

For a green development

MONGOLIAN ECONOMY



Microns Away from a Brand

Happy Meat

Mongolia's Economy Finance and Business Magazine

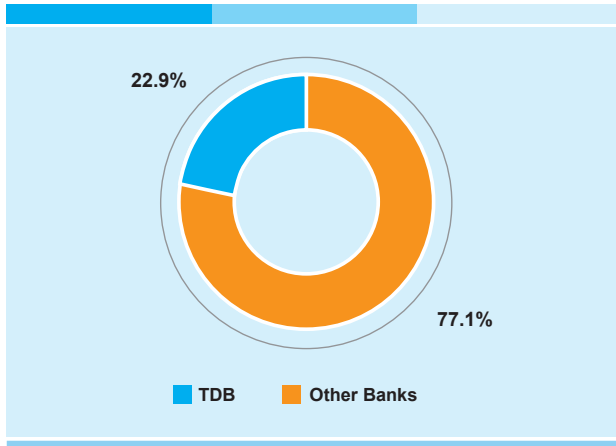
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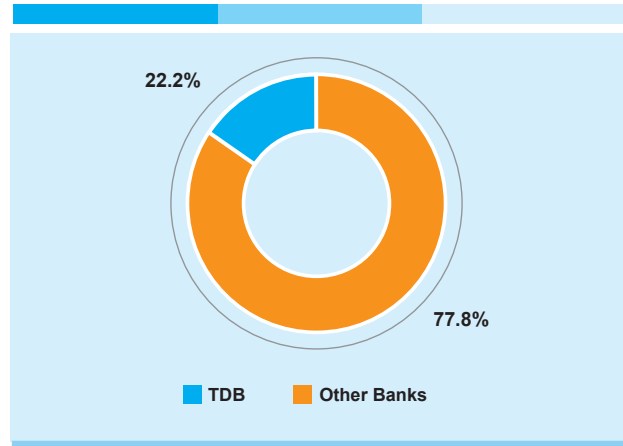
MONGOLIAN BRAND

Market share of total assets



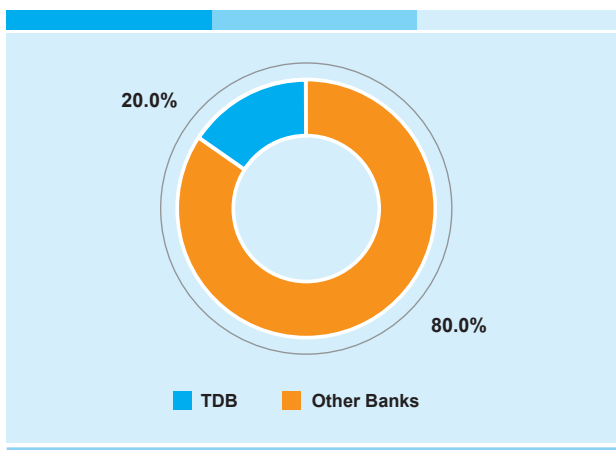
TDB accounted 22.9% of banking sector assets at the end of December 2012. In the reporting year TDB's total assets reached MNT 2623.0 billion and own capital reached MNT 295.2 billion.

Market share of total loans



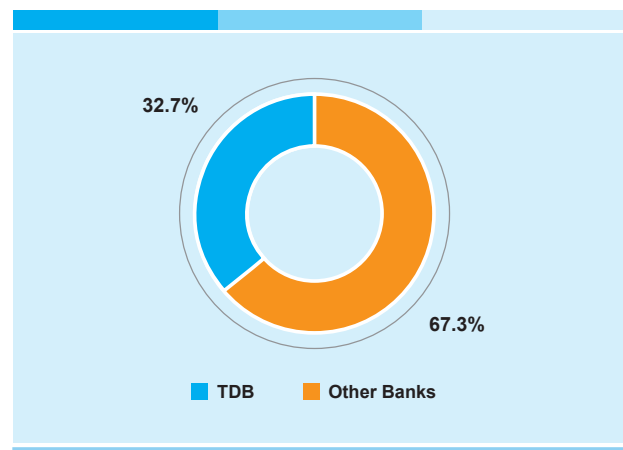
TDB is the largest lender to Mongolia's corporate customers with 29.5% corporate lending market shares at the end of December 2012. Total loans of the bank accounted 22.2% of total banking sector loans.

Market share of total deposit



TDB accounted 20.0% of total banking deposits at the end of December 2012. Total deposit of the bank have been increasing from a year to year, and reached MNT 1391.1 billion.

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MONGOLIAN ECONOMY

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Mongolian Economic Forum 2013 has its diversities compared with previous forums. This time, usually organised by the Mongolian Economic Forum NGO, the forum will be addressed by the government. Discussions during the forum are pointed towards the subjects the Government of Reform would accomplish in the Year of the Water Snake.

Attendees will be exchanging their point of views on creating brands that would represent Mongolia to the world. Private sector associates are hoping that a favourable decision will come out, since the power to grant approval is in the hands of the prime minister. A broad range of subjects were discussed at the previous gatherings. This time only a few, but important matters will be put out.

The Mongolian Economic Forum is being organised during a crucial time when the implementation of the Foreign Investment Law has begun while considerations for changes to the Oyu Tolgoi agreement and revision of the Mineral Law are making



Letter from the Editor

headlines. The forum has always served as a channel to receive opinions from NGO and private sector representatives, and to put their suggestions into action. The Outcome is the most important goal.

Next year, we could be talking about the outcomes of this year's forum, such as what accomplishments we have achieved or what products are set to start to become a global brand. The former Prime Minister of the Netherlands Wim Kok will be attending the forum as a special guest. His so-called Polder Model, which he implemented successfully during the 1980's, has turned the "Dutch disease" into a Dutch miracle in the 1990's.

Mongolian Economy is a proud media partner to the Mongolian Economic Forum. In the spirit of cooperation, we are delivering our readers a special edition, where our articles focus on the Mongolian brand, as does the forum.

We wish the forum and its attendees lots of success.

Editor in chief D. BEKHBAYAR

ENTREPRENEUR OF THE YEAR OF 2011 AWARDED BY THE MONGOLIAN NATIONAL CHAMBER OF COMMERCE AND INDUSTRY

The Business Council of Mongolia



Media Company of the Year 2012 awarded by the Business Council of Mongolia "Mongolian Economy"



MONGOLIA ECONOMIC FORUM 2013

AGENDA

Monday, March 4, 2013

- 08:00 – 09:00 Registration
09:00 – 09:20 Opening remarks: HE Prime Minister of Mongolia ALTANKHUYAG Norov
09:20 – 09:35 Guest of Honor: Ms.Lakshmi Venkatchalam, Vice President of Asia Development Bank
09:35 – 10:30 Plenary session: “Business Environment and Mongolian Brand”
10:30 – 10:45 Coffee break
10:45 – 12:15 Break-out session “ Mongolian brand and opportunities”
1: Products of the Food industry – Mongolian Brand?
2: Products of the Light Industry – Mongolian brand?
3: Tourism – Mongolian Brand?
12:15 – 13:15 Lunch
13:15 – 14:45 Plenary session: Financing for Development
14:45 – 16:15 Plenary session: Labor Market and Human Resources
16:15 – 16:30 Coffee break
16:30 -18:00 Plenary session: Legal environment
18:00 – 18:30 Plenary: Briefing of the day

Tuesday, March 5, 2013

- 08:00 – 09:00 Registration
09:00 – 09:15 Opening remarks: H.E. President of Mongolia ELBEGDORJ Tsakhia
09:15 – 09:45 Guest of Honor: Former Prime Minister of Netherlands Mr. Wim Kok
09:45 – 10:30 Plenary session: Diversification of the Economy/ Prevention from Dutch Disease
10:30 – 11:00 Coffee break
11:00 – 12:30 Special discussions/ roundtable meeting
1: Water initiative, WEF
2: PPP – International partnerships for economic growth between government, private sector and civil society
3: Green Development, WEF
12:30 – 13:30 Lunch
13.30-14.30 Presentation
1: Dr. Julia Sloan, Prof. of Columbia University, New York
2 : Byambasaikhan B., The Businessman of the Year-2012
14:30 – 16:00 Plenary session: Business Environment
16:00 – 16:30 Coffee break
16:30 – 17:30 Plenary session: Closing

A Country for Special Interests

Mongolia is a destination like no other, but how does one show that?..18



Branded Skin

Mongolia has no shortage of animal skins and hides, but very little of that is used by Mongolian manufacturers...14



Too Many Starts And Stops



Nigel Finch is an associate professor and director of admissions at the University of Sydney Business School (Australia). Finch has considerable experience in the field of business regulation and economic development across Asian and emerging economies and is actively involved in market development and institution building throughout Asia..29

The Impact of the Fiscal Stability Law on the Mongolian Economy

The following is a brief conclusion on the Impact of the Fiscal Stability Law on the Mongolian economy. The study was conducted by the Economic Research Institute. and developed by Dr. Ragchaasuren Galindev (Gerege Partners LLC Queen's University Belfast)...33



ECONOMY

- 8 **Mongolian Brand and Opportunities**
- 10 **The State of Nature**
- 12 **Happy Meat**
- 14 **Branded Skin**
- 18 **A Country for Special Interests**
- 20 **Microns Away from a Brand**
- 24 **Open the Door, Global Market**
- 26 **Working Together to Address Development Challenges**
- 29 **Too Many Starts And Stops**
- 33 **The Impact of the Fiscal Stability Law on the Mongolian Economy**



FEATURE TOPIC

MONGOLIAN BRAND AND OPPORTUNITIES

BY: I. OTGON

There are a number of top brands such as Scotch whisky, Italian cuisine, French wine, Swiss watches, and Japanese cars. But here instead of manufacturers' names, the names of countries are used to identify them. While more and more of the world's top brands are being

added into the everyday consumption of Mongolians, the concept of a Mongolian brand is still uncommon.

During the 2013 Mongolia Economic Forum to be held on March 3 and 4 will be the special break-out session "Mongolian Brand and Opportunities". Also worthy of »



Photo by B. Byamba-Ochir

► note is that while this special edition of *Mongolian Economy* for the 2013 Mongolia Economic Forum was being prepared, a number of scientists, lecturers and researchers were contacting our office to ask if it was able to provide the brand-related research materials and literature from the forum. This made it clear that this was the right time to send out an issue focused on branding.

At the moment, whether the brand needs to be oriented towards the domestic or international market is still unclear. With one of the fastest developing economies in the world, Mongolia would need to come up with a successful brand for its meat, milk and animal hides.

