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# MONGOLIAN ECONOMY

MAY, 2014, ISSUE №09 (067)

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DUSTY LIFE AT TSOGTTSETSII

**BUSINESS**  
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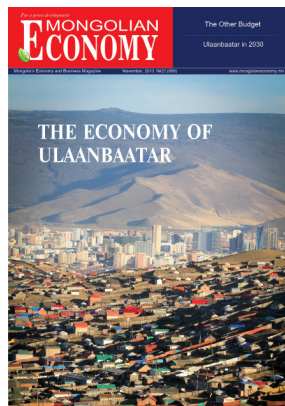
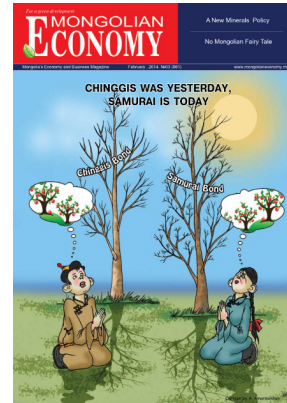
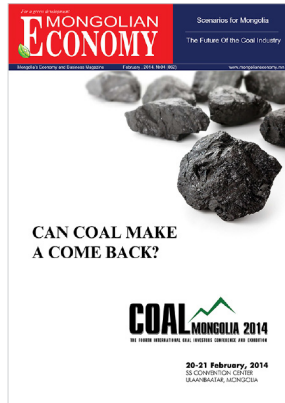
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## MONGOLIA

### Banking and Finance

Mongolia's banking and finance sector this month celebrates its 90th anniversary. Twenty-four years have passed since Mongolia adopted a two-tier banking system with a central bank to oversee a banking sector with private commercial banks.

In 1990 Mongolia saw its first commercial bank open its doors and set the stage for Mongolia's market economy. Mongolia has seen the establishment of 31 banks since then, 15 of which went bankrupt and three that underwent mergers. Mongolia's commercial banks represent 97 percent of the finance sector and comprise 80 to 90 percent of GDP.

### Rails

The 267 kilometres of railway to link the Ukhaa Khudag mine and the Gashuun Sukhait customs port will need an additional USD 200 million in investment on top of the USD 173 million already invested by the government. The government received a feasibility study for the project from McKinsey & Co.

### Tavan Tolgoi

Shenhua Energy has paid Erdenes Tavan Tolgoi USD 17.4 million as an upfront payment for an agreed one

billion tonnes of coal over the next 20 years.

Erdenes TT in April agreed to supply to Shenhua 450,000 tonnes of coal for USD 48,500 a tonne, for a total USD 21.8 million over the course of the two decades. Chinese state-owned Shenhua has already made an advanced payment to Mongolia of USD 17.4 million, or 80 percent of the total USD 17.4 million payment for shipments over the course of two decades.

### Research

The Mongolian government is introducing a new food stamps program to assist households in the country that are struggling to bring meals to the table. The Ministry of Human Development and Social Welfare surveyed the standards of living for 86 percent of Mongolian households. The ministry input the information provided by the 714,000 households into a database that was used to select 87,000 individuals from 15,141 households for the food stamps.

### Mining

The Bank of Mongolia, Ministry of Economic Development and Ministry of Mining are working together to employ an action plan to stimulate gold sales to the

central bank.

Gold sales to the central bank in the first quarter of this year were up 1.8 times from a year ago. The Bank of Mongolia has received 2,040 kilogrammes of gold since the State Great Khural amended the Minerals Law to bring the royalty rate from up to 10 percent to a flat 2.5 percent for the next two years. Some 35 companies have requested to participate in the programme to receive low-interest loans in the hopes of ramping up production.

### Insurance

Mongolia's insurance industry is seeing jumps in growth, according to data from the Financial Regulatory Commission. Mongolia's 17 insurance companies reported total assets of MNT 126.4 billion, with foreign invested companies comprising 20.3 percent. The sum total from fees collected by insurance companies was MNT 93.8 billion last year, 1.2-times growth from the end of 2012.

### Chinggis bond

Mongolia has 150 kilometres of road ready for paving for the nationwide project to build a road network linking every province with the capital.

The government has utilised MNT 369 billion from the

proceeds of the Chinggis bond to fund the total construction of 1,800 kilometres of paved roads to link Ulaanbaatar with provincial centres around the country. Companies built 620 kilometres of new asphalt roads between May and October last year and renovated 310 kilometres of existing road.

### Economic Stimulus

The Prime Minister's Office has submitted to the State Great Khural its 100-days economic stimulus plan. The plan comprises multiple initiatives to stimulate activity in mining, construction, manufacturing, and infrastructure development. The plan also aims to attract foreign investment, encourage the consumption of domestically produced goods; and raise the USD 100 million cut off for tax exemptions for earnings of banking and finance organisation.

### Agriculture

Mongolian farmers will plant seeds and grains for a sum-total area of 375,000 hectares this year. Farmers will plant wheat in 304,000 hectares, potatoes in 15,500 hectares, miscellaneous vegetables in 8.1 hectare, and sunflower seed and fodder in the remaining area. This year's harvests are expected to produce 426,000 tonnes of wheat, 198,000 tonnes of potatoes and 26,000 tonnes of fodder. ▶

## WORLD:

**United States**

US President Barack Obama said the United States will defend Japan in island dispute with China, reported The Telegraph. The United States is duty-bound to come to Japan's aid in the event of a conflict with China over a group of disputed islands in the East China Sea, Obama declared at the start of a tour of Asia aimed at reassuring Washington's allies in the face of threats to stability from North Korea and an increasingly assertive China.

**China**

Chinese media have reported on a credit crunch developing among steel and textile manufacturers in Hangzhou city as the failure of some to repay loans pushes their burden onto healthier firms, reported Reuters. Hangzhou, 175 kilometres south of Shanghai in Zhejiang province, is part of the Yangtze River Delta (YRD), an engine of growth during China's boom years but now the source of a third of non-performing loans in the country. The government ranks the city's Xiaoshan district as China's seventh wealthiest. One of the main drivers of its prosperity – small, private firms – is now a handicap.

**Japan**

Retail sales in Japan grew at the fastest pace in 17 years in

March this year as consumers rushed to make purchases ahead of the sales tax hike in April, reported BBC. Sales jumped 11 percent during the month, from a year ago – the most since March 1997. Japan raised its sales tax, also known as consumption tax, to 8 percent from 5 percent from April 1, the first hike in 17 years. The hike comes as Japan has been looking to rein in public debt, while facing rising social welfare costs linked to an ageing population. Japan's public debt, which stands at around 230 percent of its GDP, is the highest in the industrialised world.

