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ECONOMY

BUILDING A STABLE LEGAL ENVIRONMENT

SAM WALSH: MONGOLIA WAITS AS GOVERNMENT
DECIDES ON RIO'S "BEST AND FINAL OFFER"

THE NEW DEBT MANAGEMENT LAW AND RELATED
ISSUES

CREDIBILITY

THE FIRST STEP TOWARD
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EDITOR'S NOTE



Dear readers, subscribers, and Mongolia Economic Forum guests and delegates,

Four years ago, Mongolian Economy magazine released its very first issue at the 2011 Mongolia Economic Forum. The two-day annual event always reminds us of our happy memories when the Forum's participants and guests toasted our accomplishment, saying: "Congratulations on releasing a magazine that is essential to society!" Since then, we have often worked with the Mongolia Economic Forum, participating as the event's exclusive media sponsor for years. We would like to express our gratitude to the staff at the Mongolia

Economic Forum, for always being supportive and cooperative in our partnership.

For that reason, this special issue is dedicated to the 6th annual "Mongolian Davos," as it's locally known. In our 86th issue, we share with you a collection of economic, finance, business and development topics that will be featured in Forum discussions. We are confident that Mongolian Economy magazine reflects the topics, ideas and content that will interest Forum guests and delegates alike, as they assemble under the banner of 'Building Credibility'. The Economic Forum is unique in that it values the participation of every sector in society, and brings these sectors together for shared discussion. In this issue, we've given a voice to people who cannot participate in the forum, to allow them a platform to contribute to the essential dialogue.

As solutions to Mongolia's current economic issues and development will be the main topic of discussion, we've chosen to focus on Mongolia's general vision, stable legal environment, industrial policy, economic partnership agreement with Japan, credit rating, governance, financial markets and tax policies. Here within, our journalists, professional economists, analysts and researchers share news and analysis, to keep you at the forefront of the latest information.

Just as the Forum once praised our achievement, we would like to wish you all the best during this year's Forum and beyond!

I. Otgonjargal



MONGOLIAN NEWS

BANKING SECTOR LAGS BEHIND REGION



Mongolia's banking sector ranked 14th out of 25 countries, according to a Mongolian Bankers Association competitiveness report that compares Mongolian banks to the commercial banks in a selection of East Asian, Southeast Asian, Central Asian and Pacific countries. Four countries ranked below Mongolia in global competitiveness, while five countries had an assessed lower credit rating. The Association concluded that the development of Mongolia's banking sector has surpassed some of the country's social and economic development. After overcoming two systematic level crises in 1998 and 2008, where a total of 17 banks went bankrupt, today 13 banks operate 1,400 branches with 14,000 employees. At the end of 2013, commercial banks accounted for 95 percent of the total assets of the financial sector, and 50 percent of the total financing of GDP; a 10-fold increase compared to 2000.

ASEM IN ULAANBAATAR

Mongolia joined the Asia-Europe Meeting (ASEM) in 2006, becoming an active participant in the summit's activities and initiatives. In July 2016, the 11th ASEM Summit will be held in Ulaanbaatar. A total of 5,000 guests and delegates, including heads of state and government, ministers of foreign affairs, heads of international organizations, and media representatives are expected to attend the summit. Prime Minister Ch.Saikhanbileg will chair a National Council in charge of organizing and guiding the event. The Prime Minister stressed that Mongolia must pay special attention to this meeting, as the 10th ASEM Summit in 2014 brought 53 heads of state, prime ministers, and other top dignitaries to the host city of Milan, Italy.

ADB REPORT ON GROWTH

The Asian Development Bank released in late March an assessment of Mongolia's current economic situation and future prospects. Last year's economic growth slowed to 7.8 percent. In 2015, GDP growth is expected to decline to 3 percent. Last year, the mining sector accounted for 4.8 percent of growth, while the agricultural and service sectors accounted for the rest, and other sectors showed no growth. The construction sector is expected to drop throughout the year because of the declining demand for mortgage loans. Economic growth shows signs of continued decline, as money supply drops due to government loan repayments. Expectations for 2015 predict the agricultural sector will add 1.4 percent growth to the total economy; mining and other manufacturing industries will account for the rest of this year's growth.

NEW CLEAN COAL PLANT



Mongolyn Alt (MAK) Group and Germany's Siemens are cooperating to establish Mongolia's first coal gasification plant. The project team completed a feasibility study to build this plant at the Aduunchuluun coal mine; the design of a 10 km long rail and a local water analysis remains to be done. Mak LLC plans to give the USD 2.3 billion investment project to commission in 2019 or 2020. The plant is able to produce 400,000 tonnes of gasoline and 17,000 tonnes of liquefied petroleum gas per year. These production numbers amount to 30-40 percent of Mongolia's yearly fuel consumption. Germany's Thyssenkrupp Group is working on an additional project to build a coal-to-liquids plant. They cooperated with ICM and the US's ExxonMobil on a feasibility study based on the Tugrug lake deposit. The project is estimated at EUR 1.7 billion.

GROWING ENERGY DEMAND

The Energy Agency of Mongolia presented an estimate that Ulaanbaatar's electricity demand will grow by 531 mw in 2015 and 2,361 mw in 2030. Sector experts say that the existing power plants are insufficient to ensure the future demand, and warn Mongolia might need to import electricity. Thus, there's an urgency to build new energy sources. The energy sector is determined to provide enough for domestic consumption, enough to even export electricity. In this regard, preparations for Thermal Power Plant Number 5 are underway. Recently, project investors emerged, with financing as follows: Newcom Group, 10 percent; France's GDF Suez, 30 percent; Sojitz Corporation (one of the six largest Japanese trading companies), 30 percent; South Korea's Posco Energy, 30 percent. Power Plant 5 is estimated to have a capacity of 820 mw. It will consume 2.5 million tonnes of coal per year, and generate twice the current electricity and heat produced for Ulaanbaatar today. The plant has the capacity to refine 100 percent of its coal emissions and filter 99 percent of ash, which can be used in construction materials. Construction is to launch this year in order to provide Ulaanbaatar and Mongolia's central region with energy.

CEO APPOINTMENT

Director of the Securities and Central Depository Center LLC T.Gandulam was removed from duty by the decision of the board of directors in January. At a meeting held on March 25, J.Aldarjavkhlán was appointed as the acting executive director of the company. He had previously served as the director of the Housing Fund Corporation.

WORLD NEWS

CHINA'S BOAO FORUM

At the Boao Forum in late March, President Xi Jinping sketched out China's vision for a new security and economic order in Asia, offering to spread the benefits of Chinese prosperity and cooperation across the region. In a speech to a regional forum Saturday, President Xi presented China as a part-



ner willing to “jointly build a regional order that is more favorable to Asia and the world,” according to The Wall Street Journal. He highlighted the new China-led Asia Infrastructure Investment Bank (AIIB) and other initiatives designed to leverage hundreds of billions of dollars to finance railways, ports and other development projects, and foster regional economic integration. At the center of these efforts is the AIIB and plans—entitled ‘One Belt, One Road’—to build infrastructure across Asia and along the maritime routes that historically connected China to the Middle East, Africa and Europe. The plans have been welcomed by many countries (including new members Australia, South Korea and Russia) and companies throughout the region, which the Asian Development Bank estimates is in need of trillions of dollars of infrastructure. President Xi stated that over the next five years, China would import USD 10 trillion in goods, and invest USD 500 billion abroad. Mongolia is a founding member of the AIIB. The Boao Forum, which was conceived as an Asian version of the World Economic Forum in Switzerland, has typically focused on business and economic matters.

MODI TO VISIT MONGOLIA

After his forays to the US, Australia, and Europe. Indian Prime Minister Narendra Modi has set his sights on the strategically-important East Asia region, dominated by China, a geopolitical rival to India. Prime Minister Modi will undertake a three-nation tour of China, Mongolia and South Korea from May 14 to 19. According to officials, the visit is aimed at giving a boost to India’s East Asia policy, aligning it with

the ‘Make in India’ initiatives (designed to transform India into a global manufacturing hub) and bringing momentum to the country’s foreign policy in the strategically significant region. Mongolia and India are keen to move forward on the MoU for Uranium supply that the two countries had entered into in 2009. Mongolia is looking for Indian help with cyber security. Assistance in border patrolling is another area where the two countries will be stepping up their ties.

MINING ON SOLID GROUND

In the resources sector, investors are more likely to find steady cash flow in mining than in oil and gas. Both the mining and energy industries have struggled, as prices of commodities have tumbled. For miners, weak economic signals from China weigh on commodities from metals to iron ore, which make spending restraint, cost-cutting and preservation of cash flows the order of the day. Miners started cutting capital expenditures and shelving ambitious projects back in 2012, a shift that was followed by a change of management at big companies including BHP Billiton, Rio Tinto and Anglo American. Rio Tinto’s capital expenditure has more than halved since 2012; today, most miners, according to The Wall Street Journal, can cover their dividends from cash flow in 2015, with Anglo as the notable straggler. Stocks in both miners and oil companies have markedly lagged behind the market this year, and companies that have made harder cuts have been better rewarded. Big Mining stands on firmer ground for the time being, even as commodity forecasts continue to remain low.

CHINA, MONGOLIA ESTABLISH TRADE ZONE

China and Mongolia have agreed to dedicate nine square kilometres on either side of their border to a joint economic zone, in their first meeting on the issue. The two sides met in Erenhot of north China’s Inner Mongolia Autonomous Region in late March to discuss a zone comprising land in China’s Erenhot and Zamyn-Uud on the Mongolian side. They will meet again in April, according to China’s Ministry of Commerce. The agreement over land allocation follows an August meeting between President Ts. Elbegdorj



and Chinese counterpart Xi Jinping in which President Xi stressed the importance of the zone and called for a separate free trade treaty to be signed as early as possible. China and Mongolia share a border stretching 4,710 km. Erenhot, which sits on the route of the China-Mongolia-Russia railway, is the border’s most significant customs checkpoint, accounting for 70 percent of trade between the two countries.

TURQUOISE HILL UPDATE



According to Turquoise Hill’s 2014 review, Oyu Tolgoi achieved a good safety performance for 2014 with no fatalities and a remarkably low rate of injury. Oyu Tolgoi recorded net revenue of approximately USD 1.6 billion in 2014 on sales of approximately 733,700 tonnes of concentrate. During 2014, Turquoise Hill generated its first annual positive operating cash flow of USD 658.3 million. In 2015, Oyu Tolgoi is expected to produce 175,000 to 195,000 tonnes of copper and 600,000 to 700,000 ounces of gold in concentrates, with production distribution expected to be relatively similar to 2014. Contracts have been signed for 100 percent of Oyu Tolgoi’s expected 2015 concentrate production. ■

LAW

Building a stable legal environment

By Elbegsaikhan

In parliament's recently passed 'Resolution on Measures to Overcome Economic Difficulties', there's a subsection entitled 'restoring investor confidence in Mongolia'. In February, just before the week-long break between parliamentary sessions, the government vowed to uphold the first article of the subsection, which states the necessity to: "Keep the legal environment for investment stable, and create a business-friendly environment" at all levels.

Imagine a businessman, expecting a shipment of goods purchased abroad to arrive in Mongolia. At

the border, however, the goods are confiscated by the Mongolian authorities, because during the shipping process, the Mongolian government changed an applicable law. Now that his shipments are being confiscated, the businessman turns into an illegal goods smuggler and is soon arrested and called into court. Does the businessman's situation sound familiar? The business community says similar events have occurred, are occurring today, and will continue to occur, as long as the legal environment stays in its present situation. The country knows that legal uncertainties have scared away foreign investors, but domestic enterprises have as big

a problem with the ever-changing laws.

What solutions are there to the aforementioned example? The best decision is to eliminate the immediate implementation of newly approved rules and regulations. This means that time must be given to entrepreneurs to anticipate new legal violations and amend for old ones. Lawyer B. Amarsanaa said that lawmakers should consider a policy of "forgiving once", if a person shipped his goods before a relevant law was approved.

Unreliable partner

A recent example surrounds regulations in the Investment Law. The initial law was implemented in



Шог зургийг А.Амарсайхан

November 2013, but its regulations weren't approved for a full eight months. And even with the regulations finally receiving approval, the situation still hasn't improved. Former director of the Business Council of Mongolia and the current director of B2B Mongolia LLC I.Ser-Od explained that the unstable legal environment is the disease behind every symptom. When large foreign investors establish an agreement with the government of Mongolia, they think that they've established an agreement with Mongolia. However, when a new government takes office, they deny the agreements of the previous government. This oft-repeated cycle has led the international community to label Mongolia an "unreliable partner".

Random and arbitrary regulations add to the unsustainable situation. Mongolia usually has an original law that regulates matters, but sector ministers have the right to issue their own regulations and demands. Cases where entrepreneurs are found guilty are common, because of the difference between the original law and the minister's decree—follow one and not the other and you could be at fault for both.

A clear example of an unstable Mongolian law is the Minerals Law. Parliament approved the law in July 2006. To date, a total of 14 changes and amendments were added to this law. A total of 152 provisions were amended, added or withdrawn—35 provisions were amended at least twice (including invalidated provisions).