The concept of a brand likely originates from a term meaning trust, promise or feeling. So, the starting point must be considered more seriously. An attempt to brand Mongolian dairy products, such as yogurt and dried curd, would be inappropriate for the moment. But the cashmere industry is obviously near the transformation point to launch a brand. While some cashmere producers have no idea about branding, others, including Mongolia's largest producers, are spending their money and putting their efforts on brand development.

Despite its roots in the mining sector, Mongolia is apparently a country of agriculture. There is a necessity to come up with noticeable results in the processing of raw materials, rearing livestock, and manufacturing finished products. As can be seen from the experiences of other countries, agricultural products have succeeded best in global branding endeavours. To do so, however, will require support from both the government and society.

Mongolia has played a very small role in global agriculture thus far, but that does not mean it will never have the opportunity.

The reason why so many have gathered at the Mongolian Economic Forum is to discuss these issues and define a clear concept. The success of this forum hinges on identifying the demand, involving the representatives of every socio-economic sector, and sparking discussion for a successful future.

Mongolian Economy includes a number of ideas and suggestions from several experts and professionals of an array of industries for this special edition for the Mongolia Economic Forum. They explain how Mongolia's light industries for the manufacturing of hides and leather, cashmere and wool, meat and dairy products stand to compete with their brands on the global marketplace.

This forum provides the best opportunity to discuss together the types of brands needing development, the experiences of entrepreneurs and their future outlooks, and what the state can do to help. Mongolia, a shining star in the heart of Asia, is likely to have a number of economic pillars to stand on, including mining, with its quality brands to contend with competing brands around the world. ■

BY: I. JARGAL

Norov Altankhuyag, Mongolia's prime minister, expresses his position in a special edition of Mongolian Economy for the Mongolia Economic Forum 2013.

“Mongolia should brand its organic products.”

The Mongolia Economic Forum is organised every year. What is your assessment of it? As prime minister, what are your expectations from this year's forum?

In general, the right decision could be taken when we discuss it together with representatives from a number of sectors. It is very important that the state, entrepreneurs and civil society, the three main parties, sit together, discuss and exchange their ideas and information.

The Mongolian Economic Forum's value is the balanced participation of each party. Providing every party the opportunity for participation at every level is the core principle of the innovation that we always talk of. A number of policies and activities to implement for citizens, who are the chief wealth of the country, have been included in the new government's programme. One important promise is to create jobs for the citizens. The forum covers this topic, too.

The theme “Mongolian Brand and Opportunities” is attracting the most attention for this year's forum. Why is this topic so important?

We have set the large goal of having our own brand of products as we consider sustainable development for the Mongolian economy. If Mongolians could produce for themselves, they could become the main driver of the unstoppable growth in this country. As this



FORUM

THE STATE OF NATURE

forum gives attention to this issue, our expectation is for big outcomes.

We have been talking as if mining was the main driver of the country's economy. Although nobody can deny this thinking, the economy itself cannot rely on only one sector. That's why state policy is directed towards diversifying the economy and establishing a number of pillars for support.

The government should provide sup-

port and opportunities for new sectors that Mongolians can open up and where they can produce anything they want.

We have the same goal: to create a brand, neither nationally nor regionally but globally. We have plenty of opportunities to do so. A big question is by whom and how will this brand be created. In this case, the entrepreneurs will produce their brand of products themselves. During the forum we will discuss ►►

▶ the troubles that entrepreneurs have experienced in their branding and the point where we could decide things together. Also we will listen from entrepreneurs about any hindrances caused by the government such as corruption, bureaucracy, pressure, licensing, special licensing and registration; as well as support that could be provided by the government such as creating a legal setting to benefit exports, paving the way towards international markets, and enabling tax benefits.

On the other hand, the researchers and the representatives from civil society will analyse and express their opinions on whether the government is willing to make decisions on these aforementioned issues.

Of course, the government will give its direction. It is very important that we come to consensus in this way. Mongolia's national brand could be created with the combination of the government's support and entrepreneurs' intentions. The concept of branding is comprised of a lot of very detailed factors. I heard that the word's origin is from Norway. There, its meaning is a guarantee for any service done or product made by a company.

Among all the choices available, for what can Mongolians guarantee? The state is willing to support whatever that may be. That's why we are going to discuss what this could be during the forum. The chief representation of Mongolia will start from what that should be.

For example, Korea's service industry is world famous, and everybody knows that they will be satisfied with their services. This is their brand. People know that Japan produces premium quality electronic goods, Germany makes good cars, and China has the richest workforce. In this way every nation has its own brand.

How about Mongolia? What brand is most appropriate to put on the global market? The answer is "Mongolia is natural". We want our brand to be focused on the concept of natural attributes. In other words, Mongolia should be branded by its organic products.

If there is any obstacle created by the state in branding for entrepreneurs, it must be removed. With support from the government for branding development, marketing and services should be improved.

Can we expect any results from the recommendations made at the special session

"Mongolian Brand and Opportunities"? It has become apparent that the recommendations made at previous forums have borne few results.

Of course, there are many criticisms and disagreements among all the activities. I was often asked a number of questions from communities in past forums: why the issues we discussed had not been resolved, and how the issues that had been discussed last year had been handled.

Every forum depends on its agenda very much. The agendas of the previous forums were green economy and innovation; which were subject to long-term policies. These issues are not short-term issues where we can have a discussion today and then decide tomorrow with quick results. For example, the enforcement of an appropriate long-term policy may result in the successful implementation of an environmental issue. But we should not leave this issue behind. It needs to be raised again.

We will follow this routine: On the second day of the forum we plan to discuss the issues we've discussed here. But the main agenda still is to keep focused on what Mongolians could do altogether. I have no doubt that we will come up with good results. The government will commence its activities immediately after unanimous agreement from all the parties on the issue of a brand for Mongolia. I am confident that things will become more certain after a year.

Which sector is given the highest priority for development in government?

According to government policy, priority is given to agriculture and light industry for the development of nationally branded products. Our entrepreneurs have very big intentions for industry and elsewhere. In the Mongol Citizen 2020 programme, a national discussion led by the Democratic Party, we heard from entrepreneurs in every sector. Those findings were included in the new government's programmes and policies. Therefore it becomes apparent that the government's and entrepreneurs' goals are one in the same.

This time, our discussion will be more thorough and detailed, and we will behave like a business. Therefore, I would like to appeal to all the delegates from the entrepreneurs, civil society, scientists, researchers and civil servants to actively participate in the sessions and to be creative. ■

MEAT BRANDING

HAPPY MEAT

BY E. ZORIGT

Mongolia awaits the day when its meat can be found in the freezer department of grocery stores around the world.



Photo by E. Zorigt

Meat export has been controversial for nearly two decades in Mongolia, and the decision over whether to make Mongolia's meat a nationally branded product has passed through several governments. Unfortunately, the issue has never been addressed. It did not

even reach the Uralian Mountains or the cities of Ulan-Uud and Erkhuu.

However, Mongolia has encountered several issues that need to be addressed to make the dream of making a brand for meat come true and to achieve the goal of providing a secure and cheap

meat product for the domestic market.

Mongolians believe that Mongolia's meat should not only be for export purposes. They expect a Mongolian-branded meat could raise Mongolia's reputation in the world.

The consumer believes he or she makes a choice alone. But the producer believes the brand separates the product from others and makes certain promises to consumers.

"Our big target is now the European market", said Steven Kreppel, the managing director of the Mongolian National Marketing Coordination Office of the Mongolian National Chamber of Commerce and Industry. "The whole world, especially Europeans, are now paying significant attention to eco-friendly aspects. As natural, organic and cruelty-free meat consumption is more likely to appeal to Europeans, this would be absolutely a good opportunity for Mongolians".

According to a survey by the European Research Institute, 40 percent of Europeans prefer consuming "happy meat"- a term used for meat coming from animals that lived well and were slaughtered humanely- in their daily foods. Happy meat is a new concept to Europeans, but is common here in Mongolia. In fact, Mongolians have a tradition of abstaining from the slaughter of young animals. Mongolia's meat is an organic product, as its methods for animal husbandry are mostly subject to pastoral farming where animals can graze to eat natural grasses and drink fresh water.

In the European market, the price ►►

► for happy meat is several times more than the price of meat from commercial livestock. If Mongolia could advertise its meat in Europe it would have an opportunity to sell organic, happy meat, branded as its own.

Mongolia is interested in exporting its meat abroad. Foreign countries are also interested in importing meat from Mongolia. In addition to Mongolia's two neighbors to the north and south, Southeast Asia and the Middle East have sent proposals for meat imports from Mongolia. According to livestock inventory statistics from last year, Mongolia had a total of 40.9 million heads of livestock. There is an interest of supply and demand. Somehow it is ignored when it comes to export.

Mongolia exports more than 10,000 tonnes of meat every year, of which 90 percent is exported to Russia while a small amount of horse meat is exported to Japan. Moreover, Mongolia entered into an agreement with China's government for the export of processed meat, but terms have still not yet been finalised.

The current situation for meat export falls short of its potential. Meat exports fell sharply last year, mainly due to a ban on meat export from the government. Export volume could have reached 20,000 tonnes of meat last year if it had not been for the ban, according to a projection by the Mongolian Meat Association.

"The government has put a ban on [meat] exports from December 2012 until March 2013. This is due to the increase to meat prices in the domestic market" said the executive director of the association, M. Jadambaa.

"In general, it seems that the meat issue is not taken seriously by the government of Mongolia. First of all, it needs to supply domestic demand according to the stock reserves of meat for emergencies. The issue on meat export needs to be raised, but the ambitions of entrepreneurs is to compete on the global market by exporting meat".

Supplying the domestic market with meat can be a headache for all involved. Policy makers feel price hikes in the domestic market are due to insufficient meat supply and distribution methods, and uncontrolled export. Yet neither is-

sue has been addressed.

Good, Clean, Diversified Economy

Mongolia's meat is usually assessed as one of the lowest in terms of hygiene. This fact currently poses the biggest challenge for Mongolia. Therefore, foreign experts recommend establishing large meat factories that meet world standards. Before that can happen, however, accurate inventory of livestock must be carried and a database logging animals' origins and pastures grazed must be developed.