**United Kingdom**

Prime Minister David Cameron has promised to renegotiate the terms of Britain's EU membership and hold an "in-out" referendum by the end of 2017 if his Conservatives win a 2015 national election, reported Reuters. But many

of the most powerful banks, insurers and money managers in the City of London are increasingly concerned that Cameron's gamble could allow the country's USD 2.5 trillion economy the world's sixth largest, to slip out of the European Union.

**Russia**

The Central Bank of Russia has unexpectedly raised its key interest rate to 7.5 percent, despite earlier saying it would not change until June. Aimed at trimming inflation, it means more expensive loans and slows an economy that's already losing steam. The rate went up 50 basis points. The last time it was bumped up was in March to 7 percent, a 1.5 rise from the previous 5.5 percent rate.

Bank Chair Elvira Nabiullina previously said the institution would refrain from changing rates until the June meeting.

On its website the bank gave a traditional explanation, saying the move will help keep the necessary balance between inflation and economic growth.

**IT**

Four major tech companies have agreed to pay a total of USD 324 million to settle a lawsuit accusing them of conspiring to hold down salaries in Silicon Valley, Reuters reported. The move comes just weeks before a high profile trial is scheduled to begin. Tech workers filed a class action lawsuit against Apple, Google, Intel and Adobe Systems in 2011, alleging they conspired to refrain from soliciting one another's employees in order to avert a salary war. They planned to ask for USD 3 billion in damages at trial, court filings show, and that could have tripled to USD 9 billion under antitrust law. ■



## FEATURE

# FEATURE ARTICLE

BY I. OTGONJARGAL

The last issue of *Mongolian Economy* focused on the economic reality in Mongolia – rising prices, slumping demand for Mongolia's exports, and how some of Mongolia's busiest markets have become ghost towns. This month's edition focuses on how the country can overcome the current economic challenges. It also spotlights the poverty found in Ulaanbaatar's ger districts and the towns of Umnugobi, where Mongolia's largest mining projects are taking place.

The State Great Khural has yet to have made any strong actions for the economy since reconvening last month. The so-called "Double Deel" law that would prohibit parliamentarians from serving in certain ministerial positions has also been put on the backburner as policy makers argue over whether the law should take effect immediately or after the next election.

Meanwhile Prime Minister Norovyn Altankhuyag has introduced his 100-days economic stimulus initiative to lift the economy. The plan includes 23 measures that would loosen government restrictions and supervision on the private sector. It would also address lingering issues in the mining sector, such as the amendment to the Minerals Law; a resolution to the disputed 107 exploration licences; and the lifting of the ban on the issuance of new licences. The government is also continuing its support for local production for industries such as cashmere, which it hopes would boost exports and replace sub-standard imports.

*Mongolian Economy* invited representatives from three different private companies to our Economy TV studio for an interview to discuss business life in Mongolia. The company representatives shared their views on how well their businesses are holding up amid tough economic conditions as well as the industries they operate within as a whole. They also gave suggestions on how the country should go about its tax reform, the spending of Chinggis and Samurai Bond proceeds, and the benefits seen from the Price Stability Programme. ■

## POVERTY

# YESTERDAY'S LIFE WAS LIKE A DREAM

BY E. ZORIGT

[Mongolian Economy visited two struggling families in Ulaanbaatar's ger district in February 2013. Last month we checked in on the same families to see if their lives had changed.](#)

I ambled along the dusty streets, amidst the weathered fences to Ts. Batbold's home located in a ger district called Yarmag. I see many children and elderly people playing and enjoying the sunshine. Amidst this happiness, there are a number of drunken residents stumbling in the streets. One of them is passed out, unable to wake from his slumber. Nobody seems to care for him as he lies there helplessly; cars narrowly avoid him as they navigate the bumpy roads. Only stray dogs approach him, sniffing him and quickly darting away.

I reached my destination. It was the same short building I visited a year earlier. When entering, Batbold was sleeping in his bed. He is 41 years old, suffers from epilepsy and is unemployed. His sister, Lkhagvasuren, is 36 years old, and had a railway accident causing the loss of one arm. She is also not employed. Their mother Tsevelmaa, 64 years old, is partially paralysed. She cannot talk but manages to walk around. Batbold and Lkhagvasuren explained that their mother had started to slip in and out of awareness of her surroundings and where she is. The youngest resident is Lkhagvasuren's daughter Namuunaa. She is eight years old. ▶

► Lkhagvasuren laments about her family's life in the ger districts: "Life is getting tougher. When you got here a year ago, we used to have some supply of beef, flour and additional nutrition provided by the khoroo [sub-district administrative organisations] on a quarterly basis. This supply has now stopped. We have only two rooms here. So, we used to rent one room to an elderly couple to sustain our living. They have been unable to pay the rent over the last six months, however. Our pensions are barely manageable and only allow for a few basics and electricity payments."

Among residents of Yarmarg ger district, Batbold's family falls under the "extreme poor" classification. Last year, Batbold's family's revenue was

not considered in this classification. Tsevelmaa's monthly pension was MNT 240,000, the social welfare of Batbold and Lkhagvasuren was MNT 206,000 and Namuunaa's monthly social welfare was MNT 20,000 and rental assistance was MNT 30,000. This roughly totalled MNT 500,000 a month.

A year ago, this family used to cook meals twice a day. And only during special occasions would they boil traditional milk tea. Today, their faces are withered and depict a family who can no longer sustain their own lives. Buying meat to cook was well out of reach.

"We cook once a day using the cheapest flour and innards. In bad words, it is a dog's meal and in good

words, this is a collection of stomach, gut and intestine. For us, buying vegetables has become a dream. When you came to us last year, we were living the life of dream at that time, it seems. We barely survived last winter. The khoroo promised to give us free coupons to buy coal and vegetables, but it did not," Batbold said.

Batbold said that the amount of social welfare and pensions by the government had recently increased by MNT 11,000. But this family's life is getting harder – a result of the sharp increase in the prices of consumer goods and the depreciation of the tugrug. For example, the price of 25 kilograms of flour increased from MNT 15,000 to MNT 19,000, compared to a ►



Photo by E. Zorigt

In the left side, Batbold, Tsevelmee and Lkhagvasuren

► year ago.