From June 2010 until June 2011, the Law Banning the Issue of New Mineral Exploration Licenses was reapproved three times. The law's regulation implementation period needed to change many times because of the slow process to issue amendments. President of Mongolian National Mining As-

sociation N.Algaa is adamant that government approval of this law decreased investment in exploration. When the last extension was extended indefinitely (until the July 2014 update of the Minerals Law), it prohibited the transfer of exploration licenses. That only led to the trend to sell a company directly, instead of transferring exploration rights.

The updated Minerals Law stayed intact for seven months until a draft bill once again amending the law was submitted to parliament on February 6, 2015, gaining approval 12 days later. The most recent change contends that license holders for a minerals deposit of strategic importance (which are state-owned) have the right to choose state co-shareholding or a substitute that increases upfront royalties.

The mining sector is regulated by several laws other than the Minerals Law. These include the Law on Prohibition against Exploration and Mining in Headwater Areas, Protected Zones for Water Reserves and Forest Lands enacted in July 2009 (aka the Law with the Long Name), the recent Law on Common Minerals, the Petroleum Law adopted by parliament in 2014, the Mongolian law on forests adopted in 2012, Law of Mongolia on Water adopted in 2001, and the Law of Mongolia on Licensing adopted in 2001.

The error of trial and error

Entrepreneurs looking to create wealth view the law and legal environment as similar to Mongolia's erratic spring weather. The government changes laws from one moment to the next. But on no occasion have they listened to the opinions of the private sector. The flip-flopping makes the democratic legislative process itself look defective. Many people criticize Mongolian laws as mere translations of foreign laws, and believe for this

reason results don't materialise as planned. It's even said that Mongolia's Constitution was copied from those of Germany and France.

Attorney B.Bayar believes Mongolia's uncertain laws and regulations are a product of an institutional culture that embraces trial and error. There's a law provision that states a judge must make a decision based on their own beliefs. Judges make the decision, but do not provide a written explanation about their decision, because there's no law that states they must do so. Hence, similar cases receive random sentencings. The situation is a contradiction of international court principles, which state that "Court decisions must be predictable" and follow "principles of transparency". B.Bayar added: "Amendments are not a bad thing, because the law always needs to be improved and updated. However, they should not block or suppress investment and economic growth; in contrast they should create opportunities and support them."

In reality, national wealth creators are harmed less by foreign "hitmen" and more by these chaotically revised laws, amendments and regulations. Parliament's schizophrenic behavior victimised Mongolia, entrepreneurs and ordinary citizens alike. Ser-Od said that stable investment is impossible in the absence of a stable legal environment. He stated: "It's unfortunate that instability already impacted civil life; because of it, companies have no funding, and are taking measures such as reducing staff to cut their costs."

Fortunately, the situation is not irreversible. Ser-Od recognises that investors are not gone for good. Rather they are observing how Mongolia deals with private sector and private capital. Thus, any laws that create instability should not be approved in the future. ■

ANALYSIS

Mongolian mining law update

By Eland Robert Mann

The Mongolian government's continued changes to the mining sector's legal environment have damaged foreign investor confidence in the country's most crucial sector. In reputable mining journals and publications from around the world, such as *The Mining Law Review*, analysts bemoan the government's propensity to alter laws every year, to the detriment of investment needed to foster the country's economic growth. The Mongolian government has a history of short-sightedness that sees foreign investment and the mining sector as playthings, rather than as the tools they should be to spur development. Over the past year, in a welcome change of pace, the government has allowed the recent changes to mature. A commitment to and full implementation of the legal changes may bring about lasting success for the mining sector and Mongolia's development.

FDI AND THE NEED FOR LEGAL STABILITY

The stability of the legal environment directly relates to the level of foreign direct investment. More stability means more investment. The *Mining Law Review*, in an updated 2014 year-end report, stated that Mongolia's "legal framework has once more been transformed through the repeal of previous laws, enactment of new legislation, and amendments to existing statutes. This predilection for continual legal reform has reportedly caused some investors to hesitate before entering the Mongolian market." The Oxford Business Group's *The Report: Mongolia 2014* likewise remarked: "The rapid changes to rules and quick reversals of those same rules, as well as the long-delayed passing of key regulations, have made it difficult to plan and increased fears that the playing field is not exactly level."

The government's recent spate of tampering with laws can be traced back to 2012's 'Law on The Regulation

of Foreign Investment in Entities Operating in Strategic Sectors' (SEFIL), which proved especially damaging, in that it restricted most major investment opportunities and caused most foreign investors to look elsewhere, at a time when the mining sector was in the midst of a boom. The myopic government designed SEFIL to prevent China from gaining a strategic foothold in Mongolia, by restricting ownership stakes in major mining deposits; however, the law only served to scare away every investor other than China, which remained the ever-patient next door neighbor, playing the long-game, while the others left for good. SEFIL did incredible damage before the government repealed the law and passed a more liberal replacement, the Investment Law, in October 2013. Even with the new law, the after-effects of SEFIL saw FDI remain in decline since repeal, dropping 85 percent in two years. The new Investment Law, however, should not take SEFIL's blame for the fall off in FDI.

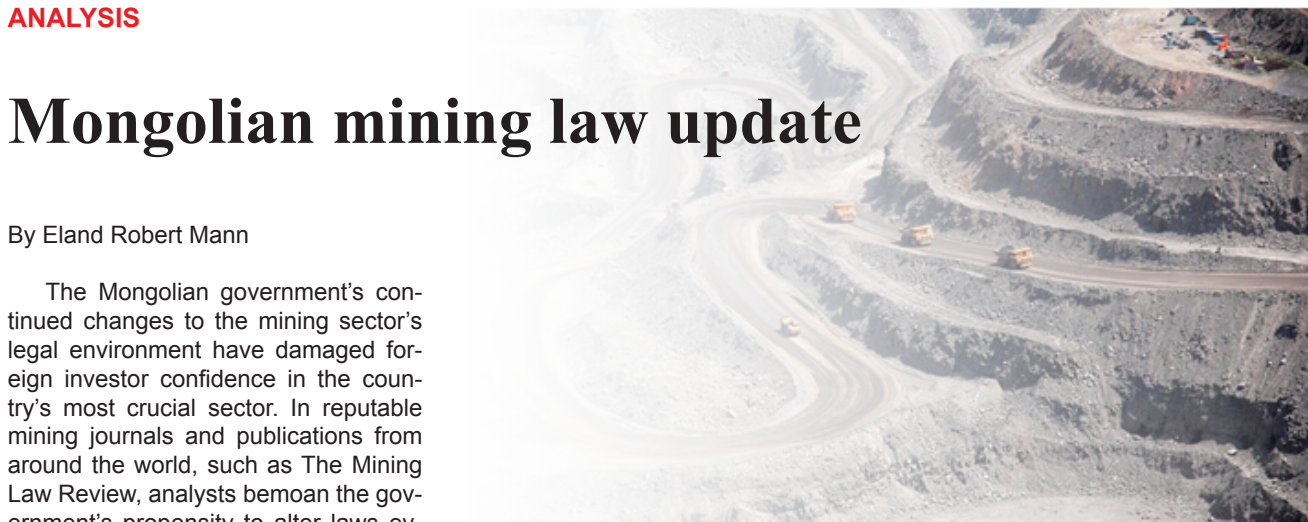
The Investment Law is part of a current group of laws that have the chance to become a part of a stable legal establishment, as long as their tenure is maintained by the government. The Investment Law, the Civil Code, the Investment Fund Law, the Law on Asset-Backed Securities, and the newly amended Minerals Law and Securities Market Law, "form the general legal foundation for investment activities in the country's mining sector," according to *The Mining Law Review*'s report. The new Investment Law crucially reopened foreign investment, leveled the playing field of domestic and foreign

investment, reduced bureaucratic meddling, and created the Invest Mongolia Agency to pursue FDI in diverse sectors from overseas.

Foreign direct investment flight has been particularly damaging for Mongolia, which relies heavily on FDI due to the country's underdeveloped securities market and financial sector. "Equity financing via a reliable securities market of international standards is certainly one avenue by which capital raising can be encouraged and the financial sector diversified," the report recommends. Until Mongolia develops a diversified financial sector, it will depend on FDI, which in turn depends on a stable investment environment.

FLAWED, BUT A MARKET TO WATCH

Recent government amendments to the Securities Market Law and the Minerals Law have also had time to blossom in their respective ways. With 2013's amended Securities Market Law, the government introduced necessary reform, moving toward increased transparency and eased capitalisation in the market place. Most changes became the responsibility of the Financial Regulatory Commission (FRC). The *Mining Law Review* report expects that it will take time before the FRC can implement the Securities Market Law to its fullest extent; however, the law lays the foundation for future success, and is a marked improvement to Mongolia's overall capital market framework. With the "improved legal framework in place, it is hoped that the Mongolian market will, albeit slowly, see improvements



via increased market capitalisation in the not-too-distant future,” states the report.

While the government amended the Securities Market Law to improve capitalisation, the 2014 amendments to the Minerals Law were to establish stability and raise quality in the investment environment. Despite improvement, disputes between foreign companies and the Mongolian government continued to make international headlines in 2015. Major headlines include Canada’s Khan Resources award of USD 100 million in a case against Mongolia settled by an international arbitration court; SouthGobi Resources failed appeal on charges of USD 18 million in tax evasion and Mongolia’s jailing and subsequent pardoning of three former company executives; Anglo-Australian mining giant Rio Tinto’s mired USD

5.4 billion expansion of the Oyu Tolgoi mine; and delayed negotiations with an investor consortium led by China’s Shenhua Energy and Japan’s Sumitomo Corp over the USD multi-billion Tavan Tolgoi deposit.

Mongolia’s one bright spot in 2015 appeared to be the government’s recent move to return to auction 106 mining exploration and excavation licenses previously revoked in 2010. Of the complete tenders, 29 returned to the previous license holders, six were won by a new party, and two remain undecided. The Mining Law Review report states: “While the Mongolian securities market struggles to gain ground, capital raising through the pledge of assets will remain a primary source of procuring financing within the country.” Yet according to a recent article in Mongolian Economy magazine, “Mongolia’s Agen-

cy for Fair Competition and Consumer Protections confirmed that it was looking into the licensing process by the Mineral Resource Authority of Mongolia” after charges of irregularities, unfairness, and corruption.

As more time passes, and recent changes in Mongolia’s mining law are allowed to mature, stability will breed success. Despite the country’s underdeveloped sectors and 2015 headlines, the untampered-with laws should achieve positive results in the long run. The Mining Law Review report concludes: “With a plethora of unique developments on the horizon, and a myriad of legal transformations occurring, Mongolia remains a market to watch”—as long as the government breaks its habit of altering the mining and investment legal environment. ■

ECONOMY

Today’s economic revival actions won’t pay off until 2016

By Tungalag /economist/

To rescue the economy from its current downward spiral, one based on external commodity price decline and a sharp drop in foreign direct investment, the government of Mongolia approved an economic revival action plan (‘Measures to Overcome the Current Economic Difficulties’) on the eve of the Lunar New Year break between the fall and spring parliamentary sessions. The plan focuses on fiscal stability, the investment environment, foreign balance of trade, and improvement of the financial sector. Generally, the action plan proposes to attract foreign investment into Mongolia’s megaprojects via improving the investment environment and loosening formerly tight policies, while simultaneously supporting infrastructure and other domestic sectors. Despite the windfall such projects will bring in the future, at present a planned USD 300 million State Bank bond appears to be the only method to bring cash into the country in 2015. Mongolia’s ‘cash cows’—megaprojects in mining and infrastructure—are facing continued delay, to the point where any expectation of benefit must be similarly

postponed.

ATTRACTING FOREIGN INVESTMENT IN MINING

The government’s action plan is designed to restore foreign investors’ trust in Mongolia and bring back FDI into the mining sector. The now defunct ‘Strategic Entities Foreign Investment Law’ (SEFIL), approved in May 2012 to limit major foreign investment in ‘strategic’ mines, and the Oyu Tolgoi mine’s underground investment delay since mid-2013, are the two main causes of foreign investors flight from Mongolia. As a result, FDI inflow finally dipped into negative territory at the beginning of 2015. The government’s revival plan stipulates that Oyu Tolgoi’s investment issues must be resolved and construction work on Power Plant 5 (PP5) must begin by the end of 2016 to prevent a major cash inflow problem. While Oyu Tolgoi’s problems are well-known, PP5 has its own barriers to investment, stemming from the government’s artificially low energy prices that ostensibly act as power subsidies. The government pressures energy producers to keep prices low, forcing most to

work with a loss. Investor’s who might finance PP5 and other similar projects under the terms of a concession agreement are nowhere to be found, as long as the government subsidises energy prices. With 2015 looking more and more like a lost year, the government mandated the USD 300 million State Bank bond to be raised on the international market to quickly attract foreign currency.

If those three initiatives succeed in moving forward, a combined minimum of USD 1.7 billion will enter Mongolia as FDI in 2015 and 2016. Although this amount is not as high as the level from 2010-2012, it is near to the level of FDI in 2013. The investment environment appears to depend more on Oyu Tolgoi’s and Tavan Tolgoi’s issues between foreign operators and the government, rather than on legislation—as policy makers already approved the investor friendly 2013 Investment Law by removing SEFIL, and added necessary amendments to the Minerals Law in 2014 and 2015. A final decision on Mongolia’s top two megaprojects should be enough for significant FDI to return to Mongolia.