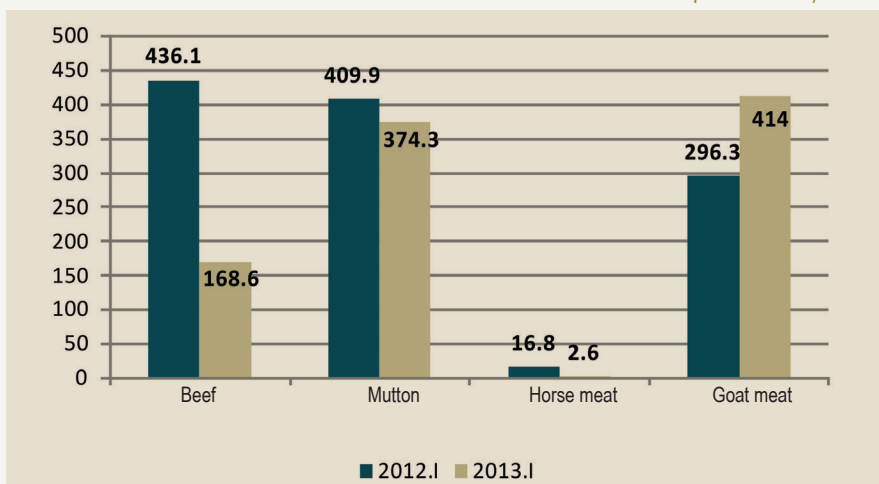
"Meat supply and distribution is insufficient. To become a meat-exporting country, the priority needs to be given to abolishing uncertainty of where meat comes from and who handles the meat

supply or delivery. Moreover, registration of livestock is also a priority", said French livestock worker Beatris Balve.

Steven Kreppel said that during this hard time when Mongolians are facing food insecurity when selling their own products that fails to meet standards of quality at high prices really makes no sense.

In addition, Mongolia's livestock grazes on wide pastures. This means the quality of meat varies depending on the region the animal grazed in. Registering where livestock grazed would enable Mongolia to survey the different meat prices foreigner buyers could be expected to pay. For example, according to a survey by the Meat Association, mutton, beef and horse meat from Mongolia's steppe and Khangai regions were found to be best suited for branding ►

Meat production /tonne/



Number of livestock head /million/

Aimag, Soum	Type	2009	2010	2011	2012
Nationwide	Total	43,981.01	32,729.53	36,335.78	40,920.92
	Horse	2,221.31	1,920.34	2,112.93	2,330.43
	Cow	2,599.33	2,176.00	2,339.70	2,584.62
	Sheep	19,274.73	14,480.40	15,668.53	18,141.36
	Goat	19,651.52	13,883.21	15,934.56	17,558.67
	Camel	277.05	269.577	280.062	305.835
Western region	Total	10,888.36	7,418.46	8,525.36	9,670.83
Khangai region	Total	16,716.23	12,216.47	13,472.39	15,379.51
Central region	Total	10,484.07	7,557.95	8,448.84	9,463.89
Eastern region	Total	5,491.54	5,273.76	5,610.28	6,098.22
Ulaanbaatar	Total	400.825	262.881	278.919	308.46

Source: National Statistics Committee

▶ Another critical issue is Mongolia must introduce the Hazard Analysis and Critical Control Points (HAACP) to its meat industry. This is the world's criteria for standards of quality for hygiene in food processing. This system has been introduced by only two companies, Makh Market and Darkhan Meat Foods.

No Transport, No sale

Poor development of logistics hampers domestic meat price and export as well. The transition to a market economy resulted in the loss of a centralised system and a number of meat merchants appeared following steep growth in demand for meat.

"The only way to remove the meat traders from the market would be a meat exchange through the capital market", said M. Jadambaa. "The ministry has not responded to this need. It is very strange that meat is not considered, yet skins, hides, wool and cashmere are sold through the market exchange".

When asked about this, the Ministry of Industry and Agriculture only responded that the matter was under discussion but a plan had not yet been arranged.

Abolishing the current system, which allows almost anyone to sell the meat they had butchered, for one that is more sophisticated and professional would be one way to improve the meat industry and reduce prices. Although the next challenge would be to tackle the lack of logistical expertise and infrastructure.

"Logistics is an entire process that includes producing and delivering safe and healthy products to consumers", said Kreppel "For instance, the country would be able to deal with logistical problems if it established an integrated transport system which could deliver products to Selenge Aimag, Ulaanbaatar, and abroad".

At present Makh Market has meat processing factories in 11 Aimags throughout the country. They buy livestock from herding families at market prices. This obviously creates conditions in which products can be traded without passing through the hands of butchers. It also enables herdsmen to sell their livestock at reasonable market

prices and profit.

Makh Market's success has prompted the Ministry of Industry and Agriculture and the Meat Association to partner in the development of a bill to improve regulations over the relations between herdsmen and producers in order to introduce this sort of logistic service across the country. The bill would likely grant subsidies to herdsmen who sell their livestock to commercial producers.

Using Opportunity

Mongolia could follow in the footsteps of high-end producers such as Japan, whose wagyu beef has gained in popularity worldwide and sells at MNT 330,000 a kilogram.

There are many reasons for the high price of a product such as wagyu beef. When a shopper in a grocery store in Europe buys a brand of meat, they buy it not ▶▶

SKIN&HIDE

BRANDED SKINS

BY KH. ANAND

Mongolia has no shortage of animal skins and hides, but very little of that is used by Mongolian manufacturers

According to Anthony Wright, a skin, hide and leather expert from the Agricultural Products Marketing and Branding Development project, said Mongolia's tanneries can contribute to Mongolia's development just as much as its mines.

"The industry could bring the country to the global level through the manufacturing of leather products for sale in both the domestic and international markets. If wisely managed, the industry could succeed, but time is limited".

D. Amarjargal, senior skin and hide expert at the Ministry of Industry and Agriculture, noted the importance of the MNT 200 billion in financing from sovereign bonds sold by the Ministry of Finance on the local stock market.

"With the bonds' support, we expect to change and innovate a number of things. Although the current circumstances are difficult, some of our tanneries have received business proposal

from the world's top brands such as Ecco and Zara".

She added that by introducing these products to the domestic and international markets, herders' campsite would become the starting point of the value chain once again. To do so, there must be focus on the health of livestock, their living conditions, and the quality of fodder and skin care. She said tanneries also needed upgraded technology, and, of course, a demand from foreign markets must be created.

Mongolian ambassadors, especially in the European Union have raised this issue in the countries in which they serve. They ask for support so the tanneries back home can successfully brand their products. The world has grown impatient with the poor quality promised by the label "Made in China", but maybe they could learn to appreciate labels that identify Mongolia as the point of origin. ▶▶

▶ only for the meat but also for the guarantee of quality the brand offers. Twenty or 30 years ago meat producers did not care about meeting the standards or requirements of their consumers. But nowadays consumers are more likely to seriously consider the countries where meat producers are physically located, their reputation, the corporate governance employed by the producer, the transparency of its operations, and its values.

If all these requirements are met, then meat producers can hold on to their consumers while charging high prices for their premium product.

Any complaints from consumers are the responsibility of the meat-processing factory, the butcher, and the herder who bred the animal. Therefore, the biggest criterion for introducing a brand starts with creating the concept amongst communities that everything made in Mon-

golia must be reliable and quality must be confirmed.

With so many livestock, is Mongolia only able to store its extra meats for emergencies? Or can it create a new, original brand that could represent Mongolia to the world?

If Mongolia can brand its meat products its herders can play an important role in the financial and economic markets of not only Mongolia but also the world. ■

▶ J. Tsendeekhuu, Director of Khukh Tug Trade LLC said "We do not print any patterns or pictures on our hides. Our preference is to keep it original. The hide, itself, is the brand".

Companies hoping to export domestically manufactured products abroad need an accreditation from an international laboratory. Unfortunately, Mongolia has not yet introduced this kind of system. Over the last twenty years, the government of Mongolia and its people have been practically giving

factories are rejected when we try to use them in our production because of their poor output quality. In Mongolia, there is no tannery that produces raw materials of a good quality", said Tsendeekhuu.

"Our consumers are often dissatisfied when we manufacture our end products using such materials. All the tanneries in Mongolia import their raw materials from China, meaning that the cash flows towards China".

A total of 10.3 million cattle skins

ing European standards and then exported to more than 10 countries, such as Italy, Spain, Turkey, or South Korea. Annual raw material costs total MNT 151.6 billion, of which MNT 38.2 billion of raw materials is purchased by national manufacturers and MNT 113.4 billion is exported to China.

There are 34 tanneries for skins and hides and 80 for leather operating in the nation. This is not enough, as the country is rich in raw materials. Global producers import 85 to 95



away to foreign buyers its low-priced semi-processed skins and hides. Mongolia's processing capacity is only at the initial stages, allowing the country's producers to receive merely 15 percent of total profits.

"Skins processed by Mongolia's

and hides are produced each year, of which 74.2 percent is exported to China, processed or unprocessed. In addition, 25.8 percent is processed by Mongolian national producers, of which more than 40 percent is processed by manufactures implement-

percent of raw materials from foreign countries such as China. Not a single company was found amongst them that could possibly represent Mongolia as a brand with the capacity to export abroad.

The ministry has projected value- ▶

▶ added earnings would increase 1.4 times if its skin-hide products were semi-processed domestically, 2.3 times if fully processed, and five times if it could produce end products.

“Semi-processed skins and hides are exported abroad at USD 39 a piece. The exported products are imported to the country as an end product costing at least USD 80 each. This issue needs to be addressed”. Enkhtur said, “State policy has for a while been lacking on terms for taxes on goods and export conditions for national manufacturers”.

“For instance, the government of China is implementing a policy that exempts its national manufacturers from tax for five years and grants loans at the lowest interest. Another factor hampering development of this sector in Mongolia is the zero tax for imports. High-cost [Mongolian] products cannot be sold at a price lower than China’s products”.

Tsendekhuu, too, said taxes were exerting enormous pressure on manufacturers, as they are taxed at the same rate as larger, more efficient operations. He said a more lenient tax policy where companies could pay tax on a quarterly basis would be preferable. A lot of financial and technical support has come from the government and private organisations trying to bring life to this industry. One of those groups is the Agricultural Products Marketing and Branding Development project where Wright works as an expert in the processing of skins and hides.

“This sector is in the devil’s circle and there are plenty of problems. At the same time there is also a chance to develop and to make a profit, according to our research team.”

He recommended that Mongolia’s tanneries install the latest equipment and technology. Afterwards they would have to manufacture goods affordable for the world market and supply them regularly. The industry, he said, would also benefit from a fair legal environment.