The family said that some of the aid provided by the khoroo had been cancelled. The termination of funds has exacerbated their situation. The family last year received loans for their mother's medical treatment and to purchase coal during the harsh winter. They are struggling to repay the loans.

"The volume of aid has been reduced, but not stopped," said district leader N. Soyolchimeg, in response to the description of Batbold's situation. "The reason behind the reduction was due to a reduction in donations and international aid. On the other hand, this was due to a lack of food stamps by the government for poor families. Unfortunately, it is quite common that some poor people use the tickets to buy vodka," Soyolchimeg said.

Lkhagvasuren feels that the government recently started treating poor citizens harshly. For example, some aids provided by the khoroo have been

“

When we look for a job, my brother is often treated like an old drunk. When I look for a job, they treat me like a dirty and disabled person. So, how can we find any job? If the government really requires us to do a job, it has to provide vacancies that suit for people like us.”

”

cancelled. Both suffering physical disabilities, Batbold and Lkhagvasuren, stay home unemployed so that can care for their mother. Lkhagvasuren says that her and Batbold are told by the khoroo staff to get a job.

"When we look for a job, my brother is often treated like an old drunk. When I look for a job, they treat me like a dirty and disabled person. So, how can we find any job? If the government really requires us to do a job, it has to provide vacancies that suit people like us." Lkhagvasuren expressed her frustration.

When I met this family last year, Batbold used to drink vodka three to four times a week. On this visit, he explained that he had not done so for six months. The day revisiting the family, Batbold had the chance to cover for his friend at work for one night. The next morning, his friend

proposed vodka as payment instead of money. He refused the proposal and instead asked for money. Finally, he managed to get MNT 10,000 from him and used some of the money to buy a sweet drink for Namuunaa.

The little girl opened the plastic bottle of the beverage and took one big swig of the beverage, but she did not swallow all at once. Instead, she returned half of the swig into the bottle. When Batbold asked her why she was doing so, she answered that she did not want to finish the drink quickly.

She had not had anything sweet in a long time, she said.

"My favourite are apples," said, lamenting that she had not had any in months. "Mom can't afford them."

## More Than Financial Wealth

B. Batmandal's family lives amid the dusty and messy streets of the Khan-Uul ger district. Finding their home was like



B. Batmandal

looking for a needle in a haystack. To find it, assistance was needed from the khoroo staff. Approaching the desk, it was a surprise to see Batmandal sitting behind the computer.

A year ago, Batmandal's family was deep into financial problems. They ate

the same noodle soup every day. At that time, their monthly revenue was MNT 220,000. He and his wife Munkhzaya were studying at schools while living at his mother's home.

But now everything is different. Batmandal and his wife have graduated from school and are now employed. Their monthly revenue has increased to MNT 800,000, not including their mother's income. They have now settled down on their own and have sufficient funds to support their four-year-old daughter.

"Our lives have improved compared to a year ago. I am in a probationary period for one month at Ard Daatgal Insurance as an officer in charge of driver's liability insurance," Batmandal said. It was just by coincidence that his office was



N. Soyolchimeg

located at the khoroo office. "If the period ends successfully, I will be permanently employed. My wife is working at a company that runs English training and provides professional advice. Somehow we can sustain our lives now."

Batmandal was busy so he was unable to give more details about his life. Instead, he called his mother Soyolchimeg to meet at the khoroo. She is now living alone on her own.

"I am now living happily. My children are employed and they have settled down. I work as a section leader at the khoroo and my wage is MNT 192,000. I am planning to take a computer and driving course soon. This money is enough for a single person," Soyolmaa said.

Soyolmaa said she had been able to take care of her health on her own. At the same ►►

▶ time, she has focused on furthering her education. For example, she has set a goal to learn English. She said that poverty is not only about not having money, but is also about lacking basic human needs, such as health and education.

“The government needs to focus on providing social and health services for every citizen. For example, a dentist is needed in every khoroо. Approximately 70 to 80 percent of our khoroо’s citizens have got a toothache. Also a special diagnosis is needed for some of them,” Soyolmaa explained.

“When one’s health condition

deteriorates, they cannot work well. When people are employed and healthy, they have purpose. The prices are increasing on a regular basis, but wages have not increased. I would like to tell the government officials that life is getting tougher especially among the residents of the ger district where poverty is commonly found.”

The stories of these two families induce a mixed bag of emotions. Sadness and anger for Batbold’s family and the daily struggles they face. Their daughter’s future is at stake and their family’s life is riddled with pain and frustration. With the country’s

economic situation worsening, there is little sign of hope for them.

On the other hand, Batmandal’s family has gone from strength to strength. Their study and subsequent employment has provided a better life for their family. Their days now have purpose and their attitudes are positive.

These are just two experiences of life in the ger districts. Surely there are many others. Acknowledging poverty and having the right policies in place that provide basic needs for the city’s ger residents is essential and result in success stories like that of Batmandal and his wife Munkhzaya.

*J. Delgersaikhan is an advisor to the Financial Management Faculty at the Institute of Finance and Economics. He discussed the reasons for poverty in Mongolia and how it can be addressed.*

Poverty is the result of long-lasting, wrong policy by the government from time to time. Poverty cannot be reduced even though mining-driven GDP is on the rise. This is due to the government’s policies for finance, social welfare and the budget on the equal distribution of revenue generated from the mining industry. In addition, the government has lost control of the exchange rate. The exchange rate’s extreme fluctuation is affecting vulnerable groups in society. In the future, the situation is likely to worsen.

On the other hand, the government has to support citizens who are looking for a job. The government has many

ways to support it in the context of the existing laws. For example, any organisation is obliged to hire a disabled person under the Labour Law. A number of disabled persons can get a job if the government conducts on monitoring employers’ duties under the law.

### **The impact of a small middle class**

For developed countries, their citizens’ living standards are rhombus-shaped. It means that middle-class is the majority. But when it comes to Mongolia’s case, it is pyramid-shaped. This means that rich people who have a very large amount of wealth are a small majority, followed by the middle-class, which is a few and then poor citizens, who are living below the poverty line, are the majority. So, the government needs to focus on creating a middle-class. In the context of state policy, regional

development also needs to be created. This policy is not mentioned by any government.

There is an increase in the number of rural people migrating to Ulaanbaatar. But indeed, this urbanisation process is creating larger ger districts and increasing the number of poor citizens. This is one of the largest indicators that conditions will worsen.