PLANNED INFRASTRUCTURE PROJECTS

In terms of big infrastructure projects, the priorities are PP5, the Tavan Tolgoi Power Plant, and the Erdenet-Ovoo rail link. Construction on these projects will begin by the end of 2016, leading to positive results in both the short- and long-run.

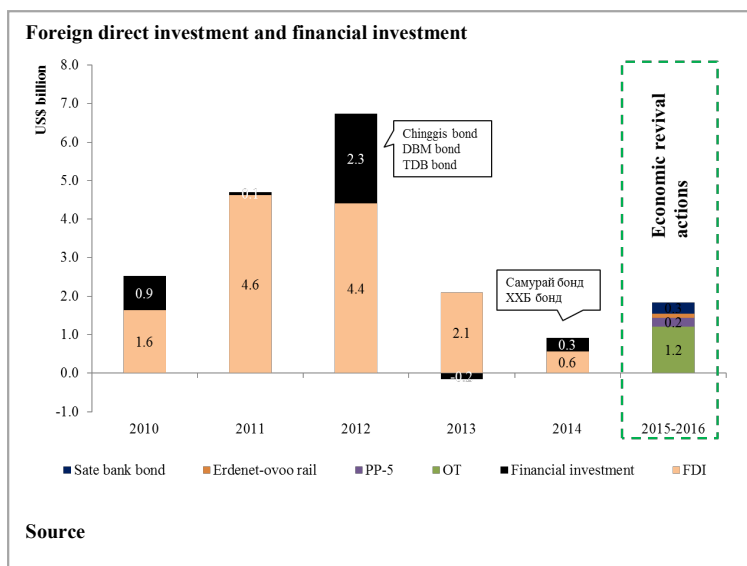
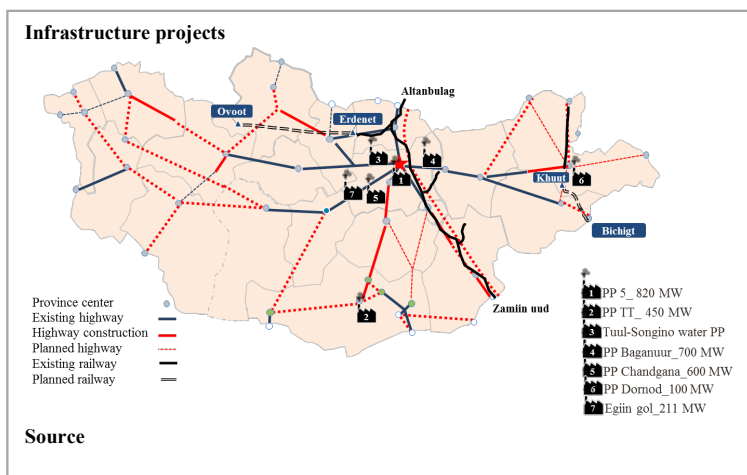
Several additional projects shown in the map will be implemented through concession agreements; concrete results will take a few more years. The infrastructure projects need at least USD 5 billion in investment. Investment environment recovery along with solutions to current obstacles in the way of megaproject financing will play the main role in achieving short and long term success.

MORE EXPORTS THAN IMPORTS

In order to achieve a trade surplus, the government has a three-fold plan to expand mining production (of gold and iron ore), to support non-mining exporters (of cashmere and sewing), and to foster import-substituting producers (of cement and leather products) through a Development Bank loan totaling USD 500 million. A handful of heavy industrial projects are to start by the end of 2016: the Tsagaan Suvarga copper project, a copper smelter, a coal gasification plant, and Mongolia's first oil refinery. The projects will require huge investment, and depend on government agreements with China, Russia and Japan. Despite the efforts, mining sector production will continue to remain more dependent on global commodity prices than on government policy decisions.

ENCOURAGING FISCAL STABILITY

Parliament's approved budget deficit ceilings, 5 percent of GDP for off-budget spending and 58.3 percent for state debt of GDP in 2015, are targeted at 4 percent and 55 percent respectively in 2016. Once parliament approved a higher debt ceiling, fiscal stabilisation fund improvement and the creation of a wealth accumulation fund creation were proposed as well. By excluding the debt of state-owned enterprises from the state debt, according to the newly created Debt Management Law, the government has allowed the debt level to increase. However, to de-



crease the budget deficit would bring about a different set of problems. First, the economic revival action plan included some public social programs that need support: an allowance for the unemployed, energy bill deductions, and proposed reductions in the unemployment rate from 7.7 percent to 6.9 percent and the poverty rate from 27.4 percent to 26 percent. Second, domestic industrial development will be supported by the off-budget USD 500 million DBM loan. Despite its drawbacks, the action plan would have a positive effect on decreasing state participation in the private sector.

DEVELOPING THE FINANCIAL SECTOR

Improving financial stability and reducing financial risks are concurrent priorities. To support the banking sector, the State Bank bond is planned to be

raised through Q2-Q3 this year. This comes at a time when insurance systems and investment funds are under development.

Overall, success in the Oyu Tolgoi and Tavan Tolgoi negotiations form the base of the government's revival action plan. Forecasts yet remain favourable, and the fundamental issues should be solved by the end of 2015. But if Tavan Tolgoi negotiations continue to stall due to the outstanding debt issue with China's Chalco, and Oyu Tolgoi's muddled underground expansion stays buried, you can expect 2015 and 2016 to be woeful years. Even in the best case scenario, questions remain. Can Mongolia start all of its megaprojects in a single year (2016)? Can the State Bank bond rescue 2015 alone? Does Mongolia need an International Monetary Fund or World Bank programme to avoid a true crisis? ■

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POVERTY

A profile on the increasing

“**Batbayar can find anything that might earn him some money from the Ulaanchuluut dumping grounds, where he can earn about MNT 5,000 to MNT 10,000 per day searching for recyclable scraps. “If this place disappears, our life will be in a difficult situation.”**”



P. Batbayar lives with his family in Altan-Ovoo 39 Zagdai, 26th District, S

By G.Orkhon

There's an expression: "only the poor understand the suffering of the poor". Many distressful issues are arising in our lives today due to rampant unemployment and the government's shoestring budget.

When looking at poverty, statistics and analysis can only reveal so much. In this interview, I tried to share my impression of the people who live on the fringe of our city and suffer from debilitating poverty.

Poverty is a condition where people's basic needs for food, clothing, and shelter are not being met. It would not be a lie to say that every person who I met for this interview suffers from a basic lack of food. A mother of six children said that mealtime usually consists of

her feeding her children one slice of bread while she eats nothing herself. Poverty in Ulaanbaatar affects about 40 percent of the total population, and has not decreased from previous years. Today's economic situation has made the lives of Ulaanbaatar's poor more miserable than ever.

The family of P. Batbayar resides on the outskirts of Songinokhairkhan district on a piece of unfenced-in land they don't own. Their household has six members; their only daughter is four year's old. When I arrived at their ger, their 15 year-old son was asleep on a bed. He occasionally groaned in his sleep; when I asked his mother, S. Tsatsraltuya, if he was sick, she replied: "No, he's not. He's dropped out of school and stays at home. So he sleeps in the morning." Batbayar and

Tsatsraltuya are only 40 years old, but their best years might be behind them. Save for food stamps, they receive no welfare from the state. They receive no childcare money from state because of documentation issues. They receive a total of MNT 40,000 per month from the Food and Nutrition Social Welfare Program initiated by the government, which gives a monthly allotment of MNT 10,000 to adults and MNT 5,000 to children who are considered the most vulnerable members of society. Batbayar's family spends the entirety of the MNT 40,000 on their monthly food. The money is basically the monthly income of their household, unless head of the family Batbayar can find anything that might earn him some money from the Ulaanchuluut dumping grounds, where he can earn about MNT 5,000

plight of Mongolia's poor



onginokhairkhan

to MNT 10,000 per day searching for recyclable scraps. His wife Tsatsraltuya said: "We will somehow find our food as long as this dumpsite exists. If this place disappears, our life will be in a difficult situation." Recently, Batbayar's family became burdened by the price decline of commodities such as copper and brass; on top of it, the price of iron is decreasing day by day. For example, one kilogram of plastic bottles were MNT 300 in 2014, but now has fallen to MNT 200 in 2015; while the copper price is at MNT 1,500, compared to MNT 4,000 last year. Batbayar is afflicted with a lung disease, which makes him unable to work any full or part-time employment; often, he can't even make it to the dumping ground when he's sick. The trash site's smoke, ash and dust only worsen his health.

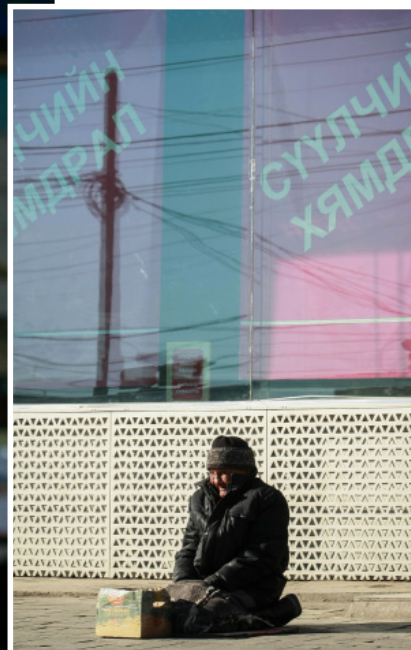


Photo by B.Byamba-Ochir

His wife's bad leg prevents her from picking through waste. They can't get treated at a public hospital, because they don't have insurance, or spare money to spend on treatment. Tsatsraltuya spends her day by looking after her children and reading newspaper fragments brought home by her husband. Her one good leg began to ache last year and has since thinned down to the size of her forearm. Their two middle sons live in the Lord's Grace foster home, and study at School Number 62 in their district. One of them is visually impaired at birth, and the other's eyes suddenly become so poor that he underwent surgery in Singapore at the expense of the foster home. For basic daily necessities, Batbayar's family collects firewood from the dumpsites, and buys five litres of water from a private well for MNT 5. They tried to get electricity from their neighbor, but they don't have long enough power cable.

NO DUMPSITE, NO FOOD

There are many households similar to Batbayar's, which survive on scraps from the Ulaanchuluut dumpsite. The family of R.Ulaanbandi, a household of seven, resides two streets away from Batbayar's. Besides Ulaanbandi's four children, his brother-in-law lives with them. Their family moved to the city from Bayankhongor aimag in 2004. Ulaanbandi and his wife D.Batsaikhan are both 32 years-old, and both are unemployed. They said that they intend to work when the construction work begins. They also make the daily trip to the Ulaanchuluut dumpsite. If R.Ulaanbandi goes to the dumpsite alone, he can earn MNT 7,000 to 8,000 thousand per day; if his wife comes along, they earn twice as much. Ulaanbandi has spinal issues, so he said that he cannot perform hard labour. Their household's main income is MNT 80,000 in childcare money they receive from the state. They spend all their money earned from the dumpsite on daily food, so they don't have the privilege to save money. Their youngest child is three years-old. There is no preschool for her to go to. The wife Batsaikhan said: "It's hard to find a job, even if I want to, because employers set age limits and look at your appearance." When she searches for a job, she finds only cafeteria washer and cleaner positions to be available. She talks proudly of the MNT 300,000

she earned working in construction last summer. But issues like overdue payments are common. She said that working a dumpsite is much easier, because there's no fear of begging someone to get paid. Their family usually uses only one sack of coal per day, but they use more during the winter. In the past, they received a 50 percent discount on their electricity bill from the government's improved boilers project; but now they're paying around MNT 50,000 per month. The seven-member household spends 10,000 to 20,000 per day, even if they try to reduce and save.

The World Bank defines poverty in absolute terms. Extreme poverty is living on less than USD 1.25 per day, and moderate poverty is less than USD 2 a day. This is about MNT 1,994 to MNT 4,000 (as of the March 25, 2015 Bank of Mongolia exchange rate). Poverty will exist in our country as long as we have families who feed their children six slices of bread per day.

B.Bauvarjan's family of nine lives in a five wall ger in the boondocks of Ulaanbaatar's central Chingeltei district. Bauvarjan's family lives in his wife B.Saruultsetseg's mother's home. They have six children; the eldest son is 16 and the youngest is two. Saruultsetseg's mother is 60, and lives together with the family. Saruultsetseg said that although they moved here from Tov aimag 15 years ago, they're livelihood became more difficult only in recent years. The family of nine live on their grandmother's pension and the children's state childcare money, which totals MNT 350,000. In Mongolia, four children bring mothers the official state honor of 'Second Order of Glorious Motherhood', and an extra yearly MNT 100,000; Saruultsetseg receives this money too. She said that her mother had to take a pension loan to celebrate Tsagaan Sar in February. Her husband used to work for a construction company, but it went bankrupt and he's now unemployed. A sack of flour lasts only a month in her family, because when they don't have meat they use flour to bake bread and fritters. They rarely buy vegetables. Saruultsetseg shyly said: "Right now we don't have flour, so I just told everyone to ration the last remaining bread. We give two slices of bread to our children in the morning, afternoon and evening. Our dinner is two slices of bread and tea, after eating it we go to sleep." Mostly they're out of supplies at

the end of the month, but when they can afford to, they usually eat soup. Their families and relatives live nearby, but they're lives are not much better. The household pays around MNT 40,000 per month for electricity, which comes from the grandmother's pension. Bauvarjan worked for two places but could not get paid, and now sits at home, his efforts no better compensated than a slave's. There were many people who performed such free labour in almost every household I met. They blame the lack of compensation on the country's economic troubles. In the past, small construction companies were able to at least pay their workers, but now the situation is different.