The government has begun its effort to save this industry by directing the funds from its local bond offerings to 200 of Mongolia’s micro manufac-

turers. But the latest equipment and technology will not be enough alone to save the industry. Most important will be reversing the flow of raw materials from foreign producers back home to Mongolia’s domestic operations.

The government has taken measures to support the herders through subsidies to herders who sell their skins and hides to national firms. A representative herder said not enough was being done, however. He pointed out that Chinese businessmen were more experienced in working with and trading raw materials than their Mongolian counterparts. Mongolian agents working for Chinese operations often pay much more than the price they can earn from national producers, even with government subsidiaries. Another problem is factories lack the resources and workforce to compete.

Wright, however, had a few ideas of how Mongolia could set itself apart from global competitors.

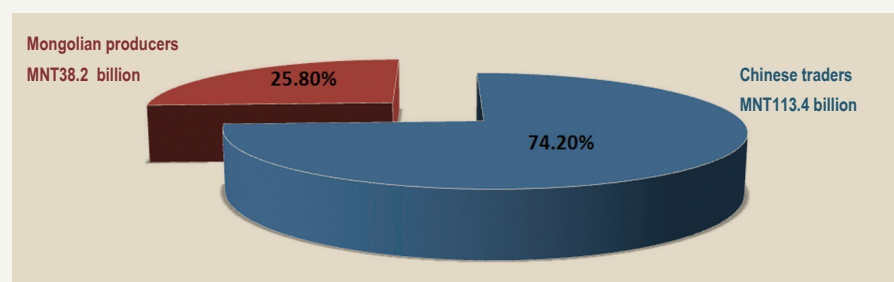
“From the viewpoint of people across the globe, especially the rich countries of the EU, their daily consumption is expected to be eco-friend-

ly and ethical”, he said. “An advertisement that introduces the skin and leather products to the world should demonstrate how well herders breed and take care of their livestock”. ■

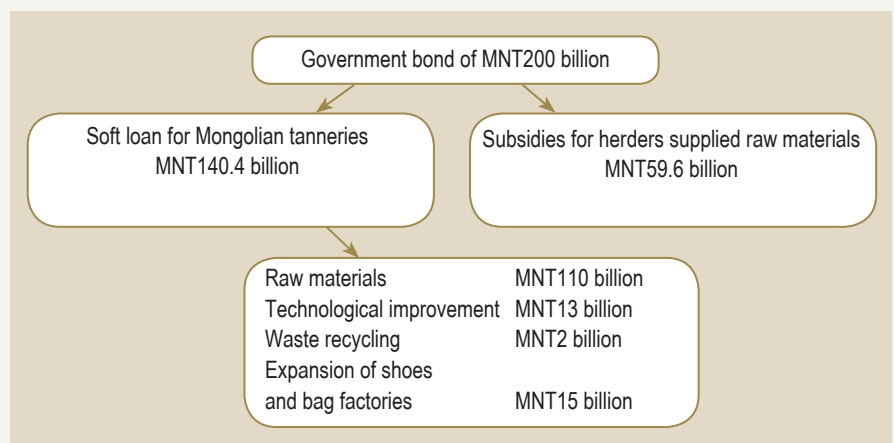
Target of tanneries /million piece/



Purchase of raw materials



Government bond spending





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TOURISM BRANDING

A COUNTRY FOR SPECIAL INTERESTS

BY. ENKHTSETSEG

Mongolia is a destination like no other, but how does one show that?

“The fool wanders, a wise man travels”, said British clergyman and author Thomas Fuller. It is prejudiced to call every traveller a tourist. A tourism industry that adapts its management and marketing well to the draws of a country and the expectations of its patrons will provide them with the best experiences. Those travellers will leave the country feeling as if it were their own.

The sustainable growth of tourism is based on the preservation of nature and traditional culture. It has been 20 years since the seeds of this industry were planted in Mongolia. Now it is time for tourism to wash its face and come out with a clean and new look.

It is hard to describe in one word how foreigners imagine Mongolia. Some envision the ancient land of Chinggis, nomadic civilization, beautiful nature, or a bustling mining industry. Though people around the world know Mongolia better now than in the past, there are still many who mistake the independent nation of Mongolia for the region of Inner Mongolia in China—or even forget that a separate nation exists.

These days the mining sector gets the most attention and is the most stand-out feature for most. This is undesirable to tourism, which looks to entertain and give a freewheeling impression. Many feel the happenings in mining is overshadowing tourism in the country.

The Mongolian Tourism Association set out to create the image that best suits the country for tourism. Meanwhile the image put out by various private companies and NGOs may be inconsistent with each other.

“It does not benefit much, though we spend a lot of money advertising to foreigners. This shows us that we do not have a definite overall understanding of marketing”, said, Nergui Shagdarsuren, director of New Juulchin Tours.

The subject that has gathered the most attention in the industry lately is branding. Travel companies have accused the government of taking tourism for granted in Mongolia. In the last two decades since the transition to a democratic and capitalist system, tourism has been grouped with various other interests and sectors in government, most recently settling with sports and culture.

Almost everyone who works in tourism admits doing business is a mess here. They are nearly begging for a single, all-encompassing policy they can follow. Recently, the Ministry of Culture, Sport and Tourism presented measures to tourism workers, one being branding.

“It is vital to give the impression to the world that Mongolian tourism is amazingly unique and invaluable”, said Tserendolgor Enebish, director of Tseren Tours.

There are many attributes of Mongolia that can represent the country, such as ▶

► the authentic nomad life, different types of natural formations, its rich history and rare animals. According to global tourism branding practice, one thing is for sure: Mongolia has to choose one particular image to position itself in the world as a “choice” market”.

Mongolia’s tourism industry will receive acceptance from the world when people from other nations can imagine a clear image of it.

“Mongolia has to emphasize what makes it a unique place in the world. At this forum, people are talking about the nomadic concept. That is a good concept because many people know Chinggis Khaan”, said Alastair Morrison, president of the International Tourism Studies Association at the 2013 Mongolian Tourism Forum. “The most important thing to focus upon is to not try to be like other destinations”.

At this year’s forum participants suggested some branding themes such as “nomadic Mongolia” and “horseback Mongolia”. But these days Mongolia has many young Mongolians who do not know much about horse-riding equipment, how to ride a horse or cannot even recall the five traditional animals.

“An image is something that is felt from a country’s wind and their resident’s eyes. It is necessary to find that image. Also, it cannot be something only seen in advertisements, but something every Mongolian can understand and express”, said Tsomorlig Erdenechluun, a lecturer of tourism at the National University of Mongolia.

According to the company Total Marketing Destination, a brand of tourism introduces personality, tells a story, arouses the senses and stimulates emotions through its connection to the core values of that place. This contributes towards a deeper relationship between the place and its key audiences. A brand is inspired by the logo, colors, key words, style, fonts, emotional benefits, and personality. These characteristics set it apart from other brands.

For tourism in developed countries, government binds the general policy while institutions like the National Tourism Organization takes responsibility over marketing. For instance, Australia’s major branding initiative, Brand Australia, was launched in 1995 by the Australian Tourism Commission. It broke new ground in how the country was branded to the outside world, separate from their mining.

Australia’s nickname, “The Land Down Under” gives the impression that Australia is carefree and laid back. In addition to tourism, Australia’s strong brand recognition was helpful to trade, business, and investment opportunities into other sectors and industries.

“Our challenge is to capture and recognize that

this connection with Australia goes beyond the physical to the emotional and is true and powerful for everyday Australia. We call it the ‘Australian effect’”, said Zoe Shurgold, a public relations manager to the United States for Tourism Australia.

Choices

There are two types of travelers: traditional and special interest. Special interest tours are designed to fit one’s specific interests. According to world tourism classifications, Mongolia’s tourism operations are categorised as special interest.

Minister of Culture, Sport and Tourism Tesedevdamba Oyungerel announced that her ministry was planning to develop regional tourism for special interests. Special interest tourism in Mongolia would include specific trips for bird watching, hunting, paleontology, nomad culture, photography, and winter excursions.

“It could be the best solution for us to have one main goal instead of chasing after many. But I cannot say that special interest tourism is the best fit for Mongolia”, said D. Gansukh, president of the Tourism Education, Training and Research Center NGO.

Choosing a single image to represent the country is the most challenging aspect of this issue, but it is one other countries have struggled with in the past.

“Special interest tourism is not just found in this particular part of Asia. It is a worldwide trend. It is a good strategy for Mongolia because it is not a mass-tourism destination”.

Mongolia’s nomadic lifestyle is the calling card of the country. This became evident after the slogan “Go Nomadic, Experience Mongolia” received nearly all the votes at the 2013 Tourism Forum. However, there is hesitation among people whether the nomadic way of life is a sustainable image for Mongolia.

“Growing urbanisation and the vanishing of the nomadic lifestyle means there might be an absence of culture to display in Mongolia”, said Tseren Tours Director Enebish.

Mongolia is not the only place featuring the nomadic lifestyle in the world, but it is perhaps the most authentic. Whereas in Mongolia nomads arouse romantic images and thoughts of adventure, in other countries the perception is of wanderers and beggars.

Governments around the globe are confidently investing billions each year into establishing and exposing to the world their destination brands. In this way Mongolia can present its image at the frontline to global travelers and draw them like a magnet. ■

CASHMERE

MICRONS AWAY FROM A BRAND

BY I. OTGONJARGAL



One industry which is near to becoming a brand in Mongolia is cashmere. Everybody in Mongolia knows the country's cashmere garment producers such as Gobi Corporation, Goyo, Buyan, and Altai Cashmere. Their cashmere and wool products are very popular in both urban and rural areas.

There should be a reasonable demand when creating a brand. Until four to five years ago, cashmere garments were thought to be a luxury product only consumed by wealthy buyers. Recently, this idea in society has change to one where everybody should wear cashmere to better cope with harsh

winters that reaches below -50 degrees Celsius. Cashmere garments are warm, soft and provide a smart look. In addition to the cashmere cardigans, sweaters, hats, and jackets available, a variety of traditional costumes made from cashmere are now very much in vogue, especially during holidays.

Back a few years ago, only famous people such as artists, politicians and wrestlers wore cashmere costumes during the Mongolian New Year, Tsagaan Sar. But now it is very common to receive one as a gift during the New Year or Lunar New Year holidays. The product costs between MNT 700,000 and MNT 800,000. Gobi

Corporation and other cashmere companies receive overwhelming orders before Tsagaan Sar. As soon as spring arrives, the number of orders for cashmere coats tends to grow, both domestically and internationally.

