August 2, 2011

July 2011 Monthly Newsletter

Dear Shareholders of Mongolia Growth Group Ltd.,

July saw us continue our property acquisitions, but at a subdued pace as much of the country was busy celebrating Nadaam. Given the size of our portfolio in relation to our balance sheet, I thought it would be useful to give an overview of what we're doing and how we're thinking about maximizing shareholder returns in our property portfolio.

To start with, I'd like to give a quick critique of most publicly traded property companies. In general, the vast majority of these companies focus on yield as their yardstick for success. That is understandable as dividends are crucial to how these companies are valued in the public market. These companies then use significant financial leverage to compensate for the fact that their effective yields are unattractive to most investors. The net result is an adequate dividend offset with significant liquidity risk should rental yields ever decline. Jordan Calonego, our COO, and I find this approach to be rather short sited.

Over time, the majority of the returns from a property portfolio are created by appreciation— especially in a rapidly growing economy. One only needs to look at Kazakhstan, to see what happens to property prices when an economy grows from a low base. We like to use Almaty, the largest city in Kazakhstan, as the template for our Mongolian investments as much of the architecture has a similar Soviet design. Currently, property prices in Almaty are five to twenty times the prices of comparable properties in Ulaanbaatar—hence the opportunity that we see as investors in Ulaanbaatar.

Remember that ultimately, real estate is valued as a function of current rental income and the future income that it will produce. Certain properties with low yields may have the potential to significantly appreciate because of various factors that will rapidly increase future income. Other properties are valued because of the land that comes with an older structure. Clearly an older structure will not see yields increase substantially, but at some point when it is redeveloped, one could foresee higher yields because of a much larger building on the land. In both instances, we are willing to accept a lower yield today because we are focused on future yields tomorrow. In summary, yield is but one of many metrics to use in evaluating our progress—in our case, it is more deceptive than most property companies as we are specifically going to focus on properties that aren't the best yielders.

Moving on to look at our actual yields, I want to walk you through our philosophy for when a property is acquired. The local custom is for the new owner to cancel existing rental contracts or re-price them to current market prices, with the result that many tenants are evicted upon the sale of a property. We find this foolish and with a few exceptions, have chosen to honor all pre- existing rental contracts in place when we acquire a property. We do this because we recognize the uncertainty that this can cause to the small businesses that lease our properties and wish to minimize that. We hope that our tenants will eventually purchase other services from us—such as insurance—and we cannot think of a better way to build a strong relationship with us, than breaking with local tradition and honoring existing leases.

The downside to this is that many of our properties have tenants in them who are paying below- market rates—frequently at less than half the current rate. Since most of our legacy leases have terms of less than a year, we will increasingly see these rental rates reset to the current market— but you should be aware that our current rental revenue has very little reflection on our true earning power.

For the properties that are not currently leased, we are finding that cap-ex goes a long way towards increasing our yields. While our sample-set is small, and our data is subjective, we have found that spending ten to twenty percent of the purchase price in remodeling a location can increase the yield substantially. We currently have a number of commercial properties that are not leased and in some stage of remodeling; we expect that all of these will be completed in the next few months. Unfortunately, while they wait for remodels, they are not earning us any income.

In summary, were we to renovate our commercial and office properties and rent them out at current prices, we would today have a low-double digit average yield. We find this quite attractive given the appreciation we are seeing in rental rates—which ultimately leads to higher property prices. Going forward, we expect this 'pro-forma' average yield to be reduced as we add some lower yielding properties that we one day intend to redevelop. A portfolio with a lower yield does not bother me as long as it is by design, rather than by our inability to select properties, or acceptable tenants. However, I want to make it clear why our current yields are a good deal lower than what we expect our future yields to be.

Sincerely,

Harris Kupperman
Chairman & CEO
Mongolia Growth Group Ltd.

For further details on the foregoing document, please refer to the Corporation's filing on SEDAR.

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