WHAT HAPPENED TO THE GOAL TO REDUCE THE POVERTY RATE TO SINGLE DIGITS?

N.Chagdarsuren's household currently guards the backyard of an office building in Songinokhairkhan district. Their family has four members; they don't have their own land and are forced to shuffle around to different places like true city nomads. The couple has a daughter, Undrakh, who is 25, and a four year-old grandson. Chagdarsuren is 77 years-old, and moved to the city from Bayankhongor aimag nine years ago. When he was young, he worked in construction, farming and animal husbandry, eventually coming to the city to send his only daughter to school. But his daughter only finished 8th grade, and didn't study further. Undrakh has been looking after her parents since 2008. Chagdarsuren's wife had a stroke seven years ago. Today, half of her body is paralysed, and she doesn't recognise her family members. The elders are retired, and their household's monthly income depends on their pensions, totaling MNT 400,000. Besides daily living needs, they spend most of their money on medicine, which can easily reach MNT 200,000 over the course of two weeks. A ten pill pack of blood pressure medicine costs around MNT 10,000. They receive no nursing, medicine or welfare money from the state. Recently, their daughter pleaded for nursing money, and a local doctor's council gave a positive answer to her plea. Their total electricity bill is MNT 10,000 per month. The owner of the backyard gave two car trunks full of coal as a guard's salary, which was a

big help for them. Chagdarsuren buys pain relievers, headache and blood pressure medicine when he gets his pension. He said that when he feels alright enough, he doesn't buy his medicine to save money. It's obvious from their talk that they closely calculate their money to make sure it's sufficient. Chagdarsuren manages the finances and gives some money to his daughter to let her buy food. Their daughter said that even though she wants to work and earn money, she needs to look after her parents.

This year, our country set a big objective to reduce the poverty rate to single digits. Yet in the last five months, poverty has skyrocketed—Ulaanbaatar's poverty rate is almost double what it was in October 2014—now at 40 percent and rising. These statistics can be seen in consumer confidence index research conducted by professor of the National University of Mongolia Dr. B.Altantsetseg. According to her, Ulaanbaatar's poverty rate depends on the level of household income and economic conditions. B.Altantsetseg

said: "Poor household livelihoods deteriorate at first when the economic situation deteriorates. This causes poverty to increase." In particular, low income households which are headed by a female are more vulnerable to the economic situation. When in the field for this report, I heard more often about single female-headed households than single male-headed households; but every household has their own troubles.

S.Enkhbayar, who lives in Songinokhairkhan district with his one and a half year old daughter and four middle-school-aged children, is in a difficult situation. His wife died 10 days ago from breast cancer. He said: "The benevolence money gathered from my wife's funeral has been enough for now. But I don't know how we will live much longer. I hope it'll work out, since I'm still alive. Everything would be fine, as long as I can feed and care for my children." His family's monthly income is his five children's childcare money of MNT 100,000. Before his wife passed, they worked in construction during

summers, earning MNT 500,000 to MNT 600,000 per month. But now he's alone, and alone bears the responsibility for his children.

Can't leave their children, even if they want to work; hard to find a job, even if they search; even if they work, they don't get paid—city life has such different shades, but the lives of the city's poorest are getting darker every day. The warden of Chingiltei district's khoroo 12, J.Oyuntsetseg, said: "Because of welfare indulgence, people have become dependent on it, and seek the easy way out instead of fighting." Of course there are people like that. But this generalisation ignores the vast majority of poor out there who will starve to death without state welfare.

Let me say it again: Ulaanbaatar's poor are increasing day by day. Only employment can drive and strengthen this weak economy. A sentence from the president of the Bank of Mongolia N.Zoljargal should say it all: "If the citizens of Mongolia become unemployed, then the whole country will fall into the abyss." ■



N.Chagdarsuren buys painkillers and medication when he receives his government pension.

MINING

Sam Walsh: Mongolia waits as government decides on Rio's "best and final offer"



By Terrence Edwards

Sam Walsh has been chief executive officer of Rio Tinto since January 2013. He stepped into the head role after Rio had planned for USD 14 billion in write-offs under the lead of Tom Albanese. He arrived in Mongolia on March 28 to commemorate Oyu Tolgoi's one millionth tonne of concentrate shipped.

What is the current status of relations between Rio Tinto and the government of Mongolia, especially since the entrance of a new prime minister, Chimed Saikhanbileg?

Relationships are good, and the Oyu Tolgoi project is an important project for the government, people of Mongolia, and Rio Tinto and shareholders. We have a lot in common as we move to improve the wellbeing of the Mongolian people. We have a project that provides returns to shareholders. I think we've redressed discussions over the last 18 months, and we tabled a memorandum of understanding in November that summarised the status of negoti-

ations to date and provided a solution in relation to outstanding issues. There are currently a few outstanding issues remaining. Let me stress that Rio Tinto's position is no different than the position any major project developer would take. We're not asking for anything extraordinary or special. It's an approach that you need to take with a really large capital project to take the project forward. There are issues we're working through with the government, and I'm hopeful we'll bring to resolution. Rio Tinto is committed to Mongolia. We think it's a good place for us to be building projects and running mines. My visit here is to show that commitment, to show our interest, and show our good will in regards to the progress in negotiations.

Are lenders still on board for the USD 4 billion project financing that Rio would use to fund construction of an underground mining complex?

There've been a number of lenders who rolled over their offers. Once we've resolved all of the negotiations, we need to go back to lenders to confirm

the availability of the funding. The world is a pretty volatile and tough place. We're certainly seeing that in relation to commodity prices, including copper. There're still areas of the world still struggling to get over the global financial crisis, and conflict in areas around the world. It's something that we'd need to go back and verify that the financing is still available.

What's the soonest you believe Oyu Tolgoi could see production from the underground mine that will be built in phase two?

There are a number of things we'd need to work through. Obviously we'd need to finalise negotiations with the government. We'd then need to refresh the study numbers because they're now out of date. We'd then need to remobilise the workforce and so on. There are a lot of moving parts there that would need to be taken into account before you can specify when it [phase two] would start.

Is the memorandum submitted to the prime minister last November Rio's final offer for a resolution for

disputes, such as the USD 30 million in taxes the government claims Oyu Tolgoi owes and borrowing USD 4 billion to finance phase two?

This is the best and final offer. We believe this a very reasonable approach to resolving the outstanding issues. Clearly, in terms of reaching a final conclusion there's a lot of detail that needs to be resolved, so negotiations were continuing last week. Of course, the entire process is a negotiation - but let me also say there's no project of this size and scale outside of Oyu Tolgoi inside Mongolia. It does need to be considered in terms of magnitude and importance to the economy. Let me reemphasise we're not looking for any special treatment. We're looking for certainty; we're looking for clarity in relation to what actually will apply to the project. It's more seeking clarity than anything particularly special.

Cabinet Secretariat Minister S.Bayartsogt has said the MoU you've put forward is against Mongolian law. The country can't provide special tax regulations for just one country, he said, even for Oyu Tolgoi. What do you think about that criticism?

We believe that we've put a fair and reasonable offer. The project's 53 percent of value in returns for the government. That does meet international standards. It's highly competitive compared to other projects around the world. We need to be sure when we look at this project over its life that it generates an adequate return to cover the risks, to cover the life of the mine. Remember that mining projects do have a greater risk than building factories at the outskirts of Ulaanbaatar. You're relying on interpretation of resources, you're relying on the accuracy of your drilling program, you're relying on the ability to be able to concentrate the ore satisfactorily and so on. Mining projects are different to generally most other projects in the world. In looking at returns of a project, you need to take that into account.

Turquoise Hill has said it would be willing to go to arbitration over the government's tax claim? Is Rio prepared to go that far?

It's generally an issue for accountants and auditors. We run with a fairly - totally - automatic process. To answer

the question, you need to provide me with exchange rates, commodity prices, oil prices and so on because all of these factors will have an impact. But all these factors being equal, I'm not expecting an impairment. Rio Tinto pays a fair amount of tax all around the world. We released our fifth taxes paid report, which indicates that the taxes paid all around the world. If you're interested we paid USD 7.2 billion globally for 2014. Every tax, we pay - at a national or federal level, state or province level, or local community taxes. We do pay our fair amount of tax. We're debating

“ This is the best and final offer. We believe this a very reasonable approach to resolving the outstanding issues. Clearly, in terms of reaching a final conclusion there's a lot of detail that needs to be resolved, so negotiations were continuing last week. ”

USD 30 million, we're in discussions with government. If necessary we will go to international arbitration.

Do you think Oyu Tolgoi risks impairment in the next set of results if the project continues to be delayed?

I don't think it'll have an impact on current production or the project. These are day to day issues that you deal with and work through. But from a government view point and a Rio Tinto view point, we're equals in all this.

Given the availability of mining contractors and suppliers in the depressed market, how much do you think you could save on construction costs for phase two now?

We need to retest the figures. We need to refresh the numbers. You're certainly right that there's been a reduction in capital project activity. There's also been a reduction in all of the major commodities - steel, copper, aluminum and so on. So I would expect there would be improvement in the numbers, but we'd need to play that all out.

The main reason for the govern-

ment's objections is it wants more immediate benefits from Oyu Tolgoi. The government is not happy to wait many years for investors to recuperate their investments before it starts receiving dividends? Is there a solution to this?

The project will be paying taxes and benefits to the government, but basically as it commences - which we've seen in relation to the open cut operation at OT - we have to date seen USD 250 million [in taxes and fees].

Still, this is a sticking point for many people in Mongolia, as well as concerns about income disparity and the environment. How can Rio convince the people of Mongolia that mining is good for the country?

First of all there're the taxes. There're also the thousands of jobs that we provide. Rio Tinto is the second largest mining company in the world. We build projects using world's best practices. We have a very strong focus on safety, health, environment, and we rigidly follow world best practices in these areas. Of course we meet legislation wherever we operate. Mining is important to the 21st century. There's almost nothing you can do in developing a country in terms of urbanisation and industrialisation without mining materials. You can't build buildings. You can't even run your mobile phone without the commodities that we supply. We are a critical part of the developing world. It's important that, yes, we operate the world's best practices, but it's also important that we do physically bring projects forward. And copper will be important to the world. We don't want to see that world run out of copper.

How does Mongolia compare as a sovereign partner to the other governments it has worked with?

As I mentioned earlier, the tax rate here is competitive against tax rates elsewhere in the world. We believe we are and will be paying a fair amount of tax. We operate in over 40 countries, and each country has its own special way of doing business and requirements for mining companies. We see that as an important part of our social license to operate; that we meet the expectations of the community wherever we operate around the world. And I think we do a pretty good job of it. ■

POLICY

Developing export targeted industrialisation

By B.Dulguun /economist/

Mongolia has been known as an importer country for some time. Currently, it's true that we produce a very small percentage of what we consume. According to a survey conducted in 2012, we import most of the products we consume: 100 percent of gasoline, 93 percent of iron and 62 percent of textile apparel. The government submitted its first comprehensive 'Industrial Policy' to parliament on February 6, 2015. During socialism, Mongolia had an active industrial development plan, but that mostly fell apart during the country's transition to a market economy. Of course a system where the government planned and state agencies implemented had its own weaknesses—nobody would argue that. However, we were able to establish industrialisation in Mongolia during that time.

Total production of the industrial sector accounted for 30.3 percent of GDP in 2013, or MNT 9.8 trillion. But of our exports (which are one of the largest indices of industrialization), low technology products are the norm (such as flour and milk) accounting for 97 percent of total exports. Why is Mongolia in such a state, 25 years on after transitioning to the market economy? The answer to this question is closely related to our natural resources. We produce our minerals raw—that's why the low technology products number is high. Domestically produced goods are unavailable to be exported due to our current low industrial standards and outdated technology. The number of export products won't increase as long as our industry stays undeveloped.

Mongolia must target industrial development by focusing on our comparative advantage, and determine precise strategies and objectives to accomplish it. The government's Industrial Policy objectives seek to do this in five year increments from 2015 to 2030.