The point of all this is Mongolians trust their cashmere products. This trust is one of the main criteria for creating a brand.

"A brand is a more like a guarantee of a product's quality than a name, label and logo", said B. Ariunaa, director of international sales at Gobi Corporation.

She said her company had brought her label to 36 stores in 11 countries, including the United States and Italy. But their real goal, she said, was to bring Gobi Corporation's garments to 100 stores around the world.

The corporation had its logo registered in 22 countries. In 2010, the company was the first Mongolian company to register in the United States.

"An old concept was that cashmere products are expensive and only bought by people above the age of forty", she said. "These days young people's interests in buying cashmere products has grown. Another change is an interest in selling cashmere garments through brand shops like Zara, etc".

Gobi Corporation and its competitors are trying to create new brands for products with good designs that exemplify Mongolia.

One example is its focus on in- ▶▶

▶roducing a new product to the market. Its Gobi Organic Mongolian Cashmere store opened near the Gobi factory on January 30. The new store sells these Organic-brand cashmere products in four colours (white, beige, brown and grey) without the use of harmful dyes. It also experimented in 2010 by working with famed Italian designer Saberio Palatella to create the Gobi Saberio Palatella collection.

Noble Fibre

Small and large cashmere companies tend not to label their exported goods. However, there are a number of international orders received by companies.

Mongolian cashmere products comprise 20 percent of the world's market. Unfortunately, there is a lack of awareness of Mongolian cashmere products in the world.

"A brand is a hope and belief," said Juergen Mendritzki, team leader of the Agricultural Marketing and Branding Development Project at the Asian Development Bank.

He said, "Branding globally takes at least five years. In other words, branding is the same as raising and taking care of a child. Once a goal has been set to become a global brand, four steps need to be taken for the brand's marketing: attract consumers, stimulate their interests, make them wanted to touch, see and try the products on their own, and make them purchase the product".

The project, which has been ongoing since September last year, has worked to bring Mongolia's cashmere products to international markets. The project team has closely worked with the Ministry of Industry and Agriculture, the Mongolian Association for Wool and Cashmere and cashmere producers in urban and rural areas to introduce the label Mongolian Noble Fibre (MNF) to the world.

The plans is to have the MNF label attached to the label of other famous brands. If the project succeeds, it will serve as an example of the good quality of Mongolian cashmere. The label

reads: "...this is a fine cashmere product of a good quality, extracted from Mongolian goats that grazed and bred on the vast steppes of Mongolia...".

The project plans to introduce two products. The first will be made of fine cashmere with 15-micron fibres while the other is 16.5 microns. Despite the fine grain, there may be other indicators of a poor product, and only a premium quality product becomes a brand in the world's fashion industry. Not every company can introduce their products under a unique name. However, Mongolia can prove that its cashmere is of a good quality, and its production is large enough.



Natural, undyed Mongolian yak down, as used in this soft and lofty "Mongolian Beach Blanket"

The project team said the MNF label must be owned by the Ministry of Industry and Agriculture. They also said NGOs and the Agricultural Marketing Division at the Ministry would be best suited to run the operation.

"As we can see from other countries' experiences, this sort of operation is more efficient when run by NGOs that specialised in marketing", said Mendritzki. "NGO's have to establish their monitoring councils, which could consist of representatives from professional associations, the government, buyers and international organisations".

"Personally, I hope that the govern-

ment of Mongolia will back the establishment of the Branding Management Agency".

MNF has started advertising, and last year representatives from Mongolia's cashmere producers and government officials attended the World Cashmere Conferences. A number of tasks have been accomplished that deal with the mistakes made and weaknesses that became apparent during the processing of cashmere. Mongolian goats comprise almost half of the over 40 million heads of livestock in the country. Mongolian cashmere is ranked highly in the world.

In January, cashmere producers held meetings and workshops on the industrialisation of the wool and cashmere industry. During the workshop, a number of objectives were set, including lifting the ban on the export of unprocessed cashmere, increasing the number of jobs available from 8,000 up to 20,000, and increasing production from 1.2 million to two million to three million units. These goals are expected to be achieved by 2020.

But it can only be done with support from the government. We hopefully look forward to the soon development of the Mongolian cashmere industry, with a future of brands. ■



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MADE IN MONGOLIA

OPEN THE DOOR, GLOBAL MARKET



KH. BURTE

Tsogt Orshikhui LLC exports 12 types of winter workwear to Rio Tinto copper miners at Kennekott, Utah. This is a clear example that Mongolia has an opportunity to compete in international markets.

Mongolian designers make a variety of traditional costumes, labeling them "Made in Mongolia". The costumes are made of thin materials, warm and well designed. National costumes include jackets, short-sleeved shirts, dresses, and so on. The door to the global market has not opened yet to Mongolia. What does Mongolia need to open that door and enter?

"The legal setting for introducing traditional costumes to the global market is challenging," said N. Narangerel, an official at the Policy Implementation Coordination Department of the Ministry of Industry and Agriculture. However, Mongolia's manufacturers are skilled in designing and manufacturing garments and clothes of good quality and design which are comparable to any of the world's top brands."

"High tax is the main factor that is stealing time away from Mongolia's brand from being accepted on the international market. With Mongolia's harsh winters as the chief characteristic of Mongolia on most people's minds, it might be best if Mongolia produced clothes for such extreme climactic conditions, said Ch. Altantsetseg, director of the Costumes Research Centre at the Mongolian Uni-

versity of Science and Technology.

"The capabilities of Mongolian designers and tailors have reached the global level" said Altantsetseg. "Only, they lack cheap raw materials and technologies. For manufacturing warm clothes, our country has an advantage over other countries, but it lacks industrial technology and the workforce".

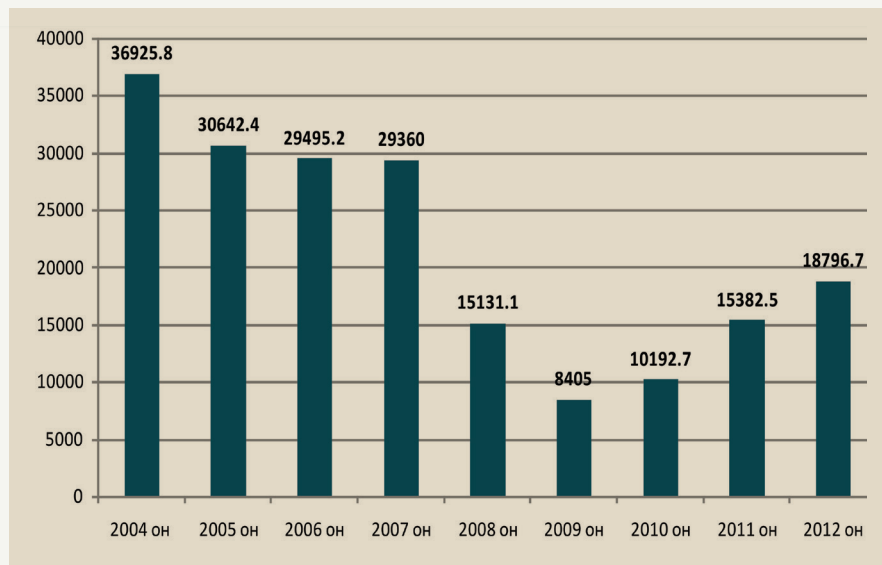
She added that much of the work-

force had been lost to the mining sector, which can offer higher wages to the country's most talented workers.

N. Tserennadmid, director of Deed Ungu said, "If the legal setting improved then access to equipment and greater technology, enhanced capacity, and the ability to place products on the international market would enhance, too". "Nobody", said Tserennadmid, "would hesitate to offer their products to meet that demand. Unfortunately, most of the factories have only just started operating. They need both financial support and support for technological improvement".

She said that warm clothes and »

Chart 3. Total textile production /million MNT/





▶ garments for temperatures as low as -50 degrees Celsius could be made by Mongolian producers. Although raw material manufacturers have just started their operations, it is probably just a matter of time before they create their own brand of clothes for sale around the world. Mongolia's cashmere and wool industry has been developing for thirty years and is unique to products from other brands. Yet most Mongolians wear mostly imported clothes. But according to clothing

manufacture Tsogt Orshikhui's director, Ch. Bayasgalan, the country does have opportunities.

"After our company was established with three persons, we submitted our bids to [Oyu Tolgoi] and succeeded. Then we started providing OT with workwear", said Bayasgalan. "We expanded our operation and now the company exports 12 types of workwear to Rio Tinto's copper miners at Kennekott, Utah".

"By increasing our production capacity and the number of employees, we can export our products to the other countries. Now the company has nine employees."

GB of Mongolia has produced underwear and clothes for sleep for four years, exporting seven to eight types of pajamas and 18 to 20 types of bras

to some U.S. cities. The company's director Sh. Enkhsetseg said that the company hopes to gain popularity in the world, as does traditional costume producer Mongol Costumes and shoe producer Noyon Gutal .

Although there is not much opportunity for Mongolian designers among the market for high-fashion garments, there might be some demand for industrial clothes. Mongolia is one of the world's 13 coldest countries and its climate is the harshest. People here usually wear a variety of warm clothes, and for some foreigners it is a matter of survival.

"In order to introduce ready-made garments to international markets, garment factories need to be built near border points", said Narangerel. "First of all, felt products, shoes, warm clothes and ready-made garment factories need to be established at the Altanbulag border point. Consequently, foreigners will buy our products and sales will grow".

In other words, the country needs ▶

Chart 1. Textile product exports /thousand USD/

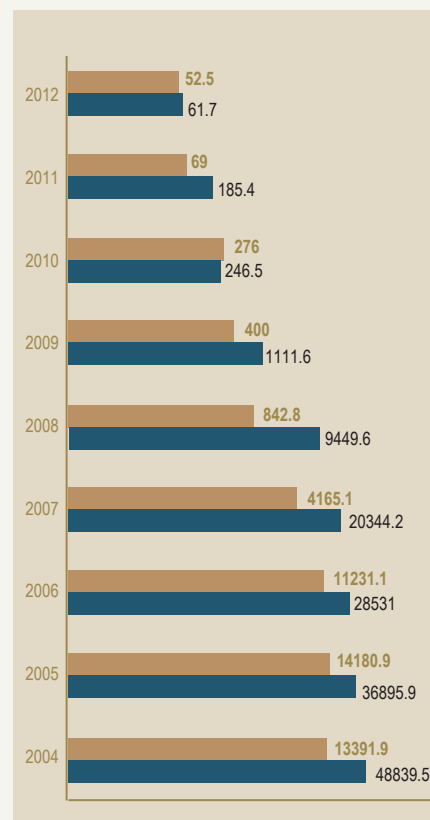


Chart 2. Total textile product sales /million MNT/



▶ many more factories producing clothes with the label “Made in Mongolia”.