Thus, it is important to create a living environment in rural areas where citizens can live happily. Also there should be mid- and long-term policies aimed at reducing poverty. Poverty cannot be reduced through a temporary short-term policy. Also poverty should not be any [numerical] figure that is made up by any politicians when they are needed. Having a policy based on the detailed estimate and research on poverty is an important step towards reducing poverty. ■

## SPECIAL ASSIGNMENT

## DUSTY LIFE AT TSOGTTSETSII

BY S. BATZAYA

There is a Mongolian saying: "You can't exhaust the cow without starving the calf." Foreign investment is important to economic development and there is a lot to learn from other countries, but mining towns like Tsogttsetsii are feeling the effects of environment degradation, water scarcity, dust-related health complications and an overcrowded education system.

In the Gobi desert, the sun shines at the break of dawn. A golden sunray in the morning evokes feelings of pride. But dusty winds detract from the beauty, but this is a part of life for people living in the Gobi. Ten years ago the town of Tsogttsetsii was a quiet place, like any other town in the Gobi. Now it is a busy and transient place because of the Tavan Tolgoi coal fields.

A heavy curtain of dust drapes over Tsogttsetsii each day. It is always as if a stampede of horses has just passed by. The dusty curtain lifts and unveils a stark reality. Everything in Tsogttsetsii, including streets and buildings, seems so messy and disorganised.

Three mines mine the Tavan Tolgoi coal deposit: state-owned Erdenes Tavan Tolgoi, the Mongolian Stock Exchange-listed Tavan Tolgoi JSC; and Energy Resource. And a slew of Mongolian sub-contractors work for the three coal miners.

Tsogttsetsii has 6,000 permanent residents. Another 15,000 people live there temporarily throughout the year. More than 1,000 cars are registered there, for a community with a mere 12 kilometres of paved road. Most drive on dirt roads, which kicks up huge plumes of dust in the air. The soil in the Gobi is much softer than that of any other regions in Mongolia.

**A Thirsty Town**

Environmental concerns are often forgotten when there is the possibility for mining wealth. Tsogttsetsii residents face many problems ranging from pasture degradation to water scarcity. For example, there were 50 springs near the town just a few years

ago. Today you can count the number of springs on one hand.

Mineral concentration in the water at Tsogttsetsii is high. Having enough drinking water is critical, according to local authorities. Water costs MNT 2 a litre at the water pumps, which filter the water for drinking. Some people ▶



Appearance of Tsogttsetsii soum, South Gobi province



Inter-soums hospital

- ▶ complained the water from privately owned wells outside the centre of town was brackish.

Around 12 to 13 wells have run dry, the Umnugobi Citizens' Council restricted water usage from Balgasiin Ulaan Lake, beginning January 1, 2016, but later recanted the order after miners complained—they being the largest driver of growth for the region.

"Everything is turning for the worse because of the current system's failure," said Tsogttsetsii Governor N. Amgalan "Counties should be developed along with mining development. But everything is challenged here and locals are no longer interested in having the minerals used by companies."

The people living in the Gobi know now more than ever that water is scarce. Water is taken by Tavan Tolgoi from Balgasiin Ulaan Lake. Water experts say that more research is needed for the water resources but nothing has been done. Tsogttsetsii has 65,000 livestock – relatively few for communities in Umnugobi. Tavan Tolgoi JSC, which is partially owned by the local government, has been mining for 50 years, providing coal for three neighbouring provinces. The dust in the air as a result of the operations prevents livestock from grazing nearby. Mining activities there expanded in 2005, and Tsogttsetsii has become all the more dustier for it. Herders are left with little other choice than to pack up and leave.

The construction of the railway that will link Erdenes Resource's Ukhaa Khudag mine and the Gashuun Sukhait customs zone is adding fuel to the fire. The railway will restrict livestock grazing even more, locals complained. Herders said the railway should be constructed so that it circumvents traditional routes they use for their

pastureland.

## Soot in the Lungs

Health conditions are deteriorating all over town. One out of three people suffers from respiratory ailments and one out of two residents is allergic to dust, according to the local hospital officials.

Symptoms are worst among children younger than five years old. Those children represent 60 percent of all who suffer from respiratory ailments. The effects are heightened during winter and spring.

In 2012, the local hospital was expanded to a trans-county hospital, but the actual size of the one-story building remains the same. It has only eight beds for patients. Ten doctors are on staff in the hospital, and the hospital only just recently received its first lab technician. The hospital lab can now provide nine types of examinations.

"The Minerals Law needs to be amended so that mining licences are not given if the mining activity is to be run at a settled area," said one angry local. "Locals will lose, but those who get the licence will not."

The growing population at Tsogttsetsii is also making the schools crowded. The school today has 800 students compared with the 440 it is able to hold. Groups of students arrive throughout the course of three different shifts each day. Energy Resource invested in the construction of a new school and kindergarten in January last year. The Muruudul School has 600 students enrolled and another 140 at its kindergarten. It also has a dormitory housing 100 children.

If the current situation continues the same as today, Tsogttsetsii's citizens will be deprived of their right to live in a healthy and safe environment. Looking out through the dusty air, the future for the residents here is hard to decipher. ■

## CUSTOMS

# TRANSITIONING TO ADIGITAL SYSTEM FOR CUSTOMS CLEARANCE



B. Batgerel, head of Gashuun Sukhait customs

BY S. AZ

B. Batgerel is head of Gashuun Sukhait customs, located at the Mongolian-Chinese border – 780 kilometres south of Ulaanbaatar. Gashuun Sukhait customs ranks third among customs organisations in Mongolia for the amount of tax collected for the budget.

*Standing ominously on the border between China and Mongolia, Gashuun Sukhait is the gatekeeper for goods passing between Mongolia and China. This crossing sees 2,000 trucks loaded with goods, mainly coal, passing through every day and its workers work around the clock with not enough time to eat. Traffic is not expected to ease at this customs point as officials prepare to streamline their operations, by educating their inspectors and cleaning up their organisation's tainted image. ▶*

► **What is the difference of Gashuun Sukhait customs from other customs where mining products are mainly transported?**

According to a resolution by the head of the Customs General Administration of Mongolia dated on February 5, 2010, Gashuun Sukhait expanded from a border point to a customs point having extended hours specially for the transportation of mining products from OyuTolgoi and TavanTolgoi. Minerals are transported from 08:00 to 20:00 Monday through Saturday and passengers are from 08:00 to 17.00. We have established our branches at the Oyu Tolgoi and Ukhaa Khudag mines.