Mongolia's opportunity

Industrialisation has become a science itself; many countries went

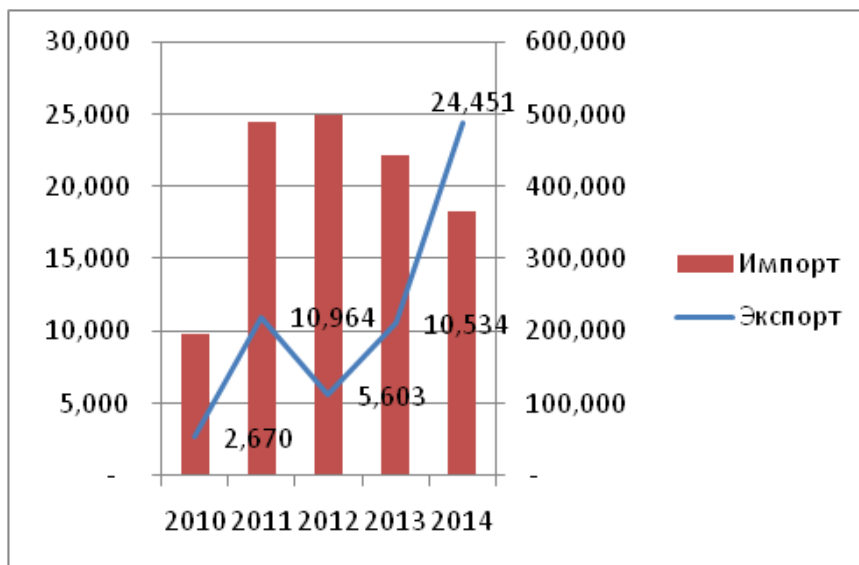
through industrialisation before Mongolia. We have a lot to learn from these foreign countries' experiences in developing our own industrialisation strategy. The most nearby examples are Japan and South Korea. Our policies will be more effective in the future if the government studies unsuccessful implementation models alongside successful implementation examples. In addition, our current government and private sector debt remains high, so we must avoid the pursuit of wrong policies that waste time and assets on uncompetitive products under the name of industrialisation.

Therefore, we must aim to develop industrialisation directed towards export. Export supportive industrialisation is our best opportunity to industrialise going into the future. The economic partnership agreement between Mongolia and Japan is part of this opportunity. Our two countries came to an agreement to establish the EPA after a strategic partnership agreement in 2010. The EPA was signed during Prime Minister Ch.Saikhanbileg's official visit to Japan on February 10, 2015. Mongolia will be allowed to export 9,300 different products to Japan with lower or no import tariffs under the

World Customs Organisation's Harmonised Commodity Description and Coding System. Today, Mongolia exports 70 different products to Japan, while importing upwards of 1,500. From 2010 to 2014 Mongolia's Japanese imports accounted for USD 2 billion, while exported goods were around USD 54 million—about 2.7 percent of what we imported from them.

This situation is because of our lack of industry, but it also closely relates to Japan's import tariffs and internal policies. Japan is a developed country, but their import tariffs on goods are uniquely high. The reason why we relate this opportunity to industrialisation is because Japan will exempt 8,000 goods out of a final total of 9,300 (or 86 percent) from import tariffs the moment of the EPA's entry into force. This opportunity to develop industrialisation by using our advantage now depends on our policymakers, private sector actors and professional associations.

According to a survey conducted in 2013, industrial activity increased Mongolia's GDP by 0.33-0.34 percent per year and total exports by 0.36 percent. This percentage could be much higher with expanded industrialisation and amplified export of industrial products ■



INTERVIEW

A great opportunity for Mongolian products on the Japanese market

By B.Enkhtsetseg

On the list of Japan's largest export and import destinations, Mongolia ranks 74th and 126th, respectively. Despite the low figures, Japanese Ambassador to Mongolia Takenori Shimizu said that if Mongolia can use the opportunities now in place under the newly signed Economic Partnership Agreement (EPA) between the two countries, Mongolia can greatly increase its status. The Ambassador's work and life has been associated with Mongolia for 40 years. Although his education and profession is in law and foreign policy, he developed an early interest in the Mongolian language, attending the National University of Mongolia's Mongolian language special programme from 1977 to 1978. Today, he's fluent in Mongolian. Ambassador Shimizu has written a number of articles about Mongolia, published in both Japanese and Mongolian. Mongolian Economy magazine spoke with the Ambassador about the recent EPA ratification and more.

How have economic relations between Mongolia and Japan developed in recent years?

Since the 1990s, Japan has been supporting the sustainable economic development of Mongolia with Official Development Assistance (ODA). Before the EPA, Japanese grant and soft yen loans to Mongolia reached approximately JPY 250 billion, or USD 2.3 billion in total, and reached out to infrastructure sectors like transportation and communications, as well as social sectors like health, education, culture and science. Ever since Mongolia started to use its mineral resources to rapidly develop its economy, Japan has been trying to establish bilateral economic relations with Mongolia, instead of one sided economic relations based on Japanese ODA. Japanese companies' interest in Mongolia is growing; the number of Japanese companies to come into Mongolia has been intensifying and increasing, espe-

cially after Prime Minister Shinzo Abe's visit to Mongolia in March 2013. Now, world famous Japanese companies are often heard in Mongolia. The private sectors of our two countries must use their full resources and further develop their economic relations. The Economic Partnership Agreement signed on February 10, 2015, after discussing for three years, will be a significant factor in the development of these relations.

On what products have the sides reached a consensus?

To match the basic principles of the EPA with the World Trade Organisation agreement that both Japan and Mongolia agree to, the sides negotiated to exempt tariffs for over 90 percent of the combined total value of trade between the two countries as soon as possible, or at most within a decade. At first, customs duties on vehicle and auto parts exports, amounting to 70 percent of total Japanese exports to Mongolia, must be fully exempt to meet the basic principles of the EPA. Customs duties will be annulled for new vehicles or those up to three years old from the date of manufacture, with an engine size less than or equal to 4,500 cc, as soon as the Mongolia-Japan EPA comes into force. Machinery mainly for construction, such as bulldozers and other equipment and parts, will be exempted from customs duties gradually within a period of 10 years. We agreed to not exempt the customs duties for vehicles up to 10 years old from the date of manufacture. Five years after the EPA is effectively put into place, negotiations to improve market access and other issues will be discussed. Mongolia requested to have agricultural products become exempt from customs duties, but these are still considered sensitive products in Japan. Through the negotiations, products such as seabuckthorn wine, other seabuckthorn products, and animal feed will be exempt from customs duties. Tariff quotas were set on some processed beef products such as beef jerky and corned beef. Due to issues

such as foot-and-mouth disease, it's impossible for Mongolia to export raw meat at the moment, but we agreed to cooperate in the agricultural and livestock sector, specifically in animal health and veterinary services, milk and dairy products, beef and organic foods, and the grain and vegetable industry.

There's an expectation that Japanese investors will look to the Mongolian market and increase cooperation with Mongolian businesses in the coming years. What kinds of exemptions and opportunities does the EPA provide to Japanese companies and investors coming into Mongolia?

Investment wise, progress has been made in improving the investment environment, compared to the previously concluded 'Agreement between Japan and Mongolia concerning the Promotion and Protection of Investment'. In other words, the foreign private sector actors can enjoy the same treatment as national actors and not only after entering the host countries investment market, but also in the lead-up to the investment approval stage. For example, when a Japanese company invests in Mongolia, they will enjoy the same treatment and privileges as Mongolian companies. Of course, it applies not only to Japan investing in Mongolia; the same goes for Mongolia investing in Japan. Mongolian companies actively investing in Japan will surely have a positive impact on the economy of Mongolia.

What difficulties are there for Japanese investors when coming to Mongolia?

As the official representative body of the Japanese government, the Embassy of Japan helps and advises Japanese companies on every necessary issue. According to a summary of their issues, the number one problem for them is that Mongolia's legal environment often suddenly changes; at the second problem is that there's no agreed upon interpretation of the law, so it varies depending on the govern-



ment person responsible; the third is that licensing regulations are not enforced in accordance with the law, because no one is accustomed to the concept of complying with the rules. Such problems are the ones most encountered. We hope the investment and business environment will improve, and a mechanism to help resolve and decrease these factors will be established once the EPA takes effect.

What is the necessary paperwork to export Mongolian products to Japan as per the EPA?

In accordance with the rules of origin, the Mongolian National Chamber of Commerce and Industry must provide certificates qualifying the proof of a product's origin, in addition to other indicated documents that must be provided for customs clearance, if the Mongolian side wants to export products using the EPA's special preferential tariff rates. When using the customs duty quota, the Mongolian side is required to verify if they are meeting the quota criteria; the designated Mongolian authority shall issue the required documents (to reflect the quantity exported) for the Japanese quota certificate, based on the application of the export applicant.

What benefits does the EPA offer in the short run?

Trade and investment flows are highly dependent on the economic climate and exchange rate changes, so it's difficult to predict the short-term outcome of the EPA; but we expect certain results, as there are a number of products that will be customs duty free after

the EPA is in place. Looking at the examples of other countries which established an EPA, it should be noted that their investment increased in addition to import and export increase.

The Mongolian government has damaged the investment environment in recent years, to the point where many foreign companies have ceased their operations in Mongolian. What's the situation like for Japanese companies in Mongolia?

The investment environment has really degraded in the past two to three years. I've heard that many companies shut their branches in Mongolia. In contrast, however, Japanese companies operating in Mongolia are tending to increase, because they have confidence in Mongolia's future despite the difficult situation for now. Investment will recover and the economy will improve if Mongolia can use its natural resources appropriately. There's a saying among our companies, that if they start their business here in difficult times, they will find more success in the future. Last year, the number of Japanese invested companies in Mongolia increased by 11, compared to the previous year.

What preparations must be made before the government and private sector can take full advantage of the EPA?

Of course the effects of the negotiation will materialise after the EPA comes into force. In other words, it's ineffective if a system and structure to implement the provisions of the agreement is not established beforehand. Therefore,

Mongolia needs to immediately start working to meet the appropriate conditions. Based on the agreement, the joint committee, relevant subcommittees and operational procedures of the agreement will be established after the date of the EPA entry into effectiveness. Also, certificates of origin will start to be issued starting from the date of effectiveness. The staff training of relevant organisations of the government, a system to implement the agreement, and public promotion to support individuals and the private sector in utilising the EPA are very important for Mongolia, as it's their first EPA establishment. I would like to advise the private sector to understand and explore the documents required for EPA tariffs utilisation.

Will Japan end its grant aid to Mongolia as part of the conditions in the EPA?

Grant aid does not apply if GDP per capita of a country reaches USD 4,000. Therefore, Mongolia needs to use the concessional loans of the Japanese government wisely from now on. For example, the New Ulaanbaatar International Airport's soft loan interest is only 0.2 percent per year. Mongolia can use soft loans such as this, but unfortunately the Mongolian authorities prefer short term loans and bonds with high interest rates. The state's repayment capability must be considered. I appreciate the government of Prime Minister Ch.Saikhambileg for giving more importance to this matter.

How do you see Mongolian-Japanese economic relations in 10 years?

Personally, I have one wish. Mongolia's and Japan's economic relations have developed slowly compared to the political and cultural relations of our two countries; I wish it will further expand and develop under the full capacity of the EPA. I wish for private sector investment and trade turnover of our two countries to increase, so that Mongolia and Japan could become mutually beneficial and irreplaceable "strategic partners" who complement one another. I harbour beautiful thoughts about our future. I hope Mongolian companies investing in Japan will become just as successful as our Mongolian grand sumo champions, and I hope that Japanese shops will be filled with many Mongolian brand products. ■



MONGOLIA THE LATEST ON TWITTER

OxfordBusinessGroup @OBGnews Mar 7

#Mongolia's #retail sector set to experience pressure throughout 2015
<http://www.oxfordbusinessgroup.com/news/tight-times-mongolia%E2%80%99s-retail-sector>

A cooling economy, persistently high inflation and tighter credit regulations will maintain pressure on Mongolia's retail sector throughout 2015, according to an update from the Oxford Business Group. "The non-mining segment of the economy was dragged down by weakness in the construction and wholesale/retail sectors last year [2014], with these pressures set to continue." According to the World Bank, the wholesale/retail sector contracted 6.8 percent in the first three quarters of 2014. Retailers are likely to be affected by tighter lending requirements and higher interest rates introduced by the Bank of Mongolia in 2014, which led to a slowdown in private sector credit growth to 22 percent in October—down more than 53 percent from a year earlier.

Andrew McLean @amcl2004 Mar 16

Lots more for #Mongolia to do "@MaxCRoser: The world's most severe environmental problem: Indoor air pollution.
<http://www.maxroser.com/we-are-making-progress-against-the-worlds-biggest-environmental-problem/>

"Indoor air pollution is by far the biggest environmental problem of the world. Every year, 4.3 million people die due to the exposure to household air pollution cause by indoor open fire. The burning of solid fuels fills the houses and huts in poorer countries with thick smoke that kills the world's poor by causing pneumonia, stroke, heart disease, chronic obstructive pulmonary disease, and lung cancer. It is predominantly women and young children who are killed by indoor air pollution. The solid fuels responsible for this include wood, dung, charcoal, and coal," says Max Roser, an economist working at the University of Oxford.

The Diplomat @Diplomat_APAC Marc 17

US only 8th largest investor in #Mongolia, should do more: Amb. Altangerel of @MGLEmbassy_USA#DiplomaticAccess
<http://thediplomat.com/2015/03/diplomatic-access-mongolia/>

The Diplomat, a current-affairs magazine for the Asia-Pacific region, interviewed Mongolia's Ambassador to the US, B.Altangerel, who discussed Mongolia's relations with its two neighbors and the US, its desire to join APEC, and its regional role in leading diplomatic talks between the two Koreas. ■

OPINION

The new Debt Management Law and related issues

L.Gangerel /economic analyst/

Since 2012, Mongolian government loans and bonds, such as the Development Bank bond of USD 580 million and the Chinggis bond of USD 1 billion, have increased to the extent that Mongolia's external debt has become one of the country's most significant issues today. Many economists state that Mongolia's external debt is a serious problem that could lead to dangerous external and internal debt crises, if repayment does not become a serious priority. Parliament approved the new Debt Management Law on February 2, 2015 to solve this threatening issue; the law is primarily to serve as an independent mechanism that facilitates comprehensive regulations on debt management.