Narangerel added textile facilities were needed nationwide. She emphasised the importance of producing towels, napkins and fabrics for household and industrial use. This would lead to greater competition and be considered a big step forwards towards the international market. Some measures have been already taken by the state for the garment industry. For instance, the Development of Ready-made Garment

Production project is underway, with three phases being implemented between 2003 and 2015. Although some criticise that the project’s implementation is slow, it has resulted in the import of spare parts as well as raw and auxiliary materials for textile production because of the tax exemptions it introduced.

Government’s targeted support of production to replace imported products bore WINTEX insulation material, which was invented using sheep and camel wool. Also some eight types of warm clothing have been tested. Now only a

few steps are left before the world market opens its doors.

Although the textile industry was a main pillar to the economy during the Soviet era, its place over the broad spectrum of the economy has fallen over the last two decades. But the industry is likely to be resurrected. As a result of economic diversification and strong coordination, a brand of garments could represent Mongolia. Hopefully that can happen soon so Mongolia can introduce its unique designs to the world. ■



WORKING TOGETHER TO ADDRESS DEVELOPMENT CHALLENGES



Robert Wihtol,
Director General for East Asia,
Asian Development Bank



Robert Schoellhammer,
Country Director for Mongolia, ADB

Two Decades of Cooperation

Mongolia became a member of the Asian Development Bank in 1991, a time of severe economic contraction and great uncertainty for its citizens. Subsidies from the former Soviet Union had fallen away, unemployment skyrocketed, purchasing power plummeted, and the intricate system of social services was unraveling. Today the picture is very different. Mongolia’s economy is growing rapidly, poverty is on the decline, and Mongolia’s

citizens have maintained a high education level.

ADB is proud of its close partnership with Mongolia, and is pleased to have been able to contribute to the country’s remarkable turnaround. In the past 20 years, ADB has provided Mongolia with over US\$1 billion in grants and concessional loans, and has been the country’s largest source of multilateral development finance.

In the 1990s, ADB worked closely with the government to support Mongolia’s economic transition, strength-

en transport infrastructure, and reform the provision of education and health services. Subsequently, ADB provided financial, technical and policy support in areas ranging from urban infrastructure, agriculture, energy, and finance to social protection and the modernization of transport in Ulaanbaatar.

At the heart of ADB’s operations are practical programs and projects that have made a difference to the lives of ordinary people. These range from pupils studying at primary schools to businesspeople travelling through Ulaanbaatar’s international ▶▶

▶ airport, patients at a clinic in one of the vast ger districts, or urban residents enjoying secure heat supply in the world's coldest capital.

The Importance of Macroeconomic Policies

Mongolia's medium-term economic growth prospects are widely regarded as favourable, with commercial production from the Oyu Tolgoi copper and gold mine scheduled to begin in mid-2013 and the Tavan Tolgoi coal mine at an early stage of development. Mongolia is fortunate to have abundant natural resources, which provide a unique opportunity for economic development. Mining revenues can help to finance critical infrastructure, core public services and

social welfare programs that benefit sustainable development and help to reduce poverty.

Reality, however, can also be very different. Countries rich in natural resources often grow more slowly and perform less well on human development indicators than more modestly endowed countries. Resource dependence can exacerbate income disparities, as resource extraction creates few jobs and a small proportion of the population may secure most of the income. For example, in 2012 the mining sector in Mongolia created 90% of exports, 17% of government revenue and 18.6% of GDP, but less than 2% of employment.

An excessive focus on natural resources entails economic risk, most

notably from the "Dutch Disease", which puts upward pressure on the exchange rate, causes high inflation, crowds out of the private sector, and increases vulnerability to external shocks. The mining industry in Mongolia is at an early stage of development, but symptoms of the Dutch Disease are already evident. A procyclical fiscal policy has led to sharp increases in expenditure, which will challenge the limits established by the country's own fiscal stability law.

The government may need to undertake substantial fiscal and monetary tightening to control inflation, which remained in double digits throughout 2012. Overly expansionary fiscal policy has increased the vulnerability of the economy to external shocks. A further fall in global com- ▶



▶modity prices would have a severe impact on Mongolia's economy, and put pressure on public finances and the current account. We should not forget that Mongolia was one of the most seriously affected countries during the global economic and financial crisis in 2008-2009, due to its high dependence on mineral exports and a history of pro-cyclical macroeconomic policies.

Diversifying the Economy

Addressing these risks and vulnerabilities is a key challenge for the government. In addition to maintaining sound macroeconomic policies, Mongolia will need to diversify the economy and create employment by encouraging investment in non-mining sectors and developing its human resources.

There is significant potential for Mongolia to diversify by developing value chains for high-quality, locally-made products. The opportunities range from fresh milk and meat to various wool, cashmere and leather products. Rich raw materials including livestock and wild berries offer much potential.

Establishing genuine Mongolian brands, and developing rigorous quality control and standardization of products, would help Mongolian companies to penetrate overseas markets. This potential has not yet been unleashed due to the lack of investment and limited professional skills.

The services sector also offers scope for development. In 2012, it accounted for 43.3% of GDP, compared with 6.2% for manufacturing. Mining services companies are small, but growing fast. Tourism has a small but expanding business base in Mongolia and significant potential to create employment. The logistics industry, which is currently in its infancy, is also regarded as a growth industry. Mongolia is a natural transit route between the People's Republic of China (PRC) and the Russian Federation, and pro-

vides a short route for Central Asian goods to reach the Pacific.

ADB has been working with the government on a number of fronts to overcome constraints. The ADB-funded Agriculture and Rural Development Project is supporting the development of agro-processing companies, and has already achieved significant employment generation in peri-urban and rural areas. It has also introduced brand marketing.

Under the Central Asia Regional Economic Cooperation program, which includes ten countries, ADB is working to strengthen sanitary standards that will allow Mongolia to export meat products readily to neighboring markets, including the PRC and Japan. It is important to remember that Mongolia has over 40 million head of livestock. Agriculture and animal husbandry remain much larger employers than mining. A new ADB-funded project to prevent transboundary epidemics among livestock will also help develop this nascent business.

Providing Jobs and Raising Incomes

The provision of decent and sustainable jobs is the key to ensuring that Mongolian citizens have adequate livelihoods. This requires a multi-faceted approach. While mining generates export revenues and growth, most jobs in Mongolia are provided by small and medium enterprises. First, the basic building blocks for enterprise development must be established, including a good transport network that allows companies easy access to their customers and suppliers, and reliable power supply.

Second, Mongolia needs to develop a modern and skilled labor force. Structural changes in the economy, greater openness, and the growing use of technology, including information and communication technology, have led to a rapid increase in the demand for skilled labor. Currently there is a mismatch between existing rela-

tively low skill levels and the needs of the labor market. Workers' skills need to be raised and geared to meet market demand to support economic diversification, and to raise the incomes of the poor.

Third, the role of the financial sector is crucial, to provide capital for businesses to develop, and to mitigate risks that companies face. Small and medium enterprises need both access to finance and supportive governmental policies to thrive in a secure and stable environment.

Working Together in the Future

In ADB's partnership with Mongolia we have jointly confronted many challenges – the difficult transition to a market economy, a series of very harsh winters, and recently the global economic and financial crisis. Mongolia weathered all these crises admirably, and today is a forerunner among transitional countries for its achievements in establishing a market economy.

Mongolia has recently joined the ranks of other fast-growing economies in the Asia and Pacific region and is currently considered a lower middle-income country. In recognition of its sound economic performance, in 2011 Mongolia also gained access to ADB's ordinary capital resources, alongside ADB's concessional lending. Given its AAA credit rating, ADB makes funding available for development projects on attractive terms.

ADB is currently working with the government to provide financial, technical and knowledge support in areas as diverse as urban infrastructure, ger area development, technical and vocational education, and financial sector development. ADB remains committed to a partnership with Mongolia that addresses new challenges and ensures that Mongolia's growth is both sustainable and inclusive. ■

Nigel Finch is an associate professor and director of admissions at the University of Sydney Business School (Australia). Finch has considerable experience in the field of business regulation and economic development across Asian and emerging economies and is actively involved in market development and institution building throughout Asia. He is a member of the Business Council of Mongolia and a consultant to the Australian Agency for International Development currently providing specialist advice to a range of Mongolian public sector agencies including the Mongolian Ministry of Finance, the Financial Regulatory Commission of Mongolia, and the Mongolian Stock Exchange.



Photo by E. Zorigt

SOLUTIONS

TOO MANY STARTS AND STOPS

What first brought you to Mongolia?

I've been coming to Mongolia since 2009. My interest is in emerging and frontier economies, and their economic development. I'm particularly interested in debt and equity capital requirements as they're growing. It didn't take long since the OT agreement was close to being established, and it was clear that the Mongolian market was open and growing. It was probably the catalyst for me to come here.

Having said that, I've spent a lot of time in Southeast Asia with other economies, which in some respect might be a

little more developed than where Mongolia is today. I've come here many times to talk at conferences and forums. Also I've been involved in delegations where Mongolians visited Australia as well for trade. We've taken Mongolian entrepreneurs to tour around Australia, down to Melbourne in particular, through to diplomatic trade missions where I've had the opportunity to meet the former prime minister in Australia.

I've been a very keen follower of development in Mongolia. It's not a very transparent country so it's difficult to get information, but it's also a relatively small economy that's really built a cou-

ple fundamental transactions. So knowing what to watch can give you a fairly strong read about what's happening with the economy.

Mongolia's democracy is only about 23 years old, and this rapid growth has only begun over the last few years. These changes are rapid. At the same time, Mongolia is experiencing many great challenges. What risks await Mongolia in this rapid pace towards growth?

Well, what's Mongolia's role? Mongolia doesn't have a massive population, so it's unlikely to be a hub for consumerism in the way China is. Mongolia ▶

▶ doesn't have highly developed industrial processes or capabilities, so it's not going to be a high-technology, manufacturing assembly area.

What it does have is minerals, and the mineral wealth is the key to unlock and transform Mongolia. Mongolia's role is the most obvious pathway for Mongolia, which is to develop the mineral wealth.

I think from that will come a whole bunch of future options for Mongolia, but right now the economy is so fragile that what's

required is significant investment to bring these resource bases online and put them into the global supply chain. I think the issue for Mongolia is if there's too much uncertainty around how major infrastructure investment and foreign direct investment is to be made in Mongolia then what will happen is the international investors will turn their back on Mongolia and find other liberalised emerging frontier economies.

Myanmar is a very good example, formerly Burma in Southeast Asia. It has direct port facilities, enormous reserves of mineral wealth, one of the largest orders with China, and a government which has just opened the doors to an embryonic democracy. What is apparent in Myanmar right now is a willingness of the government to look at, in a very sensible way, how to secure foreign direct investment and how to start to making the necessary investment in a much-less-developed economy than Mongolia is today.

The big issue with Mongolia is there are too many stops and starts in relation to foreign direct investment, and I think the IMF has had in the 23 years of Mongolia's democracy as many as six bailouts where the economy runs out of steam and needs to be re-injected. That's every four years. It seems to be a cycle where the planning and execution doesn't line up, which requires bailing Mongolia out.

What kind of mining strategy would you recommend for Mongolia? How can we move away from this situation where other sectors are suffering while mining flourishes?

Suffering may be around wage inflation. There's a shortage of skilled labor because a decade ago the demand for people experienced in property construction probably didn't exist — everything from infrastructure through to building skyscrapers and these sorts of things. The issue here for the entire population is, I'm sure, many of the careers that Mongolians are involved in today didn't exist five years ago or ten years ago. Certainly, there's going to be this long process of people entering new careers, and that's going to require an enormous effort in training and work experience opportunities.

How are these challenges resolved elsewhere?

It's resolved by using foreign workers who come in with particular expertise and knowledge. And there's very clear processes for knowledge transfer; so that's taking knowledge from experienced workers and transferring that to Mongolians while taking knowledge from experienced Australian mining engineers who transfer that into the Mongolian economy.

There has to be that transfer. To say that there's just not enough skilled workers in a population of three million with a massive unemployment rate, I don't think that's necessarily an impediment to growing an economy.

I'm pleased that there's 10 OT-style projects here. But should they be done all at one time or in succession? Well I think there's certainly benefits in doing more simultaneous projects to get efficiencies in building the necessary ▶



► infrastructure. Infrastructure costs are enormous in these major capital projects. We've seen already what's been invested in stage one of OT—USD 7-8-10 billion dollars, which is twice the size of the GDP of the country since that project started and has been the major catalyst for opportunity here with probably 10,000 vendors. Mongolian businesses, earning that money. More of these projects is what's required. I think doing simultaneous projects allows you to build the infrastructure and the corridors and power plants that will feed multiple projects. This is what's really required to make it economic.

What other sectors do you think can grow as large as mining in Mongolia?

I think the financial services sector will play a very important role. But I think that given the challenges that Mongolia faces politically and geographically as well as the challenges with a workforce transitioning into a more developing economy with very different sorts of jobs with things like the uses of computers as a mainstay skill, being multilingual and able to speak to customers in Korea and suppliers in Japan have become the skill base needed for Mongolians. I think that's going to take some time to transition through.

The Australian economy, as a parallel, was based all around mining and agriculture. Today what's being called a "twin speed economy", where we've got this primary production, which is very important to the Australian economy, and we've also got other sectors, largely property and financial service. To build up the financial services sector has taken huge investment in education to bring the development of world-class financial systems to really build that capability. With its undeveloped capital markets and its embryonic forms to banking, insurance and these sorts of issues, it's clear there's a lot of work that needs to be done institutionally. There's a lot of work that needs to be done in training people to even start building an economy like that. The future for Mongolia is very bright, but it starts with mining.

What do you think about the lack

of certainty to how the money from the USD 1.5 billion bond will be used?

The government had the legislative mandate to raise the capital. There has been a national economic innovation committee in Mongolia, which has had project proposals. And with the Development Bank of Mongolia there were clear restrictions on what they could not invest in. It wasn't designed to invest in funding a government deficit or something like this.

There were clear priority areas for investment for railways, roads, and the like. They've gone ahead and raised the capital. That's happening; it is USD 200,000 a day. The interest accruing on these bonds must be paid back by the Mongolia government. A national development economic plan might be a plan that identifies what the priority projects are and gives investors confidence around where else they can invest. For example, if the project is to build a railroad between City A and City B, and that clearly is understood, then what that does is allow property developers to make investments in City A and B and services sector investments to start to get ready for this inevitable economic development that is happening.

I think what is happening is there is a list of projects to invest in, but there's no certainty over which are going to be done. Which makes it very difficult for Mongolia to benefit from. It's too speculative, what's happening. A national economic plan might be a plan that identifies what the priority areas are, what the time tables are for these, and also how they're going to be funded. I don't think that's clear in the mind of Mongolians or foreign investors.

Do you think the anti-corruption measures in Mongolia are effective?

The corruption in Mongolia is well understood. Transparency indices and metrics don't look so favorable for Mongolia. That's well understood. I think the issues around how Mongolia deals with that, for example laws of what we might call politically exposed people such as a spouse or family member of a politician and their assets, are common all around the world. I wouldn't say it's

something unique to Mongolia, but yeah it's a move in the right direction.

It's not just preventing politically exposed people from having bank accounts overseas. I think the corruption measures go into aspects around transparency and reliability and management of state-owned enterprise. TT is a very clear example that it's not an efficient process, and where that lack of efficiency exists some might feel there's a layer of corruption that may exist within it because there's a lack of transparency. In the press just recently MIAT had the USD 5 charge levied as war insurance. It's yet another example of where the auditors for this state-owned enterprise weren't able to identify that that USD 5 went to someone else's bank account. From an audit process that should have been picked up in the accounting period in which it happened.

The state-owned enterprises are bloated with labour. They have very poor efficiency metrics, and they're very, very costly. Some in the media have said these state-owned enterprises have essentially been plundered by factions of Mongolia or perhaps government officials, former government officials, or state-owned business groups.

What kinds of experiences can Australia share with Mongolia to lead it to sustainable growth with a sustainable economy?

I think Australia has great skills in mining, but what makes it sustainable is a legislative framework that is stable and well understood. These are very long-term projects. A mine isn't a two-year project like a property development where you buy the land, quickly get some plans developed, erect it, develop, and sell it in say two or three years. These are projects that might require 30 or 50 years, and there needs to be a reliable regulatory framework that exists over a large part of that so the planning can be done.

I think the regulatory framework and financial market that can exist alongside that are key to making this work. I think both of those are really underdeveloped in Mongolia, which makes it challenging to do large-scale projects. ►►

► **What kind of advice have you given to Mongolia's agencies?**

I think right now is a challenging time for the Mongolian government to talk to foreign investors when the Minerals Law is still being debated. There's still a lack of clarity around the national infrastructure investments and how they'll be funded. The advice for the Mongolian government is really around how to start to deal with some of the criticisms surrounding sovereign risk from the international investment community and how to improve its transparency.

The best way to look at that would be Mongolia's sovereign credit rating. The sovereign credit rating issued by Moody's, Standard and Poor's, and the like gives an indication to the credit worthiness of Mongolia as a counterpart to do business in. Right now Mongolia's sovereign credit rating is ranked as non-investment grade. That doesn't mean there's not investment happening here. What it means is foreign investors, foreign sovereign wealth funds, and foreign mutual funds are precluded from investing here. Also the analyst reports from credit-rating agencies identify areas where there is weakness.

The advice to the Mongolian government is to start looking at these criticisms, look at these areas where on international benchmarking they are deficient, and start to develop some mechanisms to improve those areas. What that will do is start to improve the sovereign credit rating. That would help the entire Mongolian economy. Right now they've raised USD 2 billion, but the estimate is somewhere between USD 60 billion and USD 80 billion required investment in the Mongolian economy. There's a lot more capital raising that would need to happen to make this happen.

Improving the sovereign credit rating would reduce that. If we think about USD 60 billion as a round number, a 1 percent reduction in the interest rate on that is USD 500 million every year in savings. If you can start to address some of the criticisms, some of the obvious defects in the Mongolian public sector institutions, it would help improve that sovereign credit rating. At the same time other benefits are high levels of accessibility for direct foreign investors, the ability for Mongolian banks to improve their individual credit ratings as well so they can start to participate in the broader international financial markets, and easier access to foreign capital for Mongolian businesses.

The advice I would give the Mongolian government is to start to look at its investor relation efforts and how Mongolia can train itself to the international investment community, in particular to analysts from credit rating agencies, and try to focus on those areas in the short term.

What advice would you present to the Mongolian Stock Exchange?

It's going to find its own market. I think insisting companies that do business here over a certain size to have some of their capital listed on the Mongolian Stock Exchange doesn't do anything for what we call market integrity. Companies should be free to choose which exchanges they want to list their securities on, and I think those companies are looking at foreign exchanges and jurisdictions where there is the highest level of market integrity. This would be an informed and active financial market, a robust regulatory framework and limited information asymmetry—the idea information is shared on a timely basis throughout the economy so that all investors are informed.

I think there is a lot of challenges for the Mongolian Stock Exchange. As a capital market there isn't an active and liquid market. There are regulatory issues on the stock exchange. Anecdotally, what I've heard is many of the companies interested in listing on the stock exchange haven't even filed financial accounts for years. That doesn't suggest in any way that there's a level playing field for companies to list on the stock exchange in terms of compliance to laws and that news flowing through Mongolia is difficult. Right now it's very difficult for investors to buy and trade on the Mongolian market.

The partnership with the London Stock Exchange will provide great transfer of skills and technology. But still the market itself needs to be developed and the regulatory framework needs to be robust.

I think there's a lot of challenges ahead in terms of making that happen.

One area I think there could be some interest in activity might even be the Mongolian-owned investment funds that exist and can exist. We know obviously the important role a sovereign wealth fund can play in immunising a nation against the "Dutch disease". Another area is the social welfare. If the retirement fund that has existed in Mongolia could be active financial market participants, they could provide more liquidity into those markets as well. I've yet to see any evidence that the social welfare funds in Mongolia have a mandate for existing outside a consolidated government revenue

Do you think the Mongolian Stock Exchange should be privatised in the near future?

I think it could be privatised if it was a successful and viable business. I think the business model needs to be proved. As for the exchange itself, we understand how these things work, but it's really the market and the regulatory framework around that market that really needs to be brought up.