From Gashuun Sukhaitour branches at Oyu Tolgoi and Ukhaa Khudag in Umnugobi province are located 100 and 260 kilometres away, respectively. Our customs point has 62 public special officers and 10 public service officers in total. A new Customs Law took effect from April 1 this year. As a part of the law, our customs will have its own border administration. It will enable us to transfer our procurement section to administration and implement tasks under our main direction and function.

**Companies have said that they have experienced difficulties due to excessive red tape at customs points. How about your customs point?**

Our goal is to contribute to timely minerals' exports. In doing so, we are using 12 roads for transportation. There are two special roads for transportation of coal from Erdenes Tavan Tolgoi and another two roads for transportation of copper concentrate from Oyu Tolgoi. And another eight roads are dedicated for export companies. More than 2,000 trucks pass by the customs border point a day. This is a huge overload. Our inspectors are working 12 hours a day with no time to eat. When it comes to operations, Gashuun Sukhait is at risk.

**The customs clearance application process is now better facilitated. What are your comments on this?**

The government of Mongolia is preparing to turn all public organisations to a one-stop service. Customs organisations are leading this process. This is because customs organisations' information and technology has closely approached world

standards. Previously, 10 documents were required in the application process. This is now reduced to four documents.

Gashuun Sukhait is the first customs that now does not print a custom's declaration. All processes have been transitioned to an electronic system. Erdenes Tavan Tolgoi coal transportation is being passed by the customs in the same principle. Once minerals to be exported are loaded at Tavan Tolgoi or Ukhaa Khudag, our inspectors can see and download all information related to customs clearance through our branches by using an electronic network.

**What is the expected amount of tax to be collected by this customs point for the budget this year?**

Our customs ranks third among all customs organisations in Mongolia in terms of tax collection for the budget. The largest tax collector is Ulaanbaatar Customs Office and the second largest is Zamy-Uud Customs Office, which also sits on the border between China and Mongolia. This year, we expect MNT 136.5 billion in tax.

**A lot is being done for the purpose of customs reform. What kind of reform do you think is best?**

Customs organisations are undergoing reform. They are working to meet international requirements and standards set by world customs organisations. An amendment is expected in the Customs Law. It has to be considered if the current legal setting meets global standards. At the same time, Mongolia's cooperation with the World Trade Organisation has to

move forward. A good connection needs to be developed.

There are five issues under the customs cooperation including the transition to a joint monitoring system with neighbouring countries; and a mutual consultation. So, our prioritised function is to step away from red-tape and bribery.

**How do you deal with the social welfare issues of your staff?**

Social welfare issues at Gashuun Sukhait customs for our staff are hard. There were eight small household buildings when the border point was first established. At that time, the border point was working on a temporary basis. But so far, its operation has been expanded and foreign trade has also been on the rise.

Currently, we are living in demountable buildings. It is so cold to live in these during winter and so hot during summer, which resulted in the constant use of air conditioners and heaters. Without these devices, it would be so hard to live in the Gobi desert area. There is no possibility of bringing one's family here. Unfortunately, it leads to some divorces, which is hard to hear about. So, dealing with social welfare issues is becoming more vital.