To begin with, there were no general debt management laws or regulations before the approval of the new law. However, some regulations were reflected in the Budget Law, the Fiscal Stability Law, and the Law on the Development Bank of Mongolia. For example, article 6.1.4 of the Fiscal Stability Law states, the "net present value of government debt," aside from some debt relating to mining activities under contract, "shall not exceed 40 percent of nominal gross domestic product of the particular year." In 2013, the World Bank and the International Monetary Fund (IMF) advised that Mongolia's external debt (including loan guarantees) should not exceed 40 percent of its GDP, because Mongolia scored a 3.41 on the Country Policy and Institutional Assessment, relegating it to the 'average debt burden' category that year. (The CPIA assesses a country's economic policies and public institutions.)

Several conceptual changes were made in the newly approved Debt Management law:

1. The new law defined total external debt and government debt. The IMF's definition is quite similar to the new law's definition of total external debt: "Payment obligations of the government, local community, Bank of



Mongolia, and entities registered in Mongolia to all unregistered non-residents." It includes the external debts of the Bank of Mongolia in total external debt of the state. According to the Fiscal Stability law, article 4.1.8, government debt is defined as: "public debt is the sum of internal and external borrowings of the Government, financial leasing, guarantees, treasury bills issued by the Government, the amount of all types of financial obligations payable in the future by legal entities fully and partly owned by the state and local governments, and overdue interest, contractual sanctions and fines imposed on this amount." Of interest in the new law, then, is the alteration that borrowings of legal entities owned by the state and local governments no longer belong to the government debt.

2. Government borrowing and debt guarantees will be considered separately, and parliament will approve and set limits to new government borrowings and debt guarantees by absolute value each year. In addition, government debt and government debt guarantees shall not exceed 40 percent of gross nominal domestic product according to article 6.1.4 of the Fiscal Stability law. The government's medium-term debt management strategy accord must be approved by parlia-

ment once every three years; the Bank of Mongolia and the Ministry of Finance are required to report total external debt statistics data to the public on a quarterly basis.

3. Municipalities and provinces are now able to issue municipal bonds in order to eliminate seasonal revenue interruptions, provided that they do not receive financial support from the state budget, and that the local budget's primary balance surplus is no less than 50 percent of expenses. Thus, municipal bonds issuing requires obtaining the consent of the relevant municipal representative's council.

4. The government gets the right to issue a guarantee to domestically invested private companies' project investments that are included in public investment programmes, in addition to state-owned companies. A company which is to implement a public project must have worked with a profit for the past three years and not have overdue debts; other additional criteria are required for these project programmes. The government is able to issue a 100 percent cost guarantee to projects implemented by the Development Bank; projects costs of other entities are possible to be guaranteed up to 85 percent.

5. A government debt guarantee fund will be established in order to raise

funds necessary for the government debt guarantee performance. A debt database will keep records, and will register information such as total external debt of the state, government debt and debt guarantee remainders, and bond information of municipalities and provinces.

To summarise, the new law only regulates relations pertaining to the state and government debt. The Bank of Mongolia and the Ministry of Finance must eventually address how to manage private sector external debt issues. The Latin American debt crisis of the 1980s showed the importance of regulating and limiting external debt of the private sector in addition to government debt.

According to the most recent information provided by the Minister of Finance, the government is able to create USD 450 million in borrowing by

approving the new Debt Management Law. Since 2013, the government has discussed a USD 1 billion soft loan from China; if the loan works out, the Mongolian government will use the loan to fund the USD 827 million Eg River Hydroelectric Power Plant project and the USD 110 million Khoshig Valley International Airport highway project.

In my own opinion as a researcher, these decisions are untimely and inappropriate, and don't correlate to the current government's external debt situation that's nearing emergency levels. The Eg River plant's main purpose is to cease electricity import from Russia that costs around USD 40 million per year. How appropriate is it to use USD 827 million in debt financing to stop USD 40 million in outflow? On the other hand, every country's highway connecting the capital city and the main international airport is considered very profitable

endeavour. But the government could have made a concessional agreement to build this 38 km highway, instead of adding a USD 110 million burden to its current external debts.

Today, Mongolia faces pressing debt issues, such as repayments of the USD 580 million Development Bank bond by 2017, USD 500 million of the Chinggis bond by January 2018, and a swap agreement between the Bank of Mongolia and the Central Bank of China at USD 2.7 billion by 2017. The Bank of Mongolia and the Ministry of Finance must come up with a detailed plan to settle these debt repayments. ■

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INTERVIEW

Z.Narantuya: Commission's top priority is "to provide fair competition to market participants"

By I.Otgonjargal

We sat down with Chairman of the Financial Regulatory Commission Z.Narantuya to talk about today's stock market trends and the Mongolian Stock Exchange's new management policies.

You had an official trip to Japan a few days ago. What was the outcome of this working visit?

Our Financial Regulatory Commission has signed a memorandum of cooperation with the Financial Services Agency of Japan. Within this memorandum, our two organisations will cooperate to develop Mongolia's Financial Regulatory Commission's capacity, and it has many more provisions such as this. A project to develop our country's financial market and capacity with the support of JICA [Japan International Cooperation Agency] was launched in December of last year. We agreed to cooperate on five objectives within this



project. During the visit to Japan, we discussed the framework of the project, and the Japanese side provided us the first report, which estimated our country's financial market; in addition, we discussed about what proposals and provisions should be added in the project further on. Japan's stock market is much larger than ours—the world's third largest. Therefore, it was a good place for delegates of our organisation's new management and staff members to have visited and studied.

What's your view on the Mongo-

lian Stock Exchange? What decisive actions should be taken?

Many different organisations function around the Mongolian Stock Exchange, enough so that the stock market operates actively. Transaction settlements must be done quickly and securely after a transaction is completed. There must be a clearing house that executes a reliable end clearing. This center was not established in our country until now. Also, a central securities depository must be established so that the ownership records of security pur-

chasers can be made. The Securities Clearing House and Central Depository should be separated so that the clearing settlements can be done separately. We're focusing on these matters right now. It's very important to develop these infrastructure organisations from the early stage with the correct governing body. We hope the government will consider about these matters too. Currently, our stock exchange belongs to the state. The Securities Clearing House and Central Depository is also a 100 percent state controlled institution. Our Financial Regulatory Commission sent a proposal to the Ministry of Finance, about establishing the clearing organisation by installing the central bank's small-value transactions software and infrastructure in the first place so that we can save costs. It means that one more state-owned institution will be established. The opportunity to establish this infrastructure and the fair competition that we desire will be available only if it includes representatives of all market participants in its governance. The next issue that we're focusing on is an improvement project of market inspection and quality. Investors start to invest in the market when its system is reliable and secure. Our current inspection methods are quite outdated. The entire world is trending toward risk-based management. Therefore, one of the operations within this project will focus on the development and improvement of inspection methods and inspector skills.

A lot of time is required to establish the correct foundation and structure of these institutions, such as a clearing house and custodian bank. Which of these can be finished this year? What is the most pressing issue?

The government needs to solve the exchange's privatisation issues quickly—that's the most important thing. Also they must divide the Securities Clearing House and Central Depository into two separate operations. The clearing house's ownership must be resolved too; it would be ideal if it has no state interference in it. Custodian banks are now being established. The Securities Market Law and the Law of Mongolia on Investment Funds, which entered into force in 2013, have laid the main foundation for market-based stock market activity; these were an excellent legal regulations. Currently, two custodian banks received their permission and are

preparing to proceed within this framework. We're planning our operation in ascending order during the economic slowdown; first we establish the right infrastructure, then accelerate our service to market participants, improve the monitoring system, and reduce the payment. These measures should be taken urgently. We're aiming to establish a broad-based financial structure. We're creating a financial market development program that has to be approved by the parliament in order to implement our aims. Our economy really needs long-term investment. The stock market is the main source of long-term financing in most places in the world. The balance between demand and supply will take care of itself if the market is set right. There are quality companies that will issue securities; also investment funds that will buy shares are being established. Currently, three investment funds got approval from us after the approval of the Law of Mongolia on Investment Funds. Several private pension funds were formed by organisations.

The MSE's legal framework has strengthened considerably. Some people are saying that foreign companies might be intrigued. But foreign economists and financiers say that Mongolia must first put greater emphasis on the development of its domestic stock market. The market could be missing substantial economic incentives, in addition to its lacking infrastructure and legislation support. For example, low taxes and deductions are a current topic of conversation. What's your view on this matter?

It's true that tax and fee deductions are a lever to pull to attract investors to our market. We need a system in which people who purchased shares or invested in securities trade on the market get the right to deduct expenses from dividends or maintain a low tax rate. We find that several laws must be changed within the framework of our market development program. We are discussing to make changes in the General Law of Taxation within this framework. Besides the tax leverage, foreign investors emphasise risk protection. Better infrastructure, proper monitoring and a risk-based management system will provide that.

What work is being done to develop investment funds?

Private investment funds are permitted to be established by the Law of

Mongolia on Investment Funds. The legal foundation is already set. Our regulatory commission has approved the applicable rules and regulations. But we need to make some regulations easier. The foremost pressing issue for us is a companies' financial report. It is said that international accounting standards are used for these reports, but accurate financial statements that reflect all activities are essential. Second, we need to bring up the auditing mechanism's capacity and standard to the international level. Progress has been made, but there are cases that some audit reports are inconsistent with reality. Therefore, investors do not trust us. Third, there are issues with our professional valuers. The most needed thing is proper capital assessment. Our current valuation methodology and evaluation standards should be updated. These are also our industries infrastructure issues. Therefore, authorities must focus on these quality issues. On the other hand, they need to support national audit companies with appropriate policies. Many foreign audit organisations come to work on many reputable large projects, and are very expensive. We are lacking a coordinated policy that makes those reputable international companies cooperate with national companies, and absorb their know-how into Mongolia.

What would you say about information transparency?

Everything about information transparency is legalised and reflected in the law, so we require accurate, on time reports according to the law. Our FRC's information transparency was admittedly insufficient in the past. Since the 'Glass Accounts' Transparency Law's entry into force, we began to regularly update our website; now we report information about our internal activities on our website. Information about market participants is also available on our website. A national corporate governance program is being implemented under our initiatives. A portal website named "governance" will be established, so that financial reports, governance, shareholders and board messages of companies listed on the exchange will be posted on this website. Our employees are working to finish this information transparency work within the first half of the year. A regulatory commission's main objective is to provide fair competition opportunities to market participants. All of our activities are focused on this. ■



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The Quality Supplier Development Center (QSDC) is a business development organization founded by private sector representatives and supported by the U.S Agency for International Development (USAID) funded Business Plus Initiative project. The primary objective of QSDC is to increase the competitiveness of Mongolian companies, enabling firms to overcome barriers to increasing sales and meeting the growing demand through its technical and financial assistance.

QSDC provides technical and financial solutions to Mongolian SMEs in order to:

- Increase production capacity;
- Introduce quality improvements and standardization, including acquisition of international certifications such as ISO and HACCP;
- Acquire and adopt new technologies;
- Develop new products or services;

QSDC's Supplier Development Program serves both:

- large companies, who are seeking to develop their supplier portfolio (in size and quality) and;
- SMEs, who are in need for direct technical and financial assistance to grow their businesses.

Supplier Development Program

Quality Management Program

QSDC offers demand-driven trainings in quality assurance areas. We provide following internationally certified trainings of the Chartered Institute of Environmental Health (CIEH) in Mongolia:

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- Health and Safety in the Workplace.

Additionally QSDC provides Six Sigma – Green Belt Training in cooperation with our partner organization.

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**"WE INVEST IN YOUR
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ITB REPORT

Continuing Mongolia's ITB success

By B.Enkhtsetseg

The world's leading travel trade show, ITB Berlin (Internationale Tourismus-Börse Berlin), brings together 10,096 exhibitors from 186 countries for the tourism industry's most prominent get together. That's more than double the world's second largest tourism event, the World Travel Market London, which tops off around 5,000 exhibitors. Despite the fact that ITB Berlin-2015 further cemented its position as the world's leading travel trade show, setting new records and achieving unparalleled success in March, many in Mongolian society still question whether Mongolia, ITB's official partner country this year, will share in that success long enough to bring real results back home.

OPENING WITH A BANG

When asked about Mongolia's selection as partner country for the expo, the German ITB team revealed that there was a worry among the organisers whether or not the country would prove a suitable partner. Their worry only lasted until the opening ceremony, when Mongolia's representatives and performers stunned the crowd with one amazing show after another, to the great relief of the ITB team. By the time the last Mongolian left the stage that evening, the team said that the ITB-2015 partner country had far exceeded expectations. The ITB team thanked Mongolia on its well organised, wonderful performance. Project manager Holger Wilke, who co-organised the opening ceremony, said: "I was part of the ITB organizing team for nearly 20 years. Many countries have participated as official partners, and I worked with most of them. But I've never seen such a unique and wonderful opening ceremony like this before. Mongolia's opening ceremony was so unique. For me it was the best."

