Business Register, 2018-I</b>	<b>Share of Active Establishments</b>
1–9 employees	69,264	85.5%
10–19 employees	5,212	6.4%
20–49 employees	4,075	5.0%
more than 50 employees	2,467	3.0%
<b>Total</b>	<b>81,018</b>	<b>100.0%</b>

Source: NSO (2019b).

Table 3 shows that there are 69,264 enterprises with one to nine employees and it is the biggest group within this registry. This means most of the companies active in the SME sector have between one and nine employees. In the second biggest group, there are 5,214 enterprises with ten to nineteen employees.

**Table 3: Classification of SMEs (by Employment, by Sector)**

<b>Number of Active Establishment, by Divisions of Economic Activities, by Employment Size Class</b>	<b>1–9 Employees</b>	<b>10–19 Employees</b>	<b>20–49 Employees</b>	<b>More than 50 Employees</b>	<b>Total</b>
Total	69,264.	5,212.	4,075.	2,467.	81,018.
Agriculture, forestry, hunting, and fishery	3,441.	336.	116.	22.	3,915.
Mining and quarrying	493.	95.	80.	109.	777.
Processing industries	5,050.	472.	238.	205.	5,965.
Electricity, gas, and water supply	96.	67.	26.	69.	258.
Construction	5,018.	647.	568.	375.	6,608.
Wholesale and retail trade, repair of motor vehicles, household goods	30,010.	831.	489.	272.	31,602.
Hotels and restaurants	1,947.	238.	120.	51.	2,356.
Transport, storage, and communications	2,574.	169.	139.	127.	3,009.
Financial services	1,099.	41.	29.	24.	1,193.
Real estate, renting, and other business activities	6,820.	469.	324.	219.	7,832.
Public administration and defense, compulsory social security	508.	276.	465.	224.	1,473.
Education services	1,719.	578.	803.	513.	3,613.
Health and social work	2,619.	364.	335.	82.	3,400.
Other community, social and personal service activities	7,846.	629.	343.	175.	8,993.
Extraterritorial organization and bodies	24.				24.

Source: NSO (2019b).

According to the statistical information in Table 3, about 30,010 companies have between one and nine employees and are active in the wholesale and retail sector. The



next biggest group of enterprises are active in other communities, social and personal service activities, the processing industry, and construction.

Most of the employment in the agriculture, forestry, hunting and fishing, and construction sectors is seasonal and informal. Therefore, the numbers shown in Table 3 are not the exact numbers, but only a small subset of them. Also, the samples have to be defined carefully.

According to Zolzaya and Zhou (2018), at the end of 2017, in total 141,500 establishments were registered at the NSO and 75,700 of these were active. Ca. 77% of these active establishments are SMEs and they account for 17.8% of the total GDP and 2.3% of the exports. Some 70% of the economically active population are employed in SMEs, while the Ministry of Agriculture and Light Industry reports that there are about 760,000 people employed in SMEs, which makes up 69% of the total employment. Available statistics on SMEs are inconsistent and fragmented, due to the lack of a unified database on SMEs.

## **2.1 Mongolia's Financial Situation**

After high economic growth years in 2012–2013, the economy faced serious problems in 2015 when the GDP growth declined to 2.5% and was only 1.6% in 2016. Along with the economic boom starting in 2012, government debt also started to rise. In 2015, Mongolia's debt-to-GDP ratio was 62% and at the end of 2016 it had reached 93%.

After the elections of 2016, the new government started negotiating with the IMF, and in 2017, they reached an agreement. Under the Extended Fund Facility program, the IMF and other development partners started providing financial support with \$5.5 billion packages. The EFF of the IMF is a three-year program and will end in 2019.

In order to stabilize the economy in the short term and restructure it in the medium term, the government of Mongolia has undertaken various policies and reform measures under the terms of the agreement. These measures, which have to be taken, are strengthening the fiscal policy to reduce the vulnerability of the boom and bust cycles of the economy and strengthening the financial sector and monetary policy (UNDP 2018).

The macroeconomic environment in Mongolia is not conducive to the development of the manufacturing industry. The real exchange rate has been rising over the last 10 years, depreciating the Mongolian tugrik against major currencies. These relative exchange rate movements have widened Mongolia's cost disadvantage.

In the fourth quarter of 2018, external debt in Mongolia increased to \$28.7 billion, reaching an all-time highest debt amount. The large amount of money that has to be repaid will negatively affect the economy, depleting the resources covering critical government services, including health, social welfare, and education along with financing of SMEs.

## **2.2 Financial Infrastructure**

Mongolia is one of the most sparsely populated countries in the world, which makes traditional banking outside of settlements difficult and costly. The financial sector of Mongolia is dominated by banks, which make up about 96%. There are currently 14 commercial banks in Mongolia. The commercial banks of Mongolia have the biggest infrastructure in the country, with Khan Bank and the State Bank having the biggest networks. Financial and insurance activities (MNT1.67 trillion) contributed 5.2% of GDP (MNT32.2 trillion) in 2018 at current prices.

**Table 4: Structure of the Financial Sector**  
(billion MNT)

	Assets		Profits		Equity	
	Amount	% of	Amount	% of	Amount	% of
2018 Q-2						
Bank	30,259	94.7%	32	36.3%	3,180	74.3%
Nonbank financial institutions	1,144	3.6%	47	52.1%	888	20.8%
Insurance	282	0.9%	6.3	7.1%	127	3.0%
Credit and savings cooperatives	176	0.6%	1.1	1.2%	29	0.7%
Securities market	93	0.3%	3.0	3.4%	56	1.3%

Source: Bank of Mongolia, Financial Regulatory Commission (FRC), 2019.

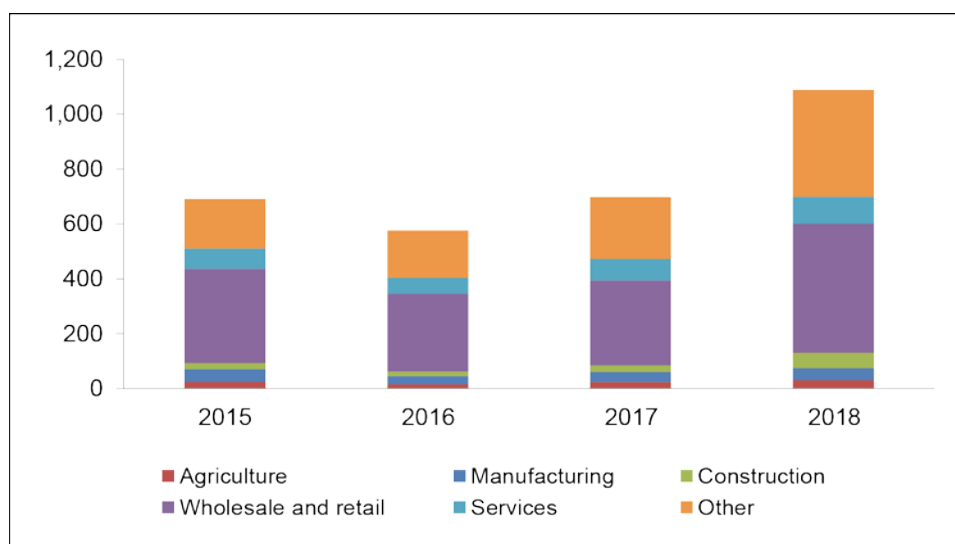
The NBFIs share in the financial system of Mongolia is about 3.6% of total assets. They provide a variety of financial services but most of them are located in Ulaanbaatar and only a few of them are active in rural areas.

According to the FRC, there are about 400 saving and credit cooperatives (SCCs) registered in Mongolia, but only 289 are active. In Ulaanbaatar, there are 186, and in rural areas, there are 103 active. The SCCs have about 61,000 members and less than a 0.5% share in Mongolia’s financial sector.

The total number of outstanding loans issued by banks to SMEs in the last three years was between MNT2.01 trillion and MNT3 trillion, about 17%–19% of total loans. That means that the number of SME loans hasn’t increased dramatically over the last three years. The average interest rate in the last three years was between 17.9% and 19.9%.

Figure 2 shows the loans of individuals issued in different sectors, taken for business purposes. Most loans taken by individuals were taken in the wholesale and retail sector, followed by ‘others’.

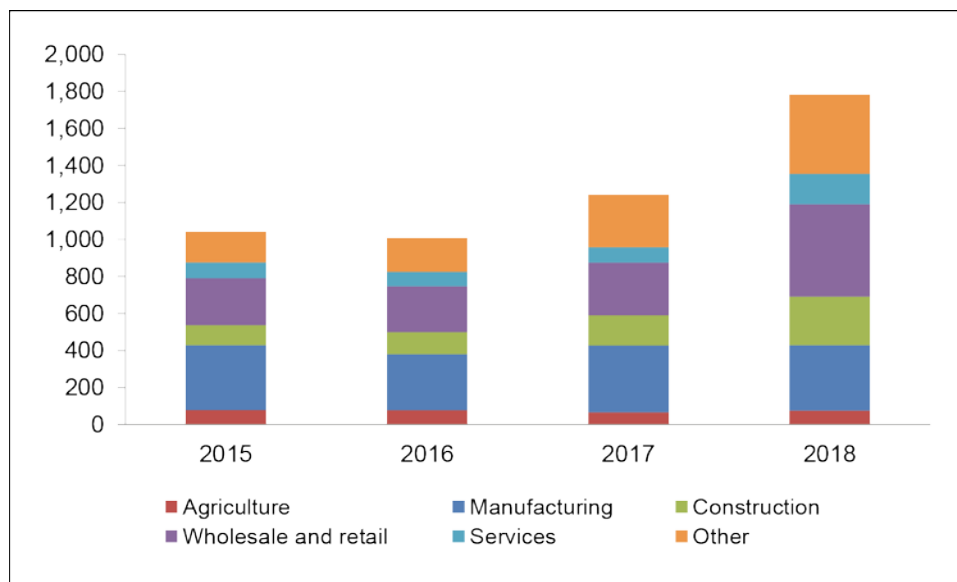
**Figure 2: Outstanding SME Individual Business Loans**  
(billion MNT)



Note: End-year data.  
 Source: Bank of Mongolia (2019).

Figure 3 shows the data of outstanding SME business loans, where the highest loans have been taken by enterprises in the processing industry, with the next biggest group of companies active being in the wholesale and retail sector followed by the manufacturing sector.

**Figure 3: Outstanding SME Business Loans**  
 (billion MNT)



Note: End-year data.  
 Source: Bank of Mongolia (2019).

In 2012, from the Rio+20 Declaration, Mongolia was chosen as one of the seven pilot countries to implement the green strategy. Within this initiative, Mongolia has signed up to the Partnership for Action on Green Economy (PAGE). With the implementation of the PAGE project in Mongolia, different green initiatives were started. The Green Development Policy was adopted by the Parliament on 13 June 2014, which defines green development goals, objectives, and their implementation policy divided into medium and long term. Mongolian government agencies, industry players, and financial institutions met in May 2013 at the first Mongolian Sustainable Finance Forum in Ulaanbaatar to discuss how they can work together towards a green civilization for Mongolia (Mongolia Bank Association 2019). This forum has become an annual event where all major stakeholders of the Mongolian banking industry, including all 14 Mongolian banks, the Mongolian Bankers Association, the Banking and Finance Academy, and government agencies like the Bank of Mongolia and the Ministry of Environment and Tourism, come together to discuss offering sustainable finance. At the first forum, the Mongolian banks declared they would jointly develop the Mongolian Sustainable Finance Principles.

Only XacBank of Mongolia received an accreditation from the Green Climate Fund, on 14 October 2016 (XacBank 2016). On 11 May 2017, they received a \$20 million

financing package. In the first phase, \$500,000 was granted to support micro, small, and medium-sized enterprises finance low-carbon initiatives.<sup>1</sup>

The EBRD and Green Climate Fund cofinanced a program to deliver climate finance through Partner Financial Institutions in developing countries. The focus of the program will be in the areas of energy efficiency, renewable energy, and climate resilience (Green Climate Fund 2017).

Khan Bank and XacBank are the two banks specialized in micro and rural lending. Another financial intermediary that are offering microfinance and are not supervised are pawnshops. Their regulation is covered in different laws, but a special regulation for them does not exist. Therefore, exact numbers or statistics are not available. It is estimated that about 1,500 pawnshops are active and about 350 of them are in Ulaanbaatar. The items that are used as collateral are mostly movable property and are not registered in a unified database. The interest rates are between 3.5% and 15% per week. Many problems occur regarding lending since pawnshop operations are not sufficiently regulated. For instance, when pawnshops sell personal property, which has been used as collateral, at a higher price, they don't return the change to the lenders. Therefore, the responsibility of pawnshops should be increased, and in order to do so, more regulations and a unified database, which registers movable property, are required.

In recent years, microlending possibilities via mobile phone have been developed and become more accessible. Now it has become possible to lend up to MNT2 million immediately using a mobile phone. For instance, the application LEND can be downloaded on a smartphone and offers such loans.

Diversified financing mechanisms are not available for SMEs. Other financing possibilities like venture capital, mezzanine capital, angels, crowdfunding, and crowdlending do not exist.

### **3. STATUS OF FINANCIAL INCLUSION FOR SMES**

Individuals and businesses are able to open an account at a bank and obtain affordable financial products and services. The banks offer a full range of banking products, such as transactions, payments, saving, credit, and insurance. According to the latest 2017 Global Findex survey of the World Bank, about 93% of the adults in Mongolia have an account. Since most payment services, including salaries, pensions, social welfare, payments, and remittances, are distributed through Khan Bank, almost every Mongolian citizen has a Khan Bank account. The Mongolian Bankers Association has stated that Khan Bank has provided its banking services to 2.4 million customers and had 1.7 million card owners and 53,000 corporate customers in 2017 (Khan Bank 2019).

In recent years, the number of mobile phone users has grown fast, which has made Internet banking, especially mobile banking users, grow steadily. Figure 4 shows that the number of Internet banking users almost tripled and the number of mobile banking users doubled from 2015 to 2017.

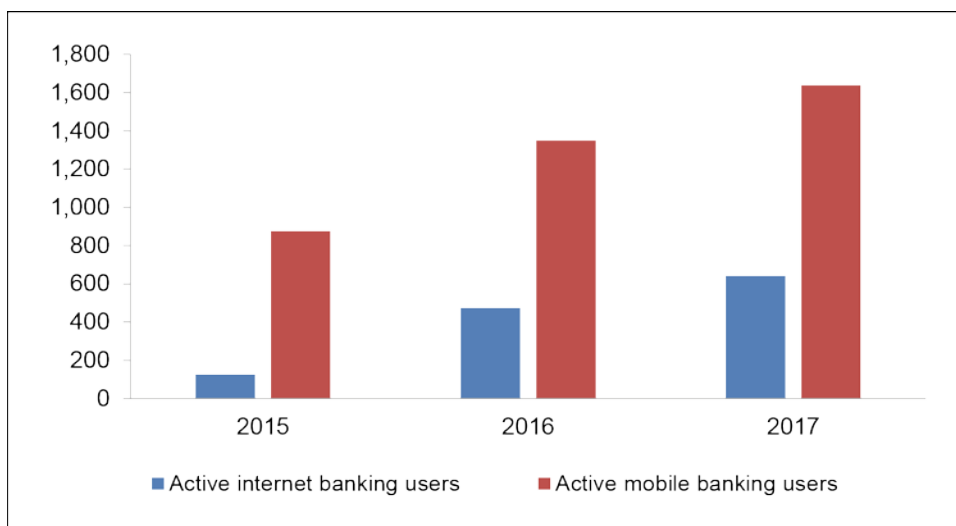
Banks are the main source of funding, but there are also support schemes from the government and IFIs available. The Bank of Mongolia publishes an annual survey, the "Development of SMEs and their financial situation" report, conducted among micro-

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<sup>1</sup> Green Climate Fund (2017).

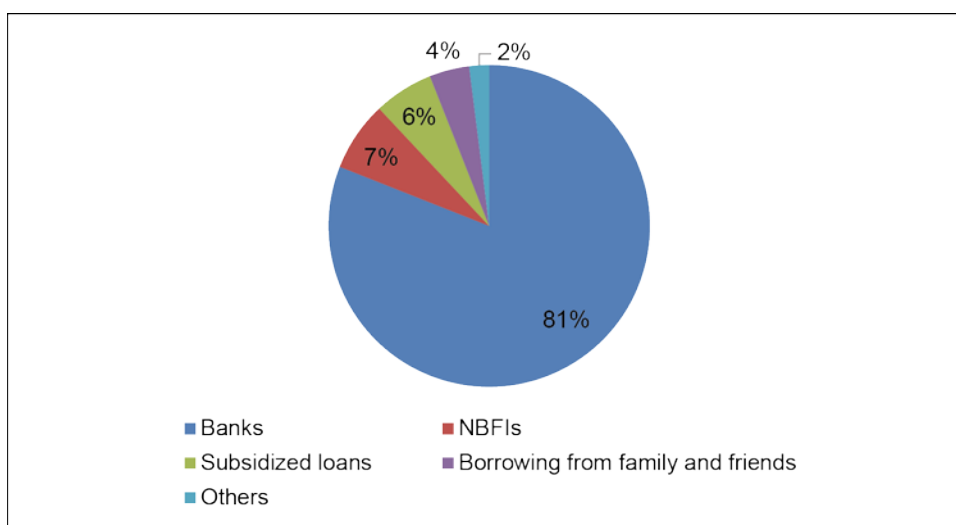
enterprises and SMEs. The objective of the study is to identify the development, operations, and financing situation, and financing issues and challenges faced by SMEs for policymakers. According to the Bank of Mongolia, there are 75,796 SMEs in Mongolia, with 48,519 in Ulaanbaatar and 27,277 in other provinces. According to the Bank of Mongolia, 56% of SMEs have used an external financing instrument for their business expansion. Among those enterprises, 81% have obtained loans from commercial banks, while NBFIs loans and subsidized loans were among the less frequently used financial sources at 7% and 6%, respectively (Figure 5). Also, 4% of SMEs use informal financial sources such as borrowing from family and friends.

**Figure 4: Active Internet and Mobile Banking Users**



Source: Bank of Mongolia (2019).

**Figure 5: SME Financing Sources (%)**



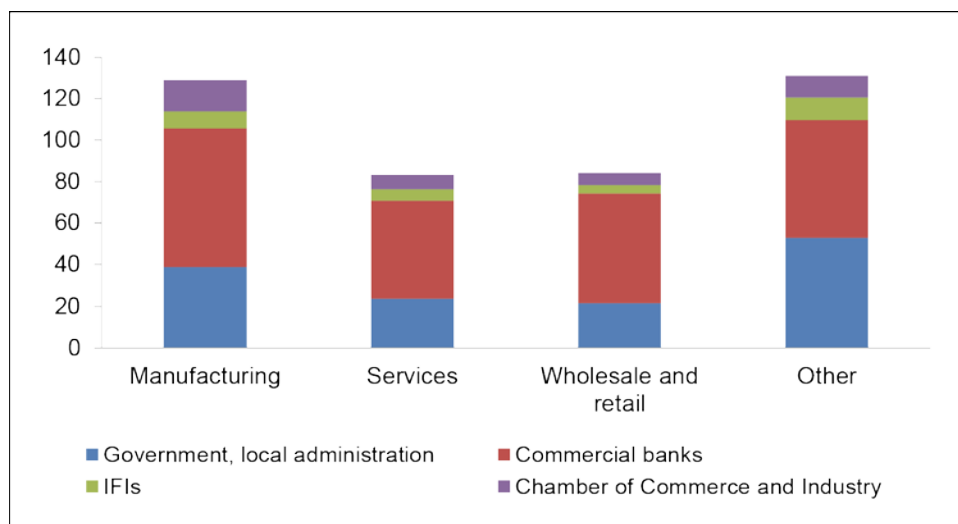
Source: Bank of Mongolia (2017).

The latest report of 2017 shows that SMEs get 53.7% of their financial support from banks, 32.8% from another source of funding, 15.3% from local government or provincial

administration, 13.5% from the government, 12.7% from trade unions, 10% from other financial institutions, 9.5% from NGOs, 7.9% from the Chamber of Commerce and Industry, 7.2% from industry associations, 6.0% from international organizations, and 5.0% from consulting companies. According to the World Bank Global Financial Development Database, 42% of SMEs had a line of credit in 2013.

Figure 6 shows in which sectors and by which organizations SMEs were supported. The commercial banks have provided the most financial support in all sectors.

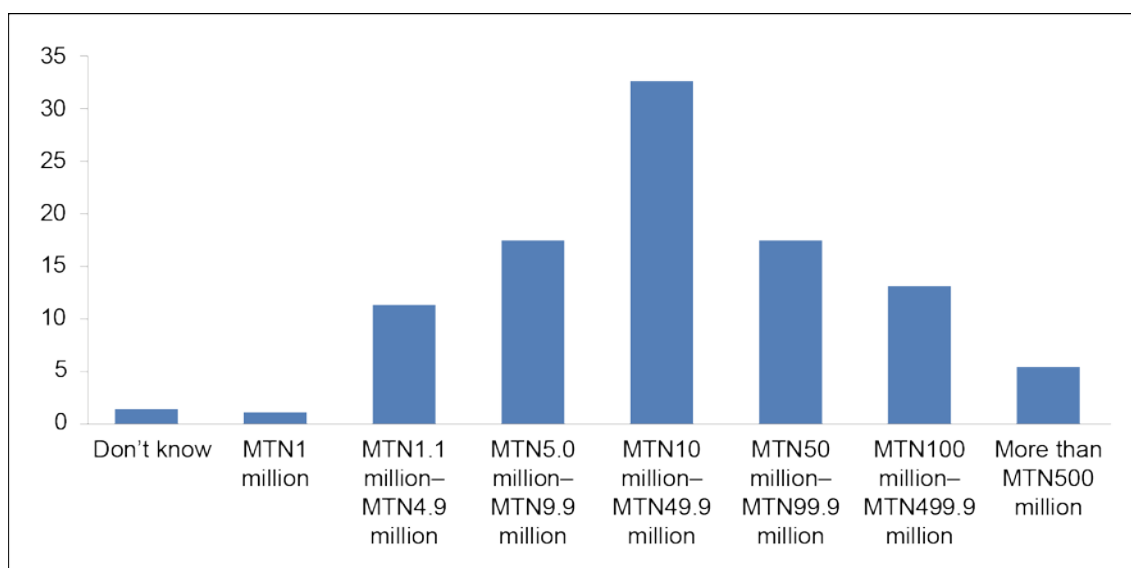
**Figure 6: SME Support from Different Stakeholders (by Sector)**  
(%)



Source: Bank of Mongolia (2017).

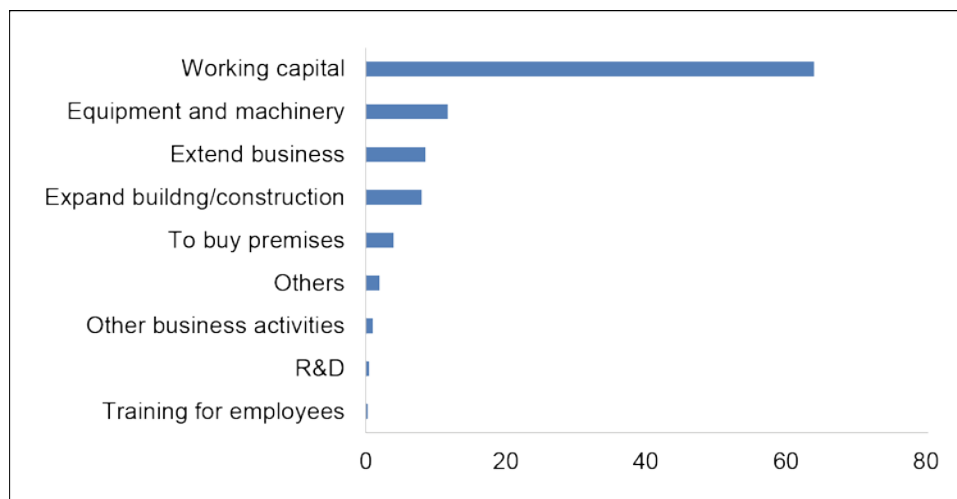
According to the Bank of Mongolia survey (Figure 7), the majority of SMEs need about MNT10 million–MNT49.9 million (about \$3,800–\$18,900). Figure 8 shows that by far the biggest use of credit is for working capital.

**Figure 7: Financial Support Needed**



Source: Bank of Mongolia (2017).

**Figure 8: Funding Expenditure by Type (%)**



Source: Bank of Mongolia (2017).

A credit information service is available at the Central Bank of Mongolia, which only holds information about the amount of credit, while only financial institutions have access to it. For collateral, there is a separate registration system.

## 4. FINANCIAL KNOWLEDGE AND SKILLS OF SME ENTREPRENEURS

### 4.1 Assessments of Financial Literacy

There are different research reports available on SMEs, but not specifically on financial literacy. Most of the banks, the Mongolian National Chamber of Commerce and Industry, and the NGO offer training on financial literacy but no assessment of financial literacy has been carried out. There are also no figures available regarding how many SMEs have taken up such training.

### 4.2 Financial Literacy Programs

The Bank of Mongolia, the Ministry of Finance, the Ministry of Education, Culture and Sport, the Financial Regulatory Commission, the Mongolian Banks Association, the Mongolian Insurers Association, the Savings Insurance Corporation, nonstate organizations operating in the financial sector, and relevant associations and universities have developed a program with the technical support of the World Bank's National midterm program 2016–2021 for financial literacy. The program focuses on four areas:

- a financial literacy program for school children
- financial education for young people
- financial education for rural residents
- financial education through mass communication/media (Bank of Mongolia 2016).



The objectives of the program are: to improve people's financial discipline; to improve their ability to make sound financial decisions; to increase long-term savings and financial investments; to increase people's trust in the banking system; and to promote the long-term and sustainable economic development of the country. No assessment has been carried out. SMEs are not part of this program.

## **5. BARRIERS TO SME FINANCE**

The biggest challenge SMEs are facing is that financial institutions that offer finance to SMEs cannot offer long-term financing and the interest rates are very high. The maximum maturity is 48 months and the average interest rate is 1.5%–2.5% per month. As usual, if an entrepreneur is applying for a loan for the first time, the maximum maturity time is 24 months and the interest rate is the highest. If they have repaid the first loan in time and they apply for a second time they get more favorable conditions.

Most SMEs lack collateral. According OECD (2016), collateral requirements are overly demanding, with the average amount reaching close to 200% of the value of loans in 99.7% of cases, which reflects the deep distrust shown by financial institutions.

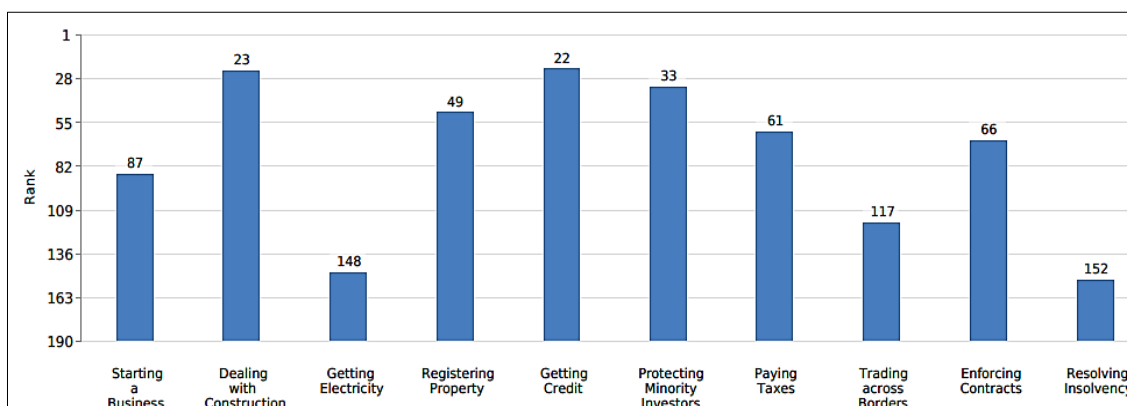
SMEs can't apply for SME funding from the SME Development Fund when they need it. They have to wait until the SME fund is announced. A committee decides which SMEs will get the funding after they receive the projects. The funding of the projects selected will be transferred directly to their bank accounts. The funds have not been used properly since the project selection process has not been transparent. Also, the tender announcement dates have also been unclear. The standing committee of the Parliament is changing the procurement process after some members of parliament misused the funding and approved funding for their own companies.

Access to finance is not sufficient for SMEs. In terms of access to finance, the financial products available are also insufficient. The main source of funding for SMEs are commercial banks, however there is no competition among the banks. The amount of loan, collateral, maturity time, and interest rate offered to SMEs by the banks are similar and show no significant difference.

The mandatory social payments in Mongolia are relatively high. The basic corporate income tax (CIT) rate is 10% for income up to \$1.14 million and the portion of income exceeding that amount is subject to 25% CIT. CIT exemptions apply to business incomes deriving from innovative and environment-friendly technology, and to entities where the majority of employees are disabled. Investors and domestic businesses often point out bureaucratic hurdles and a lack of clarity in the application of tax laws and regulations, particularly with regard to deductible costs and VAT rebates. The government revenues through taxation and state-owned entities remain high. Finally, real interest rates are very high compared to other emerging markets. With this macroeconomic environment, many companies face the following difficulties: high labor costs, high borrowing costs, and low productivity.

### **5.1 Regulatory Framework**

According to the World Bank's Doing Business report (World Bank 2019), Mongolia has been ranked 74th out of 190 economies. The most hindering issues are resolving insolvency (rank 152nd), getting electricity (148th), and trading across borders (117th). The ranking of Mongolia in Doing Business topics is shown in Figure 9.

**Figure 9: Ranking of Mongolia in Doing Business Topics**

Source: World Bank (2019).

In the Doing Business report, investors report that the business registration process in Mongolia is reasonable, efficient, and clear. There is no differentiation between foreign and domestic enterprises. The big issue is the nontransparent, legal, regulatory, and accounting practice.

To be identified as an SME and get funding from the SME Development Fund and other funds, enterprises have to apply for a certificate at the Ministry of Agriculture and Light Industry after registration. The following documents are required for the application:

1. An official letter, which states the sector and direction of activities, specification, official address, telephone number, and email address.
2. A copy of the State Registration Certificate.
3. Attestation from the Social Insurance Department of the district with the total number of insured employees.
4. Attestation from the Tax Department of the district.
5. Confirmed financial statements for the previous year.

The Law on Land was adopted in 1994 and revised in 2002. Within this law, it is possible to own, use, and possess land. A holder of immovable property usually holds two separate certificates: one for the land and one for the building on the land. Having a certificate for land doesn't mean that you are the owner of this land, you only hold possession rights.<sup>2</sup>

The Bankruptcy Law of Mongolia was first adopted in 1997 and since then there have been no amendments. It defines bankruptcy as a civil matter. The bankruptcy process is too vague, onerous, and time-consuming. According to the World Bank's Doing Business report, it takes four years to become bankrupt.

<sup>2</sup> "Owning land means legitimate control and disposing of land.

Possession of a land is the right to use the land oneself or sublease to others. Mongolian citizens and entities have the right to possess land for up to 60 years, to sublease, to transfer with the approval of the land authority, or to pledge it as collateral. Foreign citizens and entities cannot obtain possession rights over land in Mongolia" (IFC 2014).

Family ties still play a significant role, therefore many businesses are established as family businesses or with the support of family members. Business decisions are usually made jointly within the family.

Since the democratic changes in 1990, women have had a high social status in terms of, for example, equality in education and social rights. Since these democratic changes, many women have started their own business and now perform the same jobs as men. The legal framework provides equal rights in inheritance, land use, and ownership of property. The primary caretakers of households and children are women. This is the reason why women's businesses are typically smaller, demonstrate lower turnover rates, and have fewer employees (UNDP 2018).

## 6. STATUS OF DOMESTIC AND GLOBAL VALUE CHAINS IN MONGOLIA

Developing value chains is crucial to enable landlocked countries to overcome the dependency on the mining sector. Overall, value chains can be defined as follows:

*“The value chain describes the full range of activities that firms and workers do to bring a product from its conception to its end use and beyond. This includes activities such as design, production, marketing, distribution, and support to the final consumer. The activities that comprise a value chain can be contained within a single firm or divided among different firms. Value chain activities can produce goods or services and can be contained within a single geographical location or spread over wider areas.”* (Duke University 2019)

*“A set of activities that are performed to design, produce and market, deliver, and support its product”* (Porter 1985)

*“International production, trade, and investments are increasingly organized with so-called ‘global value chains’ (GVCs) where the different stages of the production process are located across different countries..... Global value chains have become a dominant feature of world trade, encompassing developing, emerging, and developed economies. The whole process of producing goods, from raw materials to finished products, is increasingly carried out wherever the necessary skills and materials are available at competitive cost and quality. Similarly, trade in services is essential for the efficient functioning of GVCs, not only because services link activities across countries but also because they help companies to increase the value of their products.”* (OECD 2019)

In order to identify value chains in a country, numerous factors have to be researched, including supply chain and operational factors such as purchase order management, production, distribution, sales orders, management, and so on. Within this paper, three factors of potential value chains are identified:

- Products that have the potential to be exported;
- The majority of raw materials used for the production come from a local source. In other words, the existence of a production supply chain in the country;
- Many people work in this VC.

## 6.1 Manufacturing Sector

Mongolia is the second largest producer of cashmere in the world and produces about 9,500 tons of raw cashmere per year, which makes up 28% of the world production, valued at \$368.2 million in total. It provides income and employment for over a third of the population. In the past, the cashmere industry has received extensive funds, incentives, and technical assistance from the government and international donor organizations.

According to the Cashmere and Wool Association, the availability of raw materials is as follows: cashmere – 8,500 tons; camel wool – 1,400 tons; sheep wool – 25,000 tons; yak molts – 500 tons. Existing manufacturers in the cashmere and wool sector are as follows:<sup>3</sup>

- Manufacturers that produce final products – 15
- Primary processing industry – 23
- Small to medium knitting manufacturers – 58
- Small household manufacturers – over 150

**Table 5: Available (Used) Capacity of Cashmere Production Range**

Washing	Combing	Spinning	Knitting	Weaving
13,000 tons (8,500 tons)	6,500 tons (6,300 tons)	1,350 tons (1,100 tons)	2.8 million units (1.6 million units)	1700 million meters (750 million meters)

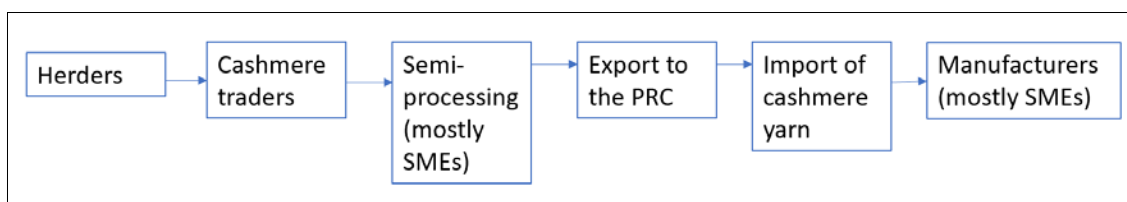
Source: <http://mongoltextile.mn>.

In 2017, there were 9,200 tons washed and 5,400 tons of cashmere exported. According to a study done by the Mongolian National Chamber of Commerce and Industry, the capacity of companies, which is crucial for production, is as follows:

First Stage	Second Stage	Third Stage	Fourth Stage
<ul style="list-style-type: none"> <li>• Washing: 100%</li> </ul>	<ul style="list-style-type: none"> <li>• wool carding: 25% of cashmere needed for production</li> </ul>	<ul style="list-style-type: none"> <li>• Spinning: 15% of cashmere needed for production</li> </ul>	<ul style="list-style-type: none"> <li>• braiding yarn: 10% of cashmere needed for production</li> </ul>

Only a few companies have full capacity until the end of production. Thus, there are two types of value chains—limited capacity (Figure 10) and full capacity (Figure 11):

**Figure 10: Value Chain in Cashmere Sector (Limited Capacity)**

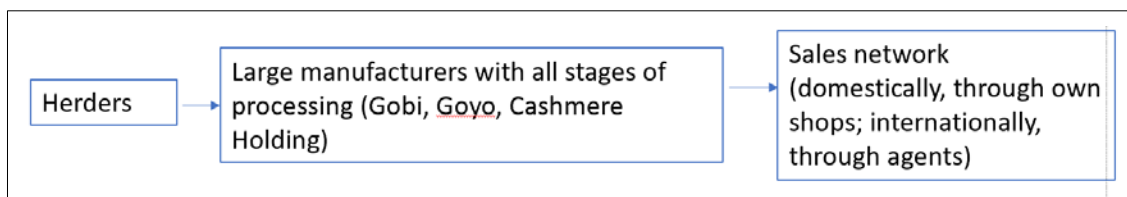


Note: PRC = People's Republic of China.

<sup>3</sup> For information on the Mongolian wool and cashmere sector, see <http://mongoltextile.mn/nav/97> (in Mongolian).

Source: Author.

**Figure 11: Value Chain in Cashmere Sector (Full Capacity)**



Source: Author.

The main export destination countries for wool and cashmere products are the United Kingdom, France, the Republic of Korea, and Japan. Twelve companies exported goods worth \$4.58 million to the UK, 11 companies exported goods worth \$4.87 million to France, 11 companies exported goods worth \$5.56 million to Japan, and 26 companies exported goods worth \$7.23 million to the Republic of Korea in 2017 (Mongolian Wool and Cashmere Association 2018).

The biggest company in this sector is Gobi Cashmere. Gobi Cashmere was established in 1981 with investment from Japan and was privatized in July 2007. Since then it has been restructured and become a joint stock company. In December 2017, it bought Goyo Cashmere LLC, which was one of the first factories established with private investment in 1993 and one of the biggest. Gobi Cashmere and Goyo Cashmere LLC have a monopoly position in the Mongolian cashmere market, owning more than 70%, and they are part of the Tavan Bogd Group. Gobi Cashmere and Goyo Cashmere are also factories that have a full production range, from washing to wool carding, spinning and knitting, braiding yarn, and final products. They sell their products in 19 countries.

The second biggest cashmere producer, Cashmere Holding, was established in 1994 with the joint investment of a Mongolian company, Altai Holding, and a British company, D.B. Holdsworth. D.B. Holdsworth had owned 30% of the shares until 2006 when Altai Holding LLC bought back the shares and became the full owner.

Companies that operate in the Mongolian cashmere sector face various challenges:

- The biggest challenge is that the People's Republic of China (PRC) causes price dumping of raw cashmere in the world market. Chinese companies also cause raw cashmere price hikes within the country when trying to buy Mongolian cashmere. As a result, the price of raw cashmere increases every year, burdening the local companies. As a countermeasure, the Mongolian government gives subsidies in order to get the herders to sell their raw cashmere to domestic companies. For example, government subsidies amounted to MNT22.6 billion in 2016 and MNT22.5 billion in 2017.
- The availability of raw cashmere is highly seasonal and possible only in spring, therefore companies need a huge amount of current assets. Furthermore, sufficient storage is required to accumulate enough raw cashmere.
- Big companies are interested in having a full production range, including washing and wool carding.
- One corporation has a monopoly position in the cashmere sector, due to insufficient regulations on fair competition. As a result, Mongolian SMEs will find it difficult to develop further.

- The fact that herders pay no taxes affects the quality of raw cashmere. There's also no tax on each livestock, which causes excessive pasture carrying capacity and degradation of grazing areas. In recent years, the problems concerning the pastureland in Mongolia have been discussed a lot.

The two biggest cashmere companies, which have a monopoly position in the cashmere sector with over 70% of the domestic market share, belong to one company group, which owns a bank as well. The fact that the two biggest companies have created a monopoly position in the cashmere sector and a bank operates under the same group makes it doubtful whether principles of fair competition apply in the Mongolian cashmere sector.

**Table 6: SWOT Analysis for the Wool and Cashmere Sector**

<b>Strengths</b>	<b>Weaknesses</b>
<ul style="list-style-type: none"> <li>• With natural breeding the quality of cashmere is without chemicals and treatments.</li> <li>• Government programs, IFIs, and other companies are supporting in-country value-added cashmere processing.</li> <li>• Relatively cheaper than other wool and cashmere products in the world market.</li> <li>• Mongolian wool and cashmere are durable and easily refreshed.</li> <li>• Some brands already have representative offices and sales agents abroad and are well-known in the world market.</li> </ul>	<ul style="list-style-type: none"> <li>• High cost of the working capital needed to purchase stocks of raw cashmere due to the availability of raw cashmere for a certain time of period. The producers have to buy the stock in the spring for the whole year.</li> <li>• Inconsistent and uneven quality (as reflected in the price) of the raw materials, due to decreased fiber quality depending on age of goats.</li> <li>• Price competition of traders.</li> <li>• Highly seasonal with availability of raw cashmere only for a certain period.</li> <li>• Exchange rates, especially the depreciation of the national currency, make the products too cheap.</li> <li>• The quality is declining due to the substantial subsidies from the government such as no taxation for herders, free medical care, no pension, health, or disability contributions. If the cashmere quality (as measured by fiber diameters) increases, the average yield per goat declines.</li> <li>• Most cashmere is exported with only low value added.</li> </ul>
<b>Opportunities</b>	<b>Threats</b>
<ul style="list-style-type: none"> <li>• Demand for, and interest in, ecologically pure, naturally made products are increasing worldwide.</li> <li>• In Europe, Scandinavia, and North America, the market for wool and cashmere products can be expanded, considering the cold, humid climate and higher living standards.</li> </ul>	<ul style="list-style-type: none"> <li>• Mongolia could face big competition from the largest producer of raw cashmere, the PRC. Since the Chinese government has subsidized its cashmere sector with very low interest rates and other programs, the PRC could potentially dominate.</li> <li>• About half of Mongolia's raw cashmere is smuggled to the PRC for processing.</li> <li>• Price dumping.</li> <li>• Natural disasters such as dzuds could cause a shortage or even a loss of raw materials.</li> <li>• Ecological imbalance and deterioration in pastureland, due to high growth of goat herds.</li> <li>• Degraded cashmere quality due to the rapid growth of the industry.</li> </ul>

Source: Author.

## 6.2 Agricultural Sector

The Integrated Mineral Resource Initiative is a GIZ project in Mongolia that is implemented in four provinces/aimags. Within this project, there has been a value chain analysis of fruit and vegetables.

The main export destination countries are Japan, the Republic of Korea, and Singapore, and companies like Seaberry, UFC, Goo, and Lhamour have become relatively well-known in the world market. The bigger companies are actively involved in improving the quality of production. Currently, the “Fruit and Berries” national program is being implemented to develop the sector. One of the main products is sea buckthorn (Figure 16).

There are a total of 54 SMEs processing raw materials and producing final products such as juice, oil, and wine in 14 sums of 10 aimags and six districts of the capital city of Mongolia. Factories have two to 50 employees and there are 595 people employed. The factories are capable of processing 500–600 tons of berries yearly, but most of them use only 3.3%–50% of their capacities. Currently, 2,041 tons of sea buckthorn are processed on average (MOFA 2017).

The fruit and berries sector in Mongolia has a good base to be developed as a value chain, but it requires a long-term development strategy and financial support to develop new technology and products with appropriate standards.

There are a number of problems that occur along the value chain pathway in the fruit and berries sector.

Ingredients and cultivars must remain the same in order to maintain a certain standard and quality of products. The biggest problem is the uncertainty concerning the cultivars of sea buckthorn. The most suitable and adaptable cultivars in the Mongolian climate have not been identified yet. Furthermore, human resources are one of the biggest challenges, since big companies or unions need an agronomist and there’s a need to prepare experts and specialized people in this sector. There are approximately 40 factories operating in the sector nationwide, and for these factories, advancement in technologies and access to financing are crucial. For instance, ca. 30%–40% of the total harvests are lost during the process of harvesting due to the lack of technologies, since the berries are tightly bunched along the branches, and the harvesting of sea buckthorn is very difficult and requires certain equipment. Therefore, technologies such as harvesting equipment are important, since harvesting requires manual labor. In the future, the production of sea buckthorn should be automated.

There is a need to cooperate with national and international research organizations in order to improve this sector.

Long-term financing is required, because sea buckthorn starts bearing fruit three to five years after planting. To date, there have been no attempts to attract foreign investments in this sector, which should be considered in the future.

In total, 6,000 ha have been cultivated and 3,000 tons of fruit and berries have been harvested. Various big companies, including Khaan Jims, Kharkhorin, and Tovkhin Jims, have been operating in this sector. There are also many sea buckthorn farming households as a result of the implementation of the “Chatsargana” project. For instance, in 2017 the Mongolian government provided an area of 10 ha with infrastructure such as fences and watering systems in each sum of Bulgan province. One household gets an area of 1–2 ha to share with others. The production of sea buckthorn can be developed further following this example.

**Table 7: SWOT Analysis for the Fruit and Berries Sector**

Strengths	Weaknesses
<ul style="list-style-type: none"> <li>• Endemic berries are well adapted to the harsh Mongolian climate.</li> <li>• They are widely used in organic beauty and treatment products due to their many medicinal properties, including biological active substances, vitamins, and mineral elements.</li> <li>• They can be processed into various kinds of products, including food like organic juice, oil, beauty and medicinal products, and so on.</li> <li>• Sea buckthorn is a specific product of Mongolia.</li> <li>• Various sea buckthorn-related researches have been carried out so far and this could be a good base for the further development of the sector.</li> <li>• Because of its extensive root system, sea buckthorn mitigates against desertification and is resistant in drought, which makes it suitable for growing in dry areas like western Mongolia.</li> </ul>	<ul style="list-style-type: none"> <li>• Only a third of sea buckthorn berries are harvested, due to the lack of technology and equipment.</li> <li>• The supply of raw materials is seasonal, thus scarcity could potentially occur.</li> <li>• Lack of knowledge and know-how about sapling varieties could be an issue for the cultivation of sea buckthorn.</li> <li>• There is a small variety of fruit and berries available.</li> <li>• The equipment and technologies used on most farms are ineffective and cause a loss of yield.</li> </ul>
Opportunities	Threats
<ul style="list-style-type: none"> <li>• The vast expanses of area where the fruit and berries can be cultivated.</li> <li>• There is a great opportunity to further develop organic fruit and berry products, since the global tendency to use organic/eco-products has been increasing.</li> <li>• The infection rate of diseases of the sapling is low.</li> </ul>	<ul style="list-style-type: none"> <li>• Mongolia has 66 million livestock, thus bigger plantations of fruits and berries must be protected with wire fencing from animals and birds, which requires a certain amount of investment. The PRC is presumably the biggest producer and exporter of sea buckthorn in the world, since most of the suppliers of sea buckthorn post on <a href="http://www.alibaba.com">www.alibaba.com</a> and <a href="http://www.zauba.com">www.zauba.com</a>. This may prevent Mongolia from expanding its sea buckthorn exports.</li> </ul>

Source: Author.

### 6.3 Service Sector

The tourism sector is one of the priority sectors of Mongolia. According to the National Tourism Association, there are 600 companies (tour operators) registered, with 280 active and 300 tourist camps operating. Mongolia has visa-free regimes with 42 countries to attract more tourists.

Although Mongolia was the host country of ITB 2015, the target to receive one million tourists by 2016–2017 couldn't be reached. The main reason was that there was no additional infrastructural development carried out within the country, such as increasing the number of flights to and within Mongolia. The tourist companies of Mongolia are part of the global value chains. They have contracts with international companies offering their tours through their network.

According to the World Travel and Tourism Council (WTTC 2019), the total contribution of tourism to GDP (including wider effects of investments, government spending, supply chain, and induced income impacts) was MNT3,774.9 billion or 11.8% of GDP, while the direct contribution of tourism to GDP amounted to MNT1,296.8 billion or 4.1% of GDP (rank 110th) in 2017. Thus, the total contribution of the tourism sector to GDP is nearly three times greater than its direct contribution.



Including the jobs indirectly supported by the sector, tourism accounted for 133,800 jobs and represents 11% of total employment.

**Table 8: SWOT Analysis for the Tourism Sector**

<b>Strengths</b>	<b>Weaknesses</b>
<ul style="list-style-type: none"> <li>• The extensive lakes, rivers, streams, and ponds abound with fish and other wildlife and have the potential to attract nature-based and more specifically eco-tourists.</li> <li>• The Gobi Desert located to the south of the region enjoys its own special tourist attractions and has extensive potential.</li> <li>• A number of historic city sites offer potential if properly protected, signed, and interpreted.</li> <li>• Genghis Khan is well-known worldwide and offers much interest to overseas visitors to the region. Marco Polo is also associated with this area and therefore provides a link with Europe, which increases the potential European interest.</li> </ul>	<ul style="list-style-type: none"> <li>• Infrastructure not improved, such as additional international flights, domestic flights, railways etc.</li> <li>• Air market not liberalized therefore expensive.</li> <li>• There is limited accommodation and much of the accommodation is not of international standard as yet.</li> <li>• There are few medical aid centers and emergency services available in rural areas.</li> <li>• There is relatively little to purchase, especially in the tourism and interpretation centers, such as food, beverages, postcards, books, guidebooks, souvenirs, and the like.</li> <li>• Greater levels of interpretation will be needed and more interpretation centres must be built, especially at sites such as those occupied by ancient cities.</li> <li>• Signage must be improved and appropriate environmental standards used.</li> <li>• Although there is little one can do about the climate, it should be recognized that the long, cold winters will make much of the tourism activity highly seasonal with consequent periods of little demand for resources and infrastructure.</li> </ul>
<b>Opportunities</b>	<b>Threats</b>
<ul style="list-style-type: none"> <li>• The vast expanses of forest, grassland and desert are barely being tapped at present and there are terrific opportunities to develop many more tourist attractions in the future.</li> <li>• Whilst Mongolia is a relatively isolated region of the world, it is that very isolation that gives the region much of its attraction.</li> <li>• Much of the tourism product is based on natural and cultural attractions and it is these types of attraction that are in high demand by international tourists. Nature-based and eco-tourism-based attractions and products are experiencing rapid growth in demand worldwide.</li> <li>• Cultural attractions are probably in even greater demand than natural attractions and there is great opportunity to further develop the cultural attractions in the region.</li> <li>• Winter sports, winter tourism, and adventure tourism, in general, have been identified as a potential growth market and there are a lot of opportunities to develop this sector a lot further.</li> </ul>	<ul style="list-style-type: none"> <li>• The very nature of both desert and grassland landscapes makes any form of development highly conspicuous and there is a great danger of poor or inappropriate development ruining the scenic appeal of much of the area.</li> <li>• Care must be exercised to ensure that pollution does not detract from the relatively pollution-free environment that exists at the moment.</li> <li>• Tourism is not the only industry in the region and care must be exercised to ensure that other industries, especially extractive industries, are not allowed to ruin the tourism resource of the region.</li> <li>• There is great faith around the world that if one develops eco-tourism all will be well and little harm can occur in the natural environment. There is no guarantee that eco-tourism will be benign and as eco-tourism occurs in some of the world's most sensitive places the potential risk to the environment is enormous. This holds true to Mongolia.</li> </ul>

Sources: 1. Lkhalkham, Nomin, Onon, and Khaliuna (2018).

2. ADB (2002).

Due to the high volatility of the Mongolian tugrik the tourist companies have to calculate their prices very carefully. Foreign tourists usually book and pay for their tours at least six months before, therefore the fluctuation of the tugrik against the US dollar can be a big risk.

The tourism sector is seasonal due to the very cold and harsh winters in Mongolia. The tourist season is from June to September each year. Special programs such as winter or adventure tourism need to be developed to prolong the season.

- It is impossible to develop the tourism in Mongolia as mass tourism, because only a few people with specific interests come to Mongolia and traveling costs are high. The tourism sector faces many other challenges as well.
- Due to the underdeveloped infrastructure, there are only domestic flights to a few provinces. Furthermore, the flights are relatively expensive.
- Another weakness is that the healthcare infrastructure is poor. In the case of an accident or illness in the countryside, the injured person needs to be transported to a city, where advanced healthcare is provided and this takes time.
- In recent years, travelers riding in their vehicles have come to Mongolia through the Russian Federation. But, due to the poor road infrastructure, there are not enough traffic signs. Thus travelers are usually unaware of the distance to the next filling station or directions.

## **7. VALUE CHAIN FINANCING ANALYSIS**

The limited access to the finance the SMEs of Mongolia need hinders them in terms of creating jobs, economic growth, and further developing their business. There are no value chain financing mechanisms available. The bank-dominated financial sector of Mongolia offers loans, and deposit and saving products. There is a need to develop venture capital, factoring, leasing, overdraft facilities, start-up finance, and other finance mechanisms.

There are no financial incentives for exporters.

## **8. POLICIES TO PROMOTE SME FINANCE**

There are different laws and programs available to support the development of SMEs. A credit risk database is available at the Bank of Mongolia, but only banks have access to this database. Some of the important and relevant laws and programs are listed below.

The Government of Mongolia has established different funds to provide financial support for SMEs. The following funds are available for SMEs (Table 10).

The SME Development Fund was established to support financing for SMEs by providing long-term concessional loans for SME operations, allowing SMEs to access production equipment through financial leasing, offering double guarantees for SMEs and promoting activities of subsidized SMEs, organizing workshops and training and operating from the Ministry of Food, Agriculture and Light Industry. In the period from 2009 to 2017 the SME Development Fund received 26,454 applications. Only 18% or 7,536 were approved and they received a total funding of MNT835.2 billion in concessional loans, or 4.3%–6.5% of total SME finance. But the government structure supporting SMEs including the

SMEDF was not sustainable in the past. For instance, the SME fund has operated under different ministries: From 2012 to 2014 it operated under the Ministry of Economic Development, from 2014 to 2016 under the Ministry of Industry, and from 2016 under the Ministry of Agriculture and Light Industry. The Ministry of Economic Development was dissolved in 2014 and the Ministry of Industry in 2016. Therefore, a long-term development strategy for SMEs is not available.

**Table 9: Laws and Policies to Promote SME Finance**

	<b>Year Introduced/ Ministry in Charge</b>	<b>Objectives</b>	<b>Short Assessment</b>
<b>Law</b>			
Law on SMEs	2007	First-time definition of SMEs.	The definition of SMEs is not widely used by SME stakeholders. The business register of the NSO has another client segmentation and also banks use their own definition.
Law on exemptions of customs duties and VAT on equipment and spare parts imported for the purpose of increasing employment, substitution of imports and export-oriented products for SME.	2009, 2014, 2017	The list of equipment to be released under these laws was approved by the government of Mongolia's resolution No. 191 in 2014 and No. 168 in 2017, respectively.	Were very effective in developing the manufacturing sector in Mongolia. But the list of equipment released was only effective till the end of 2018.
<b>Policy</b>			
SME program 2018–2020	Ministry of Light Industry and Agriculture	<ol style="list-style-type: none"> <li>1. Within the scope of the activities of the government: Improve the legal environment, support new technologies, encourage bilateral trade and investment cooperation.</li> <li>2. Within the scope of nongovernmental organizations: Create linkages between new markets, between large and small businesses, and management networks for value chain and sales. Inform and promote government policies and decisions, scientific achievements, and advanced technologies.</li> <li>3. Within the scope of business: Capacity building of human resources, increasing capital and savings, improve internal controls, risk assessment, market capacity, and pricing. Focus on export orientation.</li> </ol>	This policy is only on paper, no implementation so far. In the program, there are no monitoring activities and timelines, involvement, and the role of other ministries and agencies are planned.

Export promotion program	Ministry of Foreign Affairs	1. Creation of a favorable, sustainable export environment. 2. Diversification of export. 3. Improve quality and simplify trade and expand the export market and access.	No assessment has been done until yet.
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Source: Author.

**Table 10: Available Funds for SMEs**

	Requirements	Terms	Partners	Development Plans
SME Development Fund	Business project; Number of employees without contracts 199; Operation more than 1 year; No outstanding loans; Advanced technology implemented without adverse impact on environment and technology	4 years, interest rate 5%, min loan: MNT30 million	Fully supported from budget	No information available
Credit Guarantee Fund	Business projects; Certificate; No bad credit history; Operation more than 1 year; With certain income	Long term (10 years) Low interest rate (12%)	ADB	Additional products planned: women, eco-business and start-up
Employment Creation Fund	Unemployed citizens registered at the Labor Office; Living in the community for 3 months; Self-employed; No bad credit history	For individuals MNT2 million; for herders, individuals establishing partnership cooperatives up to MNT5 million; for individuals establishing cooperatives up to MNT10 million for 2 years, interest rate 0.85%/month	Fully supported from budget	No information available

Source: SMEDF (2019), CGF (2019).

**Table 7: Average Funding for a Project from the SME Development Fund**

	2009	2010	2011	2012	2013	2014	2015	2016	2017
Average funding amount per project (million MNT)	24.3	25.2	158.4	381.8	147.9	155.2	150.8	425.5	324.7

Source: SMEDF (2019).

**Table 8: Projects Implemented by Sector (2009–2017)**

Sectors	Number of Projects	Expansion of Production	New Factory
Light industry	2,095	443	129
Food production	1,081	243	88
Farming	752	243	88

Animal husbandry	1,158	443	129
Warehouse	122	25	18
Nonmetallic (manufacture of minerals)	657	213	101
Soap, disinfection	48	13	8
Waste	10	8	2
Trade and services	911	161	77
Processing factory	28	22	6
Other	674	102	65

Source: SMEDF (2019).

From 2013 to 2018, MNT76.8 billion for 646 guaranteed credits worth MNT164.4 billion were granted by the Credit Guarantee Fund (CGF 2019). Currently, MNT37.3 billion for 111 guaranteed credits have been granted: 84 of these guarantees were issued in Ulaanbaatar, and 27 in local areas. Financed by foreign credits and grants, no subsidiaries from the budget.

The CGF is located only in Ulaanbaatar. They cooperate with five commercial banks. If the collateral of an SME is not enough to get the credit they can apply for a credit guarantee. The usual process is that they have to apply for it at their local bank and the bank submits the application to the CGF. The CGF studies the application and documents submitted. When the CGF approves the application, the bank examines the submitted documents carefully. The final decision is made by the credit committee of the bank.

## 9. CONCLUSIONS AND RECOMMENDATIONS

The main source of funding for SMEs is commercial banks. Loan guarantees are used by the government to ease SMEs' access to finance. Some funds have been established to support the development of SMEs.

Access to finance and a lack of collateral are important issues for SMEs. The cost of financing is very high and there are insufficient support and subsidies from government agencies. The banking system offers very basic and traditional financing mechanisms, a lack of value chain financing, and other risk mechanisms for the exchange rate.

Studies on the financial literacy of SMEs have not been conducted yet. Therefore it is difficult to assess the financial education of SMEs.

Thus, the following recommendations can be formulated.

1. A proper definition of SMEs is needed with changes to the law. If not, the funding from the SME Development Fund and others will be misused in the long term.
2. A unified database for SMEs is needed in order to obtain accurate statistics and develop effective policy measures, and a credit risk database is necessary to overcome the problem of information asymmetry faced by SMEs.
3. Studies on the financial literacy of SMEs are needed to identify their real needs and a national financial literacy strategy should be developed. Such studies should be carried out on a regular base to identify their development and to develop focused products for them.

4. Expansion of the credit guarantee system through special programs for women, people with disabilities, etc.
5. Improvement of the Bankruptcy Law is needed.
6. Implementation of the SME program 2018–2020.
7. The banks should make value collaterals by themselves. The appraisal of collaterals has to be done by independent valuation companies. Thus, such regulation is needed.
8. Exploring the possibilities of developing alternatives to bank lending, and in particular diversifying the financial sector, such as venture capital, business angel investment, mezzanine financing, crowdfunding, leasing, factoring, and green financing. Development of the regulatory framework to operate for them.
9. Developing programs for the development and finance of value chains based on studies on them.
10. Improving the environment for fair competition through the improvement of Competition Law and environment.
11. Prolonging the period and extending the list of equipment under the Law on exemption of customs duties and VAT on equipment and spare parts.
12. A business voice in the design and implementation of border procedures is needed.
13. Tourism companies should cooperate with local manufacturers and promote their products by advertising them.

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