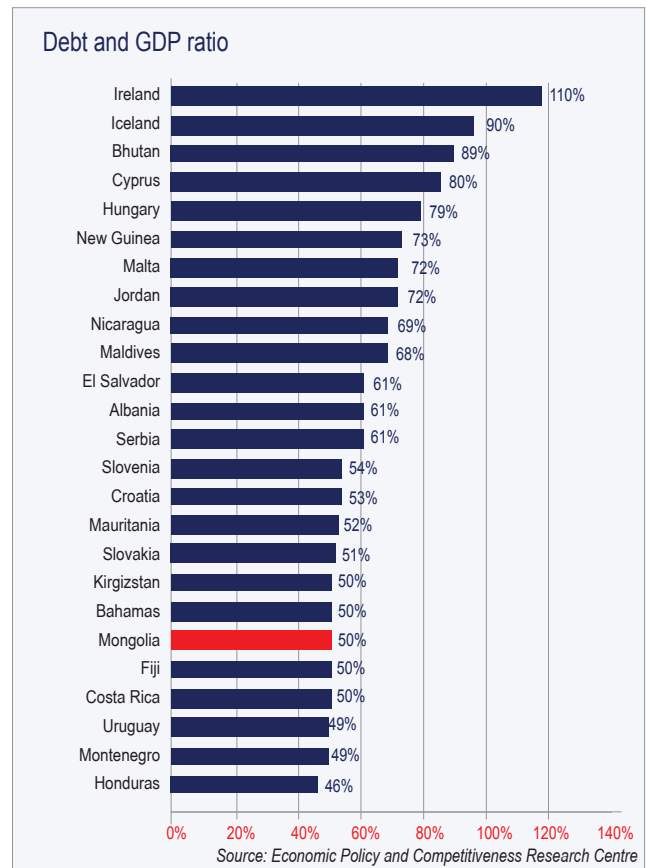
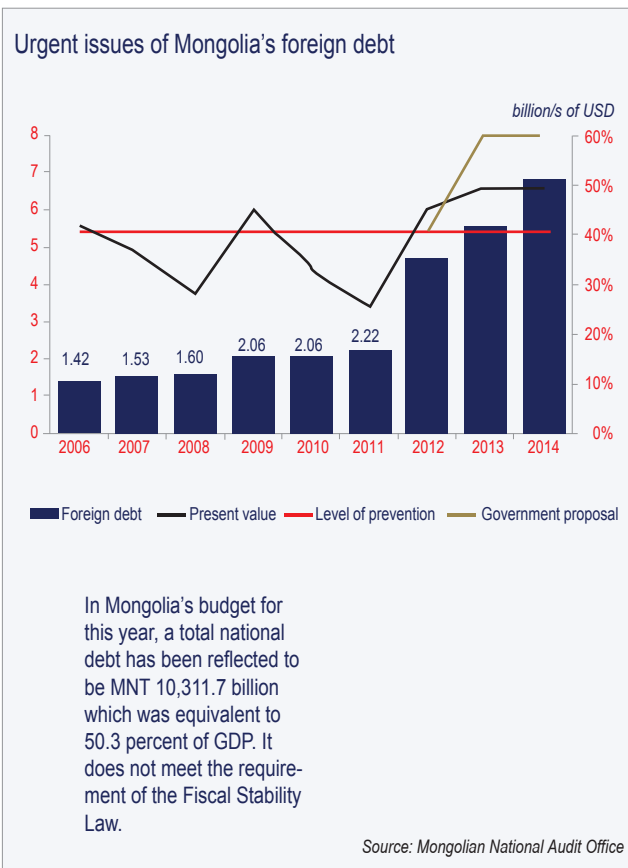
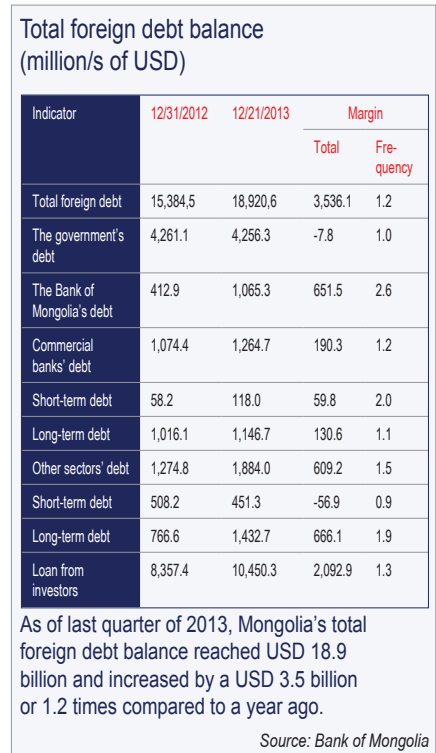
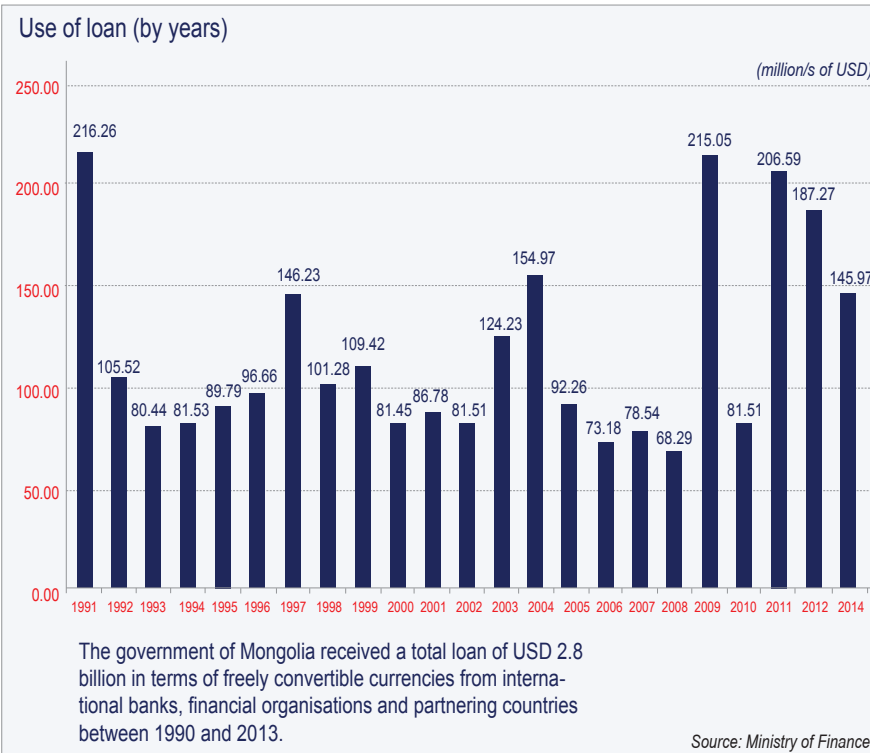
There is no school and kindergarten in this area. There is even no doctor at our office. However, the doctor has already been approved for an assignment here.

We hope the situation will improve in the future as the implementation of the new law has taken effect already. ■



*Gashuunsukhait customs, South Gobi province*

NEWS IN FIGURES



## STUDIO INTERVIEW

# A GLANCE AT TODAY'S BUSINESS LIFE

Mongolian Economy and the Economy TV studio interviewed BSB Service General Director B. Jargalsaikhan; cashmere producer

Khatan Suljee Director B. Badamkhand; and Bridge Group Chairman and a chief at the Mongolian National Chamber for Commerce

and Industry L. Davaajargal to discuss current economic hurdles, the business environment, and possible solutions.



**B. JARGALSAIKHAN**  
*BSB Service General Director*

“ ...We should remember that the world is globalising. Mongolia is sometimes nationalist in the face of globalisation. Indeed, it [Mongolia] has to work with foreigners... ”



**B. BADAMKHAND**  
*cashmere producer Khatan Suljee Director*

“ ...The budget revenue shortfall is, indeed, not because of tax payers. Tax payers are still paying for taxes. The budget revenue fell short because the policy was wrong... ”



**L. DAVAAJARGAL:**  
*Bridge Group Chairman and a chief at the Mongolian National Chamber for Commerce and Industry*

“ ...Business activities cannot be interfered upon or distorted by the state when it is not necessary... ”

► **Let us start our interview with a routine question – how is your business life?**

**Jargalsaikhan:** BSB Service is a small company that imports and trades electronic goods, computers, household goods, and office furniture. Our activities in these four areas are different. For example, the sales of computers and office furniture are low while the sales of electronic goods and household furniture are relatively good. The latter is due to the 8 percent mortgage loan programme implemented by the government.

**Badamkhand:** As Mongolians usually say everything is fine, symbolising a good thing, I would say everything is fine. I have been working in the cashmere industry for 33 years. I established my company 22 years ago. I never felt the economic crisis like this before. The crisis is affecting the business sector so hard. National manufacturers and importers are now in a more difficult situation. For exporters, the situation is a bit better.

**The cashmere industry is substantially supported by government funding from the proceeds of the Chinggis bond. Why is the cashmere industry so sensitive to the crisis?**

Yes, our industry is funded by the proceeds. The total amount of funding should be MNT 94 billion. Some 30 percent of total investment has been made while 70 percent has not been made. I am happy with such good support.

We purchase the required equipment by using the fund provided by the government and arranged raw materials and vacancies. But when it comes to the sales of our end products, the products are not sold. But we achieve the result by selling the products.

Although we been trying not to cut jobs and reduce wages, this matter is now far beyond our control. The situation will worsen if this issue is not considered at the policy-making level.