Throughout the rest of the conference, Mongolia continued to prove that it was a great choice as official partner for 2015, even surpassing previous partners in many respects. For the 15th annual Best Exhibitors Awards, which evaluates over 11,000 booths and pavilions at the ITB Berlin 2015, Mongolia's stand design won sixth place out of 162 in the Asia, Australia, and Oceania category. A survey from the Travel Re-

search Institute of Germany shows that the number of Germans interested in travelling to Mongolia rose by 4.3 percent. That's equal to three million Germans who are now aware of Mongolia as a must-visit travel destination. A further 150,000 surveyed said that they are already planning a vacation to Mongolia within the next three years.

Mongolia had a prominent presence at the conference and in greater Berlin. Dr. Christian Goke, CEO of Messe Berlin, stated: "These days, Berlin has become the capital of nomads. Because, 300 guests and delegates from the Mongolian tourism industry have come here to Berlin." A big billboard featuring Mongolia's famous natural beauty hung on the main walls of the ITB exhibition centre; taxis ornamented with Mongolian flags transported passengers around the city. Promotional posters were displayed around the ITB exhibition centre and throughout the metro stations and crowded districts of Berlin. At the opening ceremony, with 3,600 travel industry delegates in attendance, Mongolian President Ts.Elbegdorj jested: "The Mongols are back. But this time we're not here to conquer, we're here to befriend." A number of international and German reporters were on hand to capture Mongolian President's speech and quote him in their reports.

Over the past decade, only seven or eight Mongolian tour operators participated in the ITB expo. In 2015, 16 tour operators took part. Participants say that the number

of exhibitors and visitors who came looking for Mongolia at the Mongolian stand increased sharply this year. Mongolian tour companies not only had a number of prescheduled meetings at ITB, but an additional number of unexpected meetings with new partners from all over the world in 2015.

"For example, a few years ago we visited Austria and Switzerland to meet with companies, but it was not so successful back then; this year, however, they came to us themselves and talked on contractual levels, so this shows the scope of participating as an official partner" said, G.Bol-or-Erdene, German market manager for Juulchin Tourism Corporation. She added: "We met with 58 companies and associates during this year's ITB exhibition. Out of those, 21 were old associates and 37 were new companies." In total, Mongolian tours operators reported that they met 30 new foreign tours operators for future partnerships.

WHAT SHOULD YOU EXPECT FROM ITB?

Of the 10,096 exhibitors from 186 countries, more than two-thirds were from outside Germany. Overall, some 115,000 in the general public visited ITB, making up 43 percent of the expo's visitors. Additional estimates by Messe Berlin show that visitors remained longer at ITB Berlin than in previ-



ous years, due to the increase in potential business deals, with the average duration of stay rising to 2.4 days, up from 2.1 days in 2104. The volume of sales surrounding

tourist visits in the years to come.

The National Tourism Development Programme plans to welcome Mongolia's one millionth visitor by 2016. But even after

your plans and developments are. But it is now really time to walk, not talk. Everybody even high levels need to do follow ups and talk with those people again you met at the exhibition. Have an agenda and timetable for the next steps" said Martin Bart, CEO of World Tourism Forum Lucerne.

Even the World Tourism Organization stepped forward and made clear suggestions for developing Mongolia's travel industry. Taleb Rifai insisted that the World Tourism Organization is ready to provide knowledge, technical and political support to help Mongolia deal with its image challenge, legal issues, and human resource shortage, and to make the country a leader in adventure tourism countries by helping to host international tourism meetings and forums in Mongolia.

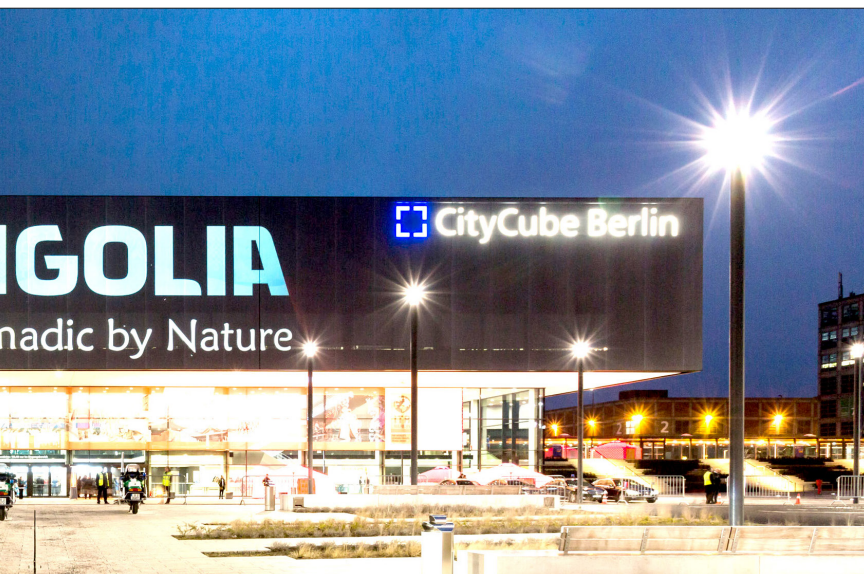
EARNED TRUST

Mongolia's biggest achievement at ITB Berlin 2015 is one that's not immediately obvious: trust. Mongolia earned the trust of international travel market community. And now what we need to do is to sustain that trust by improving our tourism sector capacity, services and marketing.

"Companies need to improve and work more efficiently at professional travel marketing. They should come up with particular products and be special and make presentations on international platforms, as this is considered successful marketing for the whole industry," says B.Indraa, managing director of Tourism for Future. She added that Mongolia must continue to deepen its tourism marketing by becoming more involved on social networks, a cheap and effective way to spread the word.

Mongolia must prepare itself for the increased interest. Mongolians must be up to the challenge of welcoming more tourists, or they can expect disappointed travellers and tour operators, and damaged relations in the future. M.Navchaa suggests that the "government should focus on improving infrastructure and the legal environment, while we tour operators can take care of the service issues and the rest."

Mongolia demonstrated the advantages and features of its tourism industry, and showed it was able to raise its reputation on an international level. But the tourism sector yet lacks good management to hold onto this newly-earned reputation. Despite Mongolia's achievements, the tourism industry remains fragile; if the country doesn't turn its fragility into firmness, the energy and time spent in preparing for the ITB exhibition will have been for nothing. ■



The newly-opened Messe Berlin CityCube, site of Mongolia's opening ceremony at ITB Berlin 2015.

the ITB show increased to 6.7 billion euros, up from around 6.5 billion euros in 2014. Approximately 5,180 accredited journalists from 75 countries, and some 350 bloggers from 29 countries, reported on events at the expo.

Mongolia tried to use opportunity of so many suitors in one place—be they tour operators, tourists or buyers—to mark its formal debut on the world travel market as a trustworthy potential partner. For its debut, Mongolia spent a large amount of money to become official partner country of ITB Berlin. Yet although the government budgeted MNT 18 billion for March event, it has doled out only MNT 7.6 billion so far, and even those payments were often delayed. Mongolia's organising body, Tourism for Future NGO, even arranged donation events to raise money for the sake of Mongolia's participation at the ITB Berlin. While the ITB event was a great success, Mongolian organisers say that they have cut the extent of marketing follow up, a crucial component for official partner countries to prolong their post-ITB success.

There is a fear and a suspicion looming over society that the money spent on ITB will amount to nil for Mongolia's travel industry. But the fact that Mongolia succeeded in spreading the word for its tourism industry at ITB should be enough to give tourism a boost. How big of a boost is another matter entirely, as Mongolia has outsized goals when it comes to increasing

ITB's success, that number does not seem realistic to tour operators. Most operators expect a significant increase in the number of tourists, but not more than double what it's been in recent years. If we look at 2014, the number of tourists that visited Mongolia was barely 400,000, a 5.9 percent drop-off from the previous year.

"We may not feel the full benefit for participating as an official partner this year, but starting from next year we are going to get real results. We're going to feel the benefit even more in the years to come," said, M.Navchaa, Director of Tsolmon Travel.

During ITB Berlin, Secretary-General of the United Nations World Tourism Organisation Taleb Rifai spoke with D.Oyunkhorol, Mongolia's Minister of Environment, Green Development and Tourism, saying: "Your performance at the ITB raised you to a high level. When you go from this level to that level, the challenge is how to stay high up there. That is the price of success."

Although countries spend a lot of money on participating in the ITB expo, they all say the most important time for a country's tourism industry comes after the expo's end. The danger is after such big event, some countries go back to zero. No structure, no money. Then there are other countries that managed to increase their visitors by over 50 percent, such as Turkey. It has a lot to do with what you are going to do with all those contacts that you built at the ITB."

"Well done Mongolia, you showed what

TOURISM

The last day of ITB is not an end, it's a beginning



By B.Enkhtsetseg

Mongolian Economy magazine travelled to Berlin in March to cover Mongolia's participation as partner country of the world's largest travel trade show, International Tourism Borse-2015. While reporting from Berlin, we interviewed David Ruetz, exhibition director and head of ITB Berlin at Messe Berlin. He joined the ITB organising team in 2001.

Looking at your final report of ITB Berlin, the event set some new records. What are this year's achievements?

We are the only trade show in the world that has not only such a high percentage of foreign visitors, which is about at over 75 percent of non-German exhibitors. But we have also the highest percentage of non-German buyers, which has risen this year from 40 to 43 percent. That is a record high. This year we had a report of 115,000 buyers, and 175,000 trade visitors. According to estimates by Messe Berlin, the volume of sales at the world's leading travel trade show increased from around 6.5 billion euros in 2014 to 6.7 billion euros within the five weeks of ITB. That's in

business transactions. So we are not only the largest gathering—the united nations of tourism, here—but also the largest business gathering, on one single spot. Of course some do business during the year, when they travel. But the advantage of a trade show is actually three-fold. First, you see things that you didn't plan on seeing. The internet cannot do that for you. Second, in Berlin we have the whole spectrum of tourism in one place. On 170,000 square metres, you can see travel technology, hotel, aviation, spa and wellness destinations—the whole hospitality and tourism sector. An average visitor at ITB walks 14 kilometres per day to do his business appointments. And third, what ITB gives you, is the personal interaction. Of course we all work with the internet, we work with social media, but personal interaction is actually the unique selling point, combined with the other two things that I just mentioned.

How does this event affect the German or Berlin economy? I notice that it is quite difficult to find a hotel in Berlin now as they're all full.

Actually the hotels in Berlin during these five days, they earn 11 million euros in overnight stays. And of course our visitors spend more. They take taxis, they pay airport fees, they do shopping, they go to restaurants, they do some tours. Actually, at the Messe [Messe Berlin exhibition centre], we secure 25,000 jobs—directly, with all the people working here now. But on a wider scale, Berlin and Germany are profiting from ITB in a range of roughly 300 million euro in wider spending and additional revenue. So that is the reason why in Germany, all of the cities are the owners of the trade show facilities, of the venue, and they also own the shows. So ITB is owned by the Berlin government. This is why we were able to have all of the political influence, and invite the political decision-makers when Mongolia was presenting itself as a partner country, since we are a part of the Berlin government.

Why did you choose Mongolia, when there were many other partner countries available to choose from?

First is we have worked with the private sector and the government people for a long time to achieve this. I would say at least four or five years we have been working together. For us it's important to have reliable partners, and we found them in Mongolia. Second, we saw the potential of Mongolia in the future. When you have a partner country that's already very developed, of course it's another focus. They might showcase just only their new hotels or whatever because the rest have been known. And people would say, "I know already this destination." But what happened here, what made us so happy, is that the media, especially the international media, all jumped on the fact that they didn't know Mongolia very well. The third reason is that we saw and still see a great potential in Mongolia as an undiscovered destination, where people, especially from the Western cultures, can have digital detox vacations.

Do you have any numbers on the amount people who view Mongolia as a travel destination?

Yes, actually this weekend before ITB, the German Travel Research Institute published a figure that within one year, from 2014 to 2015, the number of Germans interested in Mongolia and being aware of Mongolia as a travel destination rose to 4.3 percent from nearly zero. That's three million Germans that have said they are aware that Mongolia is a travel destination. Of these, 150,000 Germans have already planned a vacation to Mongolia in 2015, 2016 or 2017. This survey shows that these 150,000 travellers are mainly under the age of 40, which is interesting information for the Mongolian private sector and for their product development, because they would know, okay, our guests are under the age of 40; they are active guests, they are guests that are young. They are multi-interested. They may not rely on luxury hospitality, but they are also social media and internet focus people. That's a marketing aspect that should not be neglected. This information will help the travel industry of Mongolia to shape their products accordingly.

What aspects of Mongolia are attractive to younger visitors? Is it that they are young and view Mongolia as a destination for adventure?

I think it's different. People under 40 are also someone who's 39, so it's not always youth. This may be a settled business person. But this is a generation, I would like to say, that has travelled the world already. They have seen the world, and what they are looking for is something undiscovered, not mainstream. What they are also looking for is something that is a contrast to their everyday life. That helps them to go away from the stress. They're looking to also meet people from a culture that they would be able to interact with. And I myself, in my travels to Mongolia, have discovered that it doesn't matter where you go in Mongolia, the people are so open—I have travelled Asia very often, to many countries, and this is exceptional. It's not Asia, I don't feel that I am in Asia. The Asian culture is sometimes a little bit kept back, sometimes maybe shy, or a bit closed. But I have found the Mongolians to be very open and often very direct and to the point—which for me as a European is an ideal counterpart, because as Europeans we also like to be direct. So I think there's a nice match when Western travellers travel to Mongolia.

