

BY PETER MORROW

# From Bust to Boom: Transforming the Khan Bank

If true development means working yourself out of a job, then Mongolia's Khan Bank is a prime example of the development practitioner's art. After more than a decade of work in Mongolia's financial sector, DAI has literally worked itself out of a job, leaving behind the nation's leading bank—a growing, thriving, standalone institution that is making a material difference in people's lives.

Our assignment started in 2000 with a U.S. Agency for International Development (USAID)-funded management contract for the state-owned Agricultural Bank, which had lost \$4 million the year before and was on the verge of outright failure. As the new CEO of the bank, it was clear to me that turning the bank around required us to leverage, rather than cut back, the bank's 269 branches. This network would prove to be a crucial part of our strategy to launch new financial services that met the true demands of the 400,000 people who at that time were using our locations to do little more than pay taxes or pick up their salaries.

Within half a year, our new approach returned the bank to profitability. New products and a new brand—Khan Bank—paved the way for a privatization process in 2003 that generated three viable bids and a new owner.

A typical development project would have stopped there with the end of our contract. But the new owners from H.S. Securities, a major Japanese company, asked DAI to continue managing the bank. We further demonstrated our commitment by becoming a minority shareholder, tying us directly to the bank's considerable success. Khan Bank has long been Mongolia's largest bank in number of locations—now boasting more than 500 branches. By 2007 it had become the nation's largest bank in terms of assets, loans, depos-



The old Agricultural Bank was the only financial institution with substantial reach into Mongolia's vast hinterland.

its, and earnings. The bank is one of the nation's largest taxpayers. And while Khan Bank always saw itself as a commercial operation, we also believed that good business means meeting the needs of your customers.

## GOOD BUSINESS, SOCIAL BENEFITS

One group that has benefited greatly from Khan Bank is pensioners. Before we took over, pensioners would go to their local branch to wait for payments in cash. The government typically ran weeks or months behind on payments and rarely had enough money to pay everyone. So pensioners would jostle, sometimes even fight, for a favorable spot in line to make sure they got paid. As part of our solution, we first set up direct deposit to place pension checks in savings accounts that would generate interest, while getting rid of the lines. Next, we extended a line of credit to the pension authority so the government could always fully cover payments—on time. Then we targeted a lending program at the pensioners to give them year-round access to cash (crucial when family expenses go up, as they typically do at Lunar New Year or the start of the school season). Almost half of the nation's pensioners use this program, one of our most popular services.

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Peter Morrow, shown here in 2003.

We always understood the bank's greatest asset was its reach. Accessible in every hamlet, we are now connected to 80 percent of Mongolian households. We have even become the provider of financial services to the nation's nomadic herders.

### **CHANGING LIVES FOR HERDERS**

Before the bank started these services, herders lived in a cash economy. When they were without cash between the spring season (funded by cashmere) and the fall (by meat), they were forced to borrow money informally on short terms and at unattractive rates to deal with medical problems, food shortages, a broken motorcycle—whatever contingency came up. When they started out with the bank, we required them to open a savings account and we doubled the interest rate we paid from 9 percent to 18 percent, encouraging them to keep their money in the bank. We also pushed the meat and cashmere buyers to wire the purchase monies to the herders' accounts at the bank for payment on the loans. Thus we took the cash out of the process and encouraged savings.

These services yielded tangible benefits in herders' way of life. To look at just one indicator, the number who own solar panels has risen from 15 percent in 2002 to 75 percent in 2009. The panels power cell phones, televisions, computers, and other devices, transforming nomadic people's ability to keep in touch

with family, access opera market information, or watch the latest Korean soap opera. Most of those new panels were purchased with one of our loans.

And Khan Bank's innovation did not stop in the rural areas. After privatizing, we opened 30 branches in the capital, Ulaanbaatar. We became a leader in ATM distribution and Internet banking. More recently, we have moved into corporate banking, supporting foreign investment into the country, particularly in mining. We handle the full array of banking services at the mine site, from cash management and foreign exchange to payroll, employee services, and even mortgage lending.

### **A SUSTAINABLE ENTERPRISE**

Khan Bank no longer requires DAI to play the same role it has over the past decade. I left my role as CEO last year, though I continue to advise the institution, and DAI Senior Vice President Rob Dressen serves on the Board of Directors. But fundamentally, the bank is an autonomous institution.

In reflecting on the bank's success, it's important to recognize various players whose contributions made it possible. USAID funded the management contract despite prevailing wisdom that the bank was not fixable. The World Bank conditioned much of its assistance to Mongolia on preventing tampering with the bank by the government, which was often tempted to push ill-advised loans. The government, in turn, honored its hands-off commitment. The International Finance Corporation made a significant investment early on, providing the bank with the creditability and the capital it needed to expand. DAI moved beyond its traditional role as a project manager and spent a decade helping build a successful business. And of course a great many savvy Mongolian managers and staff did the heavy lifting in the field.

The bottom line? USAID's two-year, \$2.5 million contract put DAI in position to help turn a bleeding bank into a \$1.5 billion enterprise that has contributed \$40 million to the government in revenue and serves as a crucial part of the nation's economic infrastructure. Khan Bank is a model for donors looking to leverage their aid by focusing on potentially sustainable—by which I mean profitable—activities. ■

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