**Davaajargal:** For Bridge Group, we run three types of activities: construction, retail and foreign trade. Our industries are also sensitive to the crisis. In connection with strengthening the

exchange rate of foreign currencies, we were confident that we could overcome the crisis within a short period of time. Unfortunately, we have been losing this confidence, little by little. We assume that the crisis will continue for one to two years. If the situation continues the same in the future, I wonder how many Mongolian companies will survive.

**What do entrepreneurs' expect from the spring session of the State Great Khural?**

**Davaajargal:** The State Great Khural is expected to discuss and pass several vital laws, including tax reform. Entrepreneurs expect the government to create conditions in which companies can compete fairly. As the crisis escalates, unfair competition increases.

One issue that really needs to be fixed in Mongolia's business environment is informal business activities. It means that there is the wrong system in which those who pay tax fairly are often likely to lose while those who avoid taxes are winning. So, through the parliament session, the shadow economy will be made healthy and fair competition will be supported, I hope. In addition, one important role of the government is to put the spotlight on the future way. The government needs to make clear what Mongolia can achieve in the future and what the country is heading for.

**How bright do you think the spotlight is on this topic?**

The path is not bright. There are plenty of things there on paper, such as the concept, the political party's action plan, and so on. A policy to implement what's on paper is important. Also we need to have support from the right system. It is still unclear which way is the right way or the wrong way. If it was clear, we could choose the right way that the government will support us.

I might say the government has entirely the wrong policy in this area. Mongolia is a small country with a very sensitive economy. So, any laws adopted from developed countries such as the United States and Japan cannot work here.

The second phase of tax reform will be implemented soon. Some laws in particular have been submitted to the State Great Khural for approval. For

example, the tax reform aims to lift the threshold for value-added tax (VAT) and reimburse 90 percent of corporate income tax. As a business person, how do you see tax reform?

**Davaajargal:** The Mongolian National Chamber for Commerce and Industry is raising several issues amid today's difficult situation. One of the issues is tax. According to a study by the chamber, the current value-added tax of 10 percent, corporate income tax of 10 percent, social insurance tax of 10 percent and personal income tax of 10 percent (four 10s policy) need to reduce to 5 percent each (four 5s policy). Lifting the threshold for VAT tax would reduce the shadow economy.

The tax issue seems to me that it is too politically motivated. In general, everybody should pay taxes. In this sense, reducing the amount of the four taxes to 5 percent each would be more efficient.

There are some companies that avoid tax because of the four 10s policy. In order to transition to the four 5s policy, those companies need to be given a second chance. In this way, all of us would be able to pay for taxes.

**Jargalsaikhan:** VAT is 10 percent today. The chamber is talking about reducing the amount to 5 percent. It does not mean that the amount of tax is reduced two times.

Most business people would expect 10 percent of profits from their sales. For example, if you sell any product that costs MNT 1 million, you expect MNT 100,000 in terms of profit. So, when VAT of 10 percent comes to tax payers, paying such an amount is so hard. It makes them want to avoid tax. But those who pay for tax are losing compared to those who avoid tax. In general, 1 percent of VAT is equivalent to 10 percent of profit. If the current 10 percent is reduced to 5 percent, more companies would prefer paying tax to tax avoidance. If the amount is not reduced, they will continue avoiding tax. If they avoid tax, fair market competition cannot be created. Those who avoid tax supply the market with products that are cheaper than the market price. It hampers the profits of those who pay taxes, which might result in no profit or even no sales. ►



April 24, 2014 at Economy TV studio at Mongolian Economy Magazine

► So, the current VAT of 10 percent really needs to be cut.

**Badamkhand:** The budget and tax are two sides of a coin. The government tries to recover the budget revenue from the taxes collected. The budget revenue shortfall is, indeed, not because of tax payers. Tax payers are still paying for taxes. The budget revenue fell short because the policy was wrong.

Today, it is believed that 40 to 50 percent of companies avoid taxes. Citizens avoid tax, too. So, I think that a number of actions aimed to transition taxation to a public tax system needs to be taken instead of reducing VAT from 10 percent to 5 percent.

When we asked the governor at the Bank of Mongolia [Naidansurenin Zoljargal] about the exchange rate, he answered that we have to be responsible for any risk caused by the exchange rate. He also said that if we received a loan from a bank in U.S. dollars, possible risks should have already been taken into account by us. We were disappointed with his words. Actually, it is up to the state to stabilise the exchange rate of U.S. dollar against the local currency, which increased from MNT 1,384 to 1,780. The state exists to do this.

I would also like to tell the state something: Today, businesspeople are under pressures from loans while paying taxes. We have a number of products that we manufactured and put in the market, but there are no sales. In addition to the tax issue, there is the

necessity of working with commercial banks on loan issues. Almost every company received loans from banks.

During the crisis, we needed to forebear the principal payment for loans, which means that only interest was repaid. Otherwise, those who pay tax were also under pressure from loans and they could not pay their taxes. If the situation further continues like this, businesspeople might take actions, such as organising demonstrations against the government.

**The Price Stability Programmes has negative impacts on fair business competition. Some people believe the programme should be terminated while others argue that it is crucial to the economy. What do you think about the programme?**

**L. Davaajargal:** Firstly, state intervention is required for Mongolia, to a particular extent, because the country's economy is so sensitive. But the intervention has to be optimised as such when necessary. Business activities cannot be interfered upon or distorted by the state when it is not necessary.

When it comes to the price stability policy, state intervention is needed to some extent. The understanding of the policy is it has the foundation to make contributions to under-developed sectors through the issuance of soft loans. From this aspect, the policy seems correct. When it comes to implementation, it is problematic.

Secondly, the loans issued for the

programme are for the very short term, which was not suitable for the manufacturing sector to produce materialised wealth. A long-term policy cannot be implemented through this type of loan. The proceeds of the Chinggis bond seem more realistic, but today we need a long-term soft loan. The loan has to be issued to wealth creators in the local currency. The requirement that loans should be repaid in a foreign currency, as the loan came from external markets, could be risky and aggravate the crisis.

It can be said that banks are dominant in Mongolia. Banks are found out of laws. Companies are not allowed to provide any services or sell their products to a local market in foreign currencies, but the banks can issue loans in foreign currencies. The commercial banks treat us as if the only loans available are those in a foreign currency. The foreign exchange market has been seized by the banks. It means that the banks are exaggerating the crisis themselves. This has turned into a system that does not support the companies while benefiting from them. The time has come for the government to focus on this issue.