It seems many are happy with Mongolia's opening ceremony. What did you think about the ceremony? Is Mongolia using its opportunity as partner country to the full extent that it could?

We have worked together with the team of Tourism for Future NGO [Mongolia's ITB organising body] and the other people. The opening ceremony was one of the best I ever saw at ITB. Why was that? Because it was the contrary of what was expected. People expected an Asian performance, something like court dances and music. And it was the contrary. It was a powerful manifestation of self-consciousness of a small country with one of the oldest histories ever. Mongolia also during this opening gala showcased that from Mongolia they have sent talents to the world, by bringing international stars. And I felt this was very appropriate. You see Mongolians everywhere, you find them everywhere, and this influenced 4,000 decision makers during the opening gala. Together with the Mongolian team we created many opportunities for Mongolians to meet people. For the time being, I clearly can say they did the maximum. But I should say that the last day of ITB is not the end,

it is meant to be the beginning; the beginning of the momentum that is now taken up to transport that into the next 24 months. That will be the challenge, because ITB will now not be able to babysit—if I can say so—tourism in Mongolia. Babysitting is unfair—but maybe shepherding, guiding. But our role as a guide ends at the last day of ITB. We'll be happy to give advice, but now there needs to be some follow up. Follow up with the contacts that have been made, follow up with the media, follow up with the partners in Mongolia in order to leverage the outcome, transform tourism products. Take this information that we've gathered and say, should we do more social media and rely on the under-40 guests, and so on. That is the challenge that is there for the next 24 months. And I hope that all of the players that have contributed so well—the government, the private sector, the NGOs—that they will sit together and have a debriefing and define a milestone plan for the next 24 months.

The excitement seems to be shared by the ITB participants, who are making more contracts than ever with Mongolian tourism companies. Do you have any numbers regarding business deals at ITB-2015?

This number constantly rose over the last few years. We started out with EUR 4 billion in business transactions. Last year was EUR 6.5 billion, and this year is EUR 6.7 billion. So, a steady raise. Not every exhibitor will reveal their business figures, because of some confidentiality; but basically, over 80 percent of the visitors expect positive business also after ITB. Now, the challenge is to follow the sales leads that you made here at ITB. Statistics tell us, over and over, that 50 percent of all of the sales leads are not being followed up properly, which is just a waste of money. That should be the first emphasis, and this should be the first question in the debriefing meeting that I mentioned: "Have all the sales leads been followed up appropriately?" It's a question of sustainable impact. It can last for the next 24 months, but it also can last only 6 months. Because now there's a big media hype that we have generated. We have generated through ITB about 570 million media contacts, worldwide, resulting in a media-equivalent value of 30 million euro. That's a gigantic package that you can never buy or afford. But it will be important



ITB Berlin 2015 - Press briefing on attractions for the general public - „Partner Country Mongolia“ Astrid Zand, Press Officer, Messe Berlin GmbH; David Ruetz, Head of ITB Berlin, Messe Berlin GmbH; Dr. Martin Buck, Vice President Competence Center Travel & Logistics, Messe Berlin GmbH; H.E. Mr. Bolor Tsolmon, Ambassador Extraordinary and Plenipotentiary of Mongolia; Mrs. Erdenechimeg Batmunkh, Project manager, „Tourism for Future“, NGO (l.t.r.)

to maintain this level, and keep the fire burning, so to say.

How extensive is ITB's media coverage?

We had about 5,180 accredited journalists from 75 countries and some 350 bloggers from 29 countries reporting on events at ITB Berlin. There are 1,500 to 2,000 journalists from abroad. Additionally, for three years now, we've been open to bloggers as well. But we don't focus on getting a mass of bloggers. We select them. We just want to have bloggers with good reach, which are really interesting for our exhibitors. We started with about 200, and now we have 350 from 29 countries. This shows you that it is really good quality, and they are very international. In terms of articles, for example, just in Germany we have 12,000 articles. If we monitor the online articles, we have about thirteen or fourteen thousand online articles about ITB Berlin worldwide.

What would you advise Mongolia to do after ITB Berlin to promote its tourism sector and further develop the benefits it gained as an ITB official partner?

I would strongly suggest that Mongolia goes on in keeping up the contacts that they've made. They have made many good contacts—be it in the political field, be it in the association

field, be it the trade and in the media. And if they keep up all these contacts, like juggling balls, they will manage to stay in the game. Mongolia now has entered the big soccer game of the world players, but they must see that they don't get kicked out. They must keep the ball rolling. And that is through constantly sending messages to the trade, to the journalists, by having the right marketing mix, and by also pursuing the legal framework and going on in the markets that they have discovered. This includes continuous speaking with the new tour operators with whom they have made contracts, and discovering even new clients. If you ask from me a secret recipe, I don't have it, because we did our work here.

Where do you think the tourism world is headed next, in terms of technology, eco-tourism, and the latest trends?

With the outlook at the moment, with more than 1.1 billion travellers worldwide, crossing borders, and about seven times more domestic travellers, I think that nevertheless with the development of the global GDP and economies, trips will tend to be shorter, but need to be more efficient. So the request for a unique experience is even bigger. People who look after tourism products have to shape their products

in a way that they can cater to the needs of these people, to enable in a short period of time the maximum of an authentic experience. We also see that technology of course brings us almost everywhere with development. We see that the apps are the new internet. Apps will tend to replace the internet; this is a fact that we need to take care of in the future. And we also see that the sharing economy factor is one of the greatest drivers; not sharing only businesses, but sharing information. That means that the more authentically people report about a destination, the more likely it is that other people travel there. This is why we had a blogger speed dating session at ITB, where we generated about a thousand appointments between bloggers and destinations, so they could also start. We love the classical media reps, but we feel bloggers are also part of the media community now, and we have to deal with this phenomenon. I think today it is also very important to have good blogger relationships, and to create emphasis in the social media areas. Finally, I would hope that, as in the past, tourism helps us to understand each other better, because if we haven't seen the world, we don't understand our own microcosm. ■

ARBITRATION

Understanding international and Mongolian arbitration

By A.Burenjargal

Mongolians don't quite understand the significance of the word 'arbitration'. That's a problem, as major cases concerning Mongolia have lately been settled in international arbitration court, a side effect of the high levels of foreign investment in the economy in recent years. Dramatic news reports regarding Mongolian cases winning and losing in international arbitration court have made the buzzword an important one to understand.

The most recent case to make headlines stems from Mongolia's 2009 expropriation of uranium licenses belonging to Canada's Khan Resources. Khan Resources balked at the reneged upon license agreement, and took Mongolia to International Court of Arbitration proceedings in Paris. After a length four-year trial, Khan Resources ultimately won the case early this March, and was awarded by the Paris court USD 100 million in compensation to be paid by the Mongolian government. During a recent television interview, member of parliament Ts.Nyamdorj remarked: "We could've not lost this International Court of Arbitration case if we compromised well. I have won three such claims in the past." What Nyamdorj understands, many others do not.

Why isn't arbitration well-developed and understood in Mongolia? The answer is that citizens lack the information about this type of litigation and its use as a way to settle disputes outside of a country's court of law. Despite the lack of public awareness, arbitration in Mongolia has a long history.

ARBITRATION'S BACKGROUND IN MONGOLIA

Currently, the Mongolian International and National Arbitration Center (MINAC), part of the Mongolian National Chamber of Commerce and Indus-

try (MNCCI), is the only internationally accepted permanent arbitration court in Mongolia. MINAC is a non-government and not-for-profit organisation empowered to carry out its operations in the field of private dispute settlement. MINAC was founded on July 2, 1960 at the MNCCI. In 1995, parliament adopted the Foreign Trade Arbitration Law, based on the Model Law on International Commercial Arbitration adopted in 1985 by the United Nations Commission on International Trade Law (UNCITRAL). Mongolia went on to ratify the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards in 1995. That year, arbitration awards made within Mongolia became enforceable in the 170 or so other states and territories that have ratified the convention; and their awards became enforceable in Mongolia. Today, arbitration in Mongolia is governed by the 2003 Law on Arbitration.

MINAC has 21 branch arbitration centres in the aimags empowered to settle domestic disputes. As Mongolia has been a contracting state of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards since 1958, a MINAC award could be recognized and enforced by the courts of all 155 contracting international states.

Disputes of international or foreign companies, organisations and individuals constitute approximately 50 to 60 percent of the cases resolved by MINAC arbitration. It is not possible to obtain information regarding MINAC settlements and cases, as the arbitration process is usually confidential. One such public case, however, MINAC settled between Mongol Post bank and Korea's Nomarang Corporation. MINAC has resolved over 1,000 cases since 1960. But in recent years, their disputes have grown to around 50 to 60 cases per year. According to arbitration

experts, this number is considered as relatively high for a market of Mongolia's size. According to foreigners who work in this sector, this number is quite large regarding the scope of businesses and foreign companies operating in Mongolia. In general, the total number of cases resolved by arbitration is considerably less than the cases judged by litigation. For example, in highly developed Japan, only around 15 cases are resolved by arbitration in a given year.

THE REASON TO DEVELOP ARBITRATION

The advantage of arbitration is that arbitration proceedings are generally private. Parties agree to keep the proceedings and terms of the final resolution confidential. For the most part, it is very difficult to appeal arbitration rulings. This finality can be a positive factor in relation to ending a dispute, one way or another, and allow the parties to move on. A well-developed arbitration court will boost economic development by attracting more foreign investment. Although judiciary development determines a country's legal environment for business, entrepreneurs don't prefer litigation because of its large caseload and more built-in trial procedures that can delay cases. When investors examine a country's investment potential, they analyse economic conditions, the stability of the tax environment, and the health of the judiciary system. Arbitration is a customary mechanism to attract investment.

Speaking with AmCham Mongolia, Director of Gibson Dunn's International Arbitration Practice Cyrus Benson said: "Arbitration has many advantages over litigation. For example, court proceedings are open to the public and have many procedures such as appeals and preliminaries; additionally, arbitration is more independent, confidential, and the arbitrator's decision is final. The main

feature of an arbitration proceeding is that parties have the ability to select the arbitrator." The biggest challenge is in implementing a law that develops arbitration. Mongolia can gain the trust of investors only after overcoming this challenge. To overcome this challenge, long-term political commitment is needed.

The importance of resolving cross-border disputes by arbitration is increasing in today's globalised world. Arbitration courts in developed countries have dissolved into many branches, such as arbitration to resolve agriculture, construction, mining and even vegetable oil. Specialised arbitration companies operate worldwide, as each sector considers a relevant specialist to resolve their issues. Chambers of commerce and industry and other NGOs and associations, to protect producers and customers, may set up institutional arbitration within their organisation. Consumer protection associations and mining associations have set up institutional arbitration in the past, but these disbanded after minimal results.

In 2006, the UNCITRAL Model Law was amended. Legal reform of 2003 Law on Arbitration went undiscussed in parliament due to political instability at the time. Discussions began again in 2010, but have made little headway. A new draft bill is to be submitted in 2015 to update the 2003 law. The secretary general of MINAC, Ch.Gunjdavga, said: "The current law on arbitration is a good law that reflects every necessary rules and regulations from the international arbitration law." However, great social change has taken place since 2003.

For example, Mongolian courts wield immense power, which often extends into influencing the realm of arbitration proceedings. Improving the situation doesn't mean that the court shouldn't be involved at all; but if parties decide to resolve their issues by arbitration, court intervention should be limited by legislation. 2015's new draft bill reflects international standard provisions that limits the court involvement. Another provision that should be added is online dispute resolution. The arbitration court attached to the Economic and Agriculture Chamber of the Czech Republic adopted additional procedures for online arbitration in 2004.



Online arbitration can facilitate arbitral proceedings and resolves disputes via the internet. This innovative technique reduces costs and save time. This method was introduced nine years ago; the provision that requires handwritten signatures is already far outdated.

As international communication expands, more disputes in contracts and agreements will be resolved by international arbitration court. But the significance of turning to arbitration in one's own country is quite large. In particular, the cost of overseas accommodation exceeds the cost of arbitration fees, if an agreement set a condition to use foreign arbitration in case of disputes. Thus, choosing your own country's arbitration will be an investment to your country's economy, and will save your own costs.

However, experts say that the biggest problem related to arbitration is that anyone has the right to establish arbiter. It means that anyone's irresponsible act can ruin a country's or company's reputation and lose the trust of investors. For a small-market country like

Mongolia, too many arbitrators would be a mistake. Mongolia has 58 national and international arbitrators and 11 foreign experts. Ch.Gunjdavga remarked: "Mongolia's legal court inspects 30,000 cases per year, and 12,000 of those are registered in the capital city. Next to this number, our 60 cases per year might look less. But arbitration doesn't resolve issues by force, because two parties must include a provision to use arbitration in the contract." The Mongolian International and National Arbitration Center is constantly doing promotional, training and consulting campaigns for National Chamber of Commerce and Industry members and non-member organisations. To improve arbitration in the future, the MNCCI signed a memorandum with 21 international arbitration organisations to hold training for lawyers, attorneys and students for advanced arbitrator training. The more everyone in Mongolia understands arbitration, the better it will be for the country's investment and development environment. ■



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