The MSE could be privatised but I think there's other, more attractive assets that could be privatised in the short term rather than the stock exchange or national airline. ■

POLICY SURVEY

THE IMPACT OF THE FISCAL STABILITY LAW ON THE MONGOLIAN ECONOMY

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The following is a brief conclusion on the impact of the Fiscal Stability Law on the Mongolian economy. The study was conducted by the Economic Research Institute, and developed by Dr. Ragchaasuren Galindev (Gerege Partners LLC Queen's University Belfast).

During the economic boom between 2005 and 2008 originating from the soaring commodity prices in the world market, the government revenue increased dramatically through increased proceeds of copper and gold mining companies. In fact, the price of copper per tonne increased from USD 3,675 to USD 6,731 between 2005 and 2006. At the same time, the price of gold increased by about 26 percent. As a consequence, the nominal government revenue excluding grants and transfers increased by 62 percent between 2005 and 2006, by 37 percent between 2006 and 2007 and by 15 percent between 2007 and 2008 according to the National Statistical Office (NSO). On the other side of the fiscal balance, the government expenditure increased by about 61 percent between 2005 and 2006, by about 40 percent per year in the next two years. During the boom years, real GDP grew, on average, by 10 percent annually. The crisis in 2008 hit the economy hard—the price of copper per tonne fell from around USD 7,000 to almost USD 5,100 between 2008 and 2009. The effect on the economy was direct—it shrank by 1.6 percent in 2009. It was partly due to a decrease in government spending which fell by 5.7 percent in nominal value originated by a 8.6 percent decrease in government revenue. Given these figures, one can conclude that contemporaneous correlation between government revenue and expenditure has been high and positive. In addition, the inflation rate was 6.8 percent in 2006, 17.8 percent in 2007, 22 percent in 2008 and 4.4 percent in 2009. Mongolians learned a lesson from this experience that pro-cyclical macroeconomic policy amplifying the effect of external shocks is not a right one for our economy, especially ▶



- ▶ in the current environment where the mining sector is expanding so that the economy is more exposed to the volatility of commodity prices. Many experts, economists and politicians suggested that we should have saved more during the boom rather than spending so as to maintain the health of the economy during a crisis—i.e., countercyclical policy. As a result in 2011, the Mongolian parliament approved a Fiscal Stability Law (FSL) which spells out the rules for the stability of the growth rate of government expenditure. The parliament has recently approved the budget for 2013 which is constructed on the basis of the FSL.

In this research, we develop a dynamic and small open economy Computable General Equilibrium (CGE) model to examine the effect of the FSL on the Mongolian economy. Our CGE model is based on the Input-Output (IO) table of Mongolia which was constructed in 2005. It is a small open economy model—i.e., the country takes the prices of all goods exogenously. The model is also recursive dynamic as it has capital stock and foreign debt. In that sense, the model is an open economy, multi-sector extension of the Solow model. The model considers static expectations about the future events—i.e., the current events such as current inflation are used as proxies for the corresponding events in the next period. The model has the following equations in each period of time:

- Household demand for each product
- Investment demand for each product
- Government demand for each product
- Export demand for each product
- Industry (or producers') demand for each product and production factor
- Supply of each product and production factor
- Production cost and purchasers' price
- Normal profit conditions
- Market equilibrium for each product and production factor
- Various macroeconomic indicators such as GDP, GNP, a balance of payment, price indices, etc.

The transactions between the industries (suppliers of goods and services), final users (households, government, investors and exporters) over commodities and production factors (labour, capital, natural resources and land) are based on the decisions derived from the profit and utility maximisation problems.

The model parameters are calibrated (validated) to replicate the main characteristics of the economy as of 2012 to be used to predict the effect of the FSL over the next few years. In doing so, we first aggregate the 55 industries in the 2005 IO table to the following industries: Livestock, Other agriculture, Fishery and Forest, Oil, Gas, Thermal coal, Coking coal, Washed coal, NonOT copper, OT copper, NonOT gold, OT gold, NonOT minerals, OT minerals, Petroleum, Electricity, Manufacturing, Transport, Construction, Health, Education, Public administration and Defence, and Service. Then, we simulate the model by imposing certain targets consistent with the available data observed between 2005 and 2012 to generate the IO table as of 2012. The targets include the average GDP growth, the average GDP deflator inflation, the composition of GDP into consumption, investment, government expenditure and net exports, the average growth rates of gross output of some industries and the average changes of price indices in some industries (e.g., coal, gold and copper prices). From this simulation, we validate the parameter values. The results suggest that the model needs to improve in certain areas as some variables act quite differently from their observed values. This will certainly be the focus of our future research.

The main point of the FSL is that it restricts the growth of total government expenditure. Any excess government revenue will be saved in a Fiscal Stability Fund which contributes to the national savings. The fiscal stability fund is supposed to be at least 5 percent of GDP and the fund in excess of 10 percent of GDP can be invested into the economy through the Development Bank and the Human Development Fund subject to meeting certain conditions such as inflation. In this research, we are concentrating on the period between 2013 and 2015 which seems a natural given the newly-approved budget for 2013, and it is known as a medium term for the government. In that respect, investment from the Fiscal Stability Fund into the economy seems quite remote. In this report, however, we only present the results for 2013 from various simulations.

As mentioned earlier, the Mongolian parliament has recently approved the 2013 budget on the basis of the FSL. According to this, the total government expendi- ▶

¹ The author would like to thank Economic Research Institute at the National University of Mongolia for financial support. Please notice that this is an ongoing project so that the results are preliminary.

² The 2005 IO table does not provide the transactions which would appear in a Social Accounting Matrix (SAM) – i.e., a less transparent picture of the economy. For example, it does not show the sources of household incomes (e.g., labour compensation, capital income and transfers) so that the model requires an assumption.

³ All the optimisation problems have a nested structure. In other words, optimisers solve for the demand for each product and choose their sources (i.e., either domestic or import) simultaneously. We assume Cobb-Douglas utility functions for households and government while Leontief production functions for industries in which production factors enter in a Cobb-Douglas fashion. For the preference between domestic and imported, we assume Constant Elasticity of Substitution functions.

ture is allowed to increase by 18 percent in nominal terms in 2013. As our model is not based on a Social Accounting Matrix, it does not consider the full extent of government total revenue and expenditure. However, it considers government spending and tax revenues which are the parts of the government budget relevant to the system of national accounting. Assuming that nominal government spending will grow at the same rate as total expenditure as outlined in the 2013 budget (18 percent), we simulate the model for 2013 in four different environments—a baseline case, an optimistic case, a pessimistic case and a case without the FSL. In the baseline case, the price of main mining products follow what the government anticipates for 2013 which are substantially lower than those in 2012. For example, the price of coking coal and copper are expected to be about USD 80 and USD 6,329 per tonne respectively. In the optimistic case, we assume that the prices will remain the same as those in 2012—i.e., USD 106 for per tonne of coking coal and USD 7,471 per tonne of copper while everything else remains the same as those in the baseline case. In the pessimistic case, the price of the main mineral goods is uniformly 10 percent lower than those in the baseline case. We also simulate the model without imposing the FSL. More specifically, the growth rate of nominal government spending takes its historical average of 26.7 percent while everything else remains the same as those in the baseline case. The following table compares some macroeconomic variables across the cases in terms of their growth rates.

Macroeconomic variables (%)	Baseline	Optimistic	Pessimistic	Without FSL
Real export	38.07	38.78	39.35	37.71
Real GDP	23.59	23.65	23.23	23.60
Real imports	19.19	19.53	17.97	19.84
Tax revenue	25.50	27.13	26.03	25.75
GDP deflator	5.85	8.97	3.81	7.01
Mining sector output	44.30	44.64	43.93	44.30
Non-mining sector output	11.26	11.17	11.61	11.63
Real wage	12.34	12.44	9.98	14.28
Nominal national saving	34.97	42.72	29.82	34.88

As can be seen, there is significant volatility in the inflation rate measured by GDP deflator, real wage and nominal national saving whereas GDP growth, real export growth and growth of non-mining sector output are quite stable as we enter the production projection of the mining sector and the unemployment rate exogenously. Endogenising them depending on the price changes may lead to different results.

The following table shows the growth rates of gross output of selected industries. As can be seen, the results vary more noticeably at the micro level.

Growth rate of gross output (%)	Baseline	Optimistic	Pessimistic	Without FSL
Livestock	3.18	3.05	3.38	2.39
Other agriculture	0.68	0.58	0.37	0.06
Electricity	8.50	7.53	9.17	7.85
Manufacturing	3.87	3.60	9.18	2.79
Transportation	24.49	25.02	23.8	24.07
Construction	18.91	18.96	18.81	19.00
Health	4.80	4.39	2.35	8.52
Education	2.16	1.79	1.76	6.05
Public admin. and defence	4.03	3.64	2.78	10.52
Service	10.05	9.95	9.49	9.62

Given these results, we believe that the FSL is doing its job in a volatile environment. It is observed that the government budget deficit decreases in the first three cases as government spending increases at an exogenous pre-determined rate (18 percent) to meet the requirements set out in the FSL. Moreover, GDP growth is rather stable while national saving is more volatile as it absorbs the changes in the commodity prices. The results from without the FSL case in comparison to the baseline case also suggest that the FSL leads to lower inflation, lower current account deficit and an increase in non-mining industries except for health, education and public administration and defence.

We understand that there is room for improving the model's performance, especially for the period between 2005 and 2011 by choosing better values for the parameters. Nevertheless, we are not concluding that the model is not good enough. As an equilibrium model, it is doing a reasonably good job. There are about 10,000 variables and over 8,000 equations in the model. About 2,000 of them are exogenous variables so that their values are supposed to be entered in every simulation. It is, however, not practical as we simply do not know their values. The performance of the model depends on the usual suspects that are the quality of the data and the specification of the model. Ideally, we want a method which can choose the values of the parameters and the exogenous variables simultaneously in the process of minimising the difference around the targets. We will search for such a method and a programme in the literature. ■

⁴ This approach is common in the literature. The reason is that traditional estimation approach of CGE model parameters has several problems. One of the main problems has been lack of information, mainly in developing countries. Given large number of parameters to be estimated, long time series data for numerous variables are required to provide sufficient degrees of freedom for estimation. For this reason, it is common to adjust parameters informally to meet target observed variables. However, we admit that adjusting parameter values in this way needs a more structured approach than ours and we will work on that in the future.

⁵ In addition to these, we enter the projection of the productions of copper and coal industries in the model exogenously.



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