**The government plans to fund 888 projects for its aim to jumpstart the domestic production of goods for export and to replace imports. However, there is little research on what Mongolia should be manufacturing and what goods are better off imported. What are your thoughts on this? ►►**

► **B. Badamkhand:** I am surprised by these 888 projects. I will give a real-life example on this. I received a phone call from someone who asked me if I was available to write a project. He was interested in the projects' tender selection. So, I asked him what line of business interested him. It was cashmere, but he had no experience in the cashmere industry. This is a typical example of the 888 projects that were selected and are being funded by the government. I wonder if the proceeds will reach real manufacturers that will replace imports and increase exports.

Some 60 percent of total funds for the cashmere industry from the Chinggis bond have not yet been allotted, but companies [with the potential for loans] are being restricted by banks with huge criteria. The small, medium and large enterprises that should replace imports cannot access the loans they need.

**L. Davaajargal:** The 888 projects selected are appreciable. If Mongolia was one big company, operating would be risky if the company was not manufacturing anything, but, instead, selling products that were manufactured by other companies.

On the other hand, when it comes to the implementation of a project in the manufacturing sector, it seems that there is no potential in the banking and finance sector. It is good that the government selected the 888 projects to fund those who are in the manufacturing sector. As Badamkhand mentioned before, we have to consider whether the selection process was conducted fairly. The idea is that the funding from the proceeds should reach those who have been working hard in the sector and those who pay taxes fairly.

The question is if there is any monitoring mechanism to prevent illegal or unfair selection. I think that the policy makers have made the right decision, but when it comes to the implementation of the policy, it cannot succeed if it is only seen from the aspect of profit making. I've heard that there is a huge gap between the total investment for the 888 projects' investment and the amount of funding from the proceeds.

**B. Jargalsaikhan:** This is a question with no answer. We have talked about

the issue from the funding aspect. Manufacturing needs workers and engineers who are experienced in the operation and maintenance of equipment. If a company wants to export products, it depends on a number of essential processes, such as finding the appropriate market and marketing.

Mongolian companies are bad at selling their products. If a company wants to succeed in exporting it needs to work with foreign companies and get to know their market demands. Exports and imports are more available to joint ventures.

If we cannot manufacture quality products that are competitive on the global market, Mongolians would not be interest in such products. It means there would be no sales. If that is the case, they will prefer imported goods, even if the products are more expensive than the domestic product alternatives. So we cannot say that we have to manufacture anything, but we have to manufacture certain products at a cheap cost that will meet international standard in terms of quality and competitiveness. This won't be easy. If it was that easy the whole world would already be developed.

**Recently, there has been a lot of talk about foreign investment. Perhaps it would be better if Mongolia received investment in the form of technology and know-how rather than dollars? How do Mongolian companies benefit from foreign investment?**

**B. Jargalsaikhan:** We should remember that the world is globalising. Mongolia is sometimes nationalist in the face of globalisation. Indeed, it [Mongolia] has to work with foreigners.

We are from an under-developed society. We do not speak English. We have not prepared ourselves even though a good investment environment has been created. Today, when foreign companies want to work with Mongolian companies, we lack experienced staffs. Do we have enough people who speak English? Our companies need to work with foreign companies, whether Mongolians like it or not.

Cooperating with foreign companies or foreigners' entrance to Mongolia does

not mean that we will lose the country or the Mongolian way. We have to create a new environment where we can live together. Otherwise, the world will not open up to us. We would not have any idea about what was happening across the globe.

We will learn a lot from cooperation with foreign companies. Hence, we have not learnt anything on our own. We cannot pretend that we can do it alone. We have to accept our mistakes and learn more. People who train others are important. Foreign investment teaches us how to do the work. On the other hand, it is an instrument that makes us closer to the world.

**Today we talk about the crisis, but it will eventually end and the sun will shine again. How can we best prepare for this eventuality?**

**B. Jargalsaikhan:** To prepare, we have to learn English first. The priority is making progress in improving English education among the public. It is important to focus on quality English training at schools and universities. We have to learn English very well until we can freely communicate with foreign people.

The Asian "Tiger" countries invested in their people. The development does not necessarily come to the country through big money but through human development. Mongolia needs to prepare its people to convert money into a real wealth. Humans are capital themselves, so it is important to train and teach people first. It would be a lie to think that Mongolians who graduated from university abroad return and can develop the economy. They should work with the people who create the wealth.

**B. Badamkhand:** There is the obvious example in Mongolia that the current economic situation was caused by the halt at Oyu Tolgoi's underground mine. We can see from here that small economies like Mongolia are easily shaken by reductions in foreign investment towards the country. Investment is the leverage of the developing manufacturing sector. So, one type of investment is a long-term project loan. It is especially needed for small-and medium-sized enterprises. ■

## POLICY

# RECOVERING FROM MINING LICENSE MISHAPS

BY S. ZAYA

Mongolia's attractiveness fell sharply after the controversial Strategic Entities Foreign Investment Law (SEFIL) was passed in the second half of 2012. This law, designed to restrict foreign ownership, sparked a rapid decline in foreign direct investment – recorded at 70 per cent in less than two years. Realising SEFIL's effects, the 2013 Investment Law was ratified in an attempt to return foreign investment to the levels from before SEFIL was passed. Restoring investor confidence will take much more than a new law, however.

The government cancelled 107 mining licences last November after a court ruled that they were illegally issued by the Mineral Resources Authority in 2009 and 2010.

Among the companies that had cancelled licenses, 24 companies argued their licenses were valid. They have united and are taking action against the government for the cancellation. They deny any knowledge that their licenses should be considered invalid and have

complained about the financial loss the cancellation of these licenses has had on their businesses. Those 24 companies claim they had already invested a sum total of MNT 25 billion into their deposits before the licenses were cancelled.

One company that had its mining license cancelled had already launched the construction of a fluorspar concentration plant and received a loan to fund construction before its mining license was cancelled.

Eleven of the affected companies are foreign. The move to cancel the mining licenses tainted Mongolia's image abroad when its reputation was already flagging because of the disagreements with Rio Tinto over project financing for the Oyu Tolgoi copper mine. The Ministry of Mining established a working group to resolve the issue, but it is still unclear how it will resolve the situation.

The cancelling of these licenses follows the voiding of 200 mining licences for the Law on the Prohibition of Minerals Exploration at Forests and Headwaters in 2009. The law proved too difficult to

implement because the government could not reimburse those companies for the investments they made. Some of the licenