

440 new stocks to be offered. Any buyers?

On one corner of Ulaanbaatar's main square, there is a grand old building painted in flaking orange and white. It used to be a children's cinema screening Mickey Mouse, Mongolian and Russian cartoons. These days it is the national stock exchange.

Although the movies are no more, the scenes inside are just as fantastic. Beyond the glass revolving doors, computer banks line the marble floors in the trading room. In the centre, high above the stock price board, clocks show the times in London, Moscow and New York. Nor is it just the trading room that buzzes with technology, complete with systems for scripless settlement. Since the opening of the exchange in February 1992, brokers have been connected by modem link to offices in every province in the country.

"This is the best designed capital market in the world," says Naidansurengiin Zolzhargal, stock exchange chairman and chief executive, whose idea first sparked the market back in 1991. "It is a huge achievement."

The exchange's many critics feel otherwise. Some say its gleaming white interior and whirring technology bear no relevance to a country stymied by years of waste and poverty, where livestock outnumber people 10 to one, and where half the population lives in tents, known as yuts. "It's like a James Bond movie," says one foreign consultant. "And they are paying for it." More seriously, market regulators, officials, and international aid donors disagree on the exchange's regulations. "A handful of traders don't need a stock exchange," says one IMF official. "What they need is a bar, an arbiter, a government representative and a couple of entrepreneurs."

Secondary market trading was to have begun in early 1994, but has been held back by delays in implementing a Securities Act. The long-promised Securities Law of Mongo-

One of the world's poorest countries, Mongolia is one of the latest capitalist converts to jump on the stockmarket bandwagon. Its supporters herald the new exchange as a symbol of progressive capitalism; its critics say it is pure fantasy

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lia was finally passed in September, but required a Securities and Exchange Commission to act as a supreme body. Now the stockmarket board is up and running, but its members are demanding changes in the rules and the appointment of outside advisers.

Still, Zolzhargal and the heads of Mongolia's 29 stockbroking firms may now lay claim to some success. Since Mongolia launched its privatization programme in May 1990, some 440 state companies have been returned to the private sector. (Each Mongolian received vouchers, which were swapped for shares in companies auctioned off on the exchange.) But Solzhargal thinks privatization is only the first step; secondary market trading is needed to attract risk capital that will finance new private enterprises and further motivate workers and managers to make a profit.

Indeed, analysts agree Mongolia needs a market where share consolidation can take place. What they don't agree on is how big it should be and what rules should govern it.

The new securities law, which was drawn up with ADB support, has caused disagreement as it is based on a developed-country perspective. It has 26 articles with over 115 provisions (ranging from the right of brokers to set up mutual funds to quorums for shareholder meetings). It requires annual financial statements of the past three years and six monthly profit-and-loss statements, audited by a certified public accountant. The problem is that Mongolia has few accountants; most companies do not keep accounts. "Half of them don't have a clue what a quarterly statement is," says a foreign adviser. "They don't have financial statements available, let alone audited accounts." Says another consultant: "Instead of enshrining complicated laws, the ADB should simply have entrusted the stockmarket board to bring out simple administrative rules. There's no need for all this."

The seeds of the stock exchange were sewn

by the collapse of the Soviet Union, Mongolia's former patron and main trading partner. In 1991, Mongolia's GDP fell 9.2%; inflation soared more than 120%. The mess paved the way for the country's first free elections, Mongolia's membership of the IMF, and a radical privatization programme pushed by a group of young economists. Privatization led to the idea of a stock exchange and a secondary market. "The idea was my own," says Zolzhargal, a former member of the government privatization commission and director of the Bank of Mongolia, the central bank. "Creating a capital market was vital to privatization."

Zolzhargal, who had neither the money nor the allies to realize his dream, teamed up with the well-known economist and Harvard professor, Jeffrey Sachs, whom he met at the annual meeting of the World Economic Forum in Davos, Switzerland. Sachs arranged for six or seven of his graduates to be sent to Mongolia to train local brokers. Hong Kong-based International Securities Consultants, the ADB, and the Financial Service Volunteer Corp of the US were given key advisory roles. Hence, in June 1991, the old children's cinema building in Ulaanbaatar was acquired with government funds and refurbished at a cost of US\$3 million. The computers were financed by the Asian Development Bank; the software was developed in-

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house. "It was very important to give people trust," says Zolzhargal. "This could not be an old communist building. It is like a church. It had to be nice and different."

Still, Mongolia's leap into the modern world has not come without problems. At the end of 1991, shortly after its transition to a free-market economy, young foreign exchange traders lost millions of dollars when futures trades

went wrong, almost wiping out Mongolia's forex reserves. It also cost the job of Zolzhargal's brother, then governor of the Mongol Bank. "This was the concept of private initiative and it just got out of proportion," explains an IMF official "There are still fantasies of building big things and getting rich quickly."

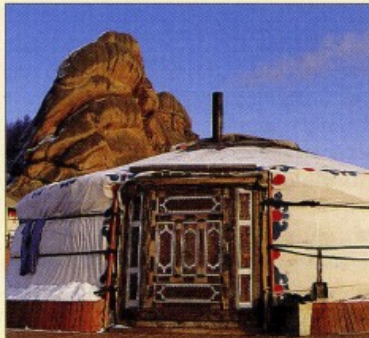
The IMF would have nothing to do with the stock exchange, but Zolzhargal disagrees. "These people understand figures," he says. "But they have no imagination." He has many sympathizers: brokers who have attended courses from Harvard University graduates, ADB consultants, and the Hong Kong-based International Financial Service and Financial Service Volunteer Corp have nothing but praise for the exchange, the software and the paperless trading. "This is part of history," says Erdene-Od, who joined the stock exchange after completing military service and is awaiting the

Yuppie on the steppes

He has got long hair and wears a black leather jacket. In most countries he would be taken for a motorbike courier. He is a Mongolian stockbroker.

Since joining stock exchange member firm Delger Hangay in December 1991, Tserendash has undergone a crash course in economics and survival. "When the stock exchange started I was not so sure what it was," he says. "Now I have read many books and believe it is very important."

The Mongolian Stock Exchange has 28 other member broking firms and over 300 brokers and traders like Tserendash. They are all connected to offices outside Ulaanbaatar by computer links and modems. Most of them were attracted by the promise of a high-profile financial career; others by the high salary. And since completing the two-month



stock exchange training courses given by the consultants of Harvard University, the Asian Development Bank and the International Financial Service, they have become more at ease talking about valuations and price/earnings ratios. "There are many companies on a p/e of one, but some are as high as four or five," Tserendash explains from the exchange's second-floor conference room lit up by spot lights.

Still, working out which stocks to buy in Mongolia could be difficult given the poor accounting and limited research. But Tserendash has picked out his own winners. "I recommend travel

enterprises like Zhulchin, which has many hotels and is very profitable," he says. "And I like telecommunications and infrastructure companies," he adds, referring to companies which may be sold to the private sector in the next batch of cash privatizations.

Other dealers have their favourites. And Naidansurenliin Zolzhargal, chairman and chief executive of the Mongolian Stock Exchange, is prepared to point investors in the right direction. "Of course the biggest companies like Gobi and Erdenet Copper will be profitable when they are listed," says Erdene-Od, a dealer from the far-flung province of Khentii. "You will get a high return in tourism, in leather processing and in mineral resources," says Zolzhargal.

For now, Mongolia's brokers are unlikely to make a pile from their commissions. But longer term, those with either the flair or the inside track could make a fortune — and that would beat the pickings from a nomadic life or the fantasies of a film buff.

start of secondary market trading. "It is very important to Mongolia's future."

When it begins, trading in the 440 or so companies will be over the counter. Initially, the only requirement for a company to be traded is that it is privatized and the trading is scripless. Later, however, companies that fulfil more demanding criteria will be listed on a special board.

Even the current rules could cause problems. Of the 440 companies that have so far been privatized, a number is believed close to bankruptcy. Although the stockmarket's capitalization is estimated at Tk20 billion (US\$50 million), Zolzhargal believes the figure could be five times higher. And basic ratios could be hard to work out given that companies understate profits to avoid taxes.

So who will be the buyers? Although locals are expected to be the initial driving force in the market, foreigners could prove the biggest players in the long term. Zolzhargal claims that a target of 10% by the end of the year would not be unreasonable; in the longer term, he expects as much as 80% of volume to be accounted for by foreign institutions. "Many people want to invest in our market — from America, from Hong Kong and from Switzerland," says Bud Maitsetseg, senior officer at the exchange's trading and information department. "There will be big demand for mining companies as well as cashmere companies."

Not that Mongolia has many of the sort of companies that would attract foreign institutional investors. Analysts claim the majority are relatively small, while the big and profitable concerns — such as Erdenet Copper and the state telecommunications and infrastructure companies — have yet to be privatized. And liquidity could be a problem as the daily turnover is expected to be less than US\$1 million: indeed, initially trading may only take

place for two sessions a week.

Whether or not companies will be able to raise enough capital is another question. Mongolia's per capita income is officially estimated at US\$1,600. However, that figure could be significantly higher given the undeclared funds of traders, some of whom made their fortunes almost overnight. Zolzhargal even counts Mongolia's herdsman and nomads among the potential investors. "The average nomad owns 300 livestock," he says. "Each is worth US\$100. It will be a very easy thing to invest in stocks because they have no confidence in the banking sector." But until secondary market trading begins, even the nomads with their vouchers will have no real channel for selling.

The conflicting advice from international donors and consultants, and attempts to model the bourse on other international exchanges have already cost much time and money. The ADB, which is providing assistance, has consultants checking the valuation of each company and considering banning from trade shares suspected to be inaccurately priced. "This is sheer madness," says a resident analyst. "All this market needs is a place where entrepreneurs can register share transactions and where share saturation can take place. Of course it may be rough and ready. But that's the only way people learn."

That is already happening. While the stock exchange chairman frets and the donors argue, Mongolia's entrepreneurs have begun to trade shares informally. And despite calls by Zolzhargal to ban off-market trading, street-wise salesman are already doing what the stock exchange and dozens of highly paid consultants have failed to do — make a market.

Zolzhargal is undaunted. "This is not fantasy land," he insists. "Fantasy land is expensive advisers that come here costing millions of dollars. This is the real world because it will create funds. This is investment for the future." am

Vain or visionary?

He wears pin-striped suits and has a gold cup donated by the Korean Stock Exchange. He moves with the country's influential figures.

Naidansurenliin Zolzhargal, president of the Mongolian Basketball Association and chairman and chief executive of the Mongolian Stock Exchange, has power and self-confidence in abundance. Supporters call him a visionary, critics a megalomaniac.

"He is unique," says an admirer

who claims Zolzhargal could become the next president. Critics think otherwise. "Personally I think he's got his head in the clouds," says one. "But judge him for yourself."

Zolzhargal was born in Ulaanbaatar in 1964. He graduated with a master's degree in economics science from the University of Economics Science in Budapest. In 1991, following a UN Fellowship programme at the US Department of Trade in Washington, the young Zolzhargal returned home to become a director of the State Bank of Mongolia. That was when the 25-year-old economist made his mark. Zolzhargal and a group of young economists advised the government on the country's privatization programme. It was Zolzhargal who

dreamt up the idea of a stock exchange.

In 1992, following his appointment as chairman of the stock exchange, Zolzhargal was selected by the Mongolian youth federation as *The Leading Young Economist of Mongolia*. A year later he was named one of the 200 *Global Leaders for Tomorrow* by the influential World Economic Forum.

Zolzhargal's drive, commitment, obstinacy and predilection for speaking his mind are legendary. "They simply don't understand," he says of his critics. "They are fools."

His self-confidence is staggering. "I can do everything," he claims. "I have better infrastructure here than anyone. And I have better staff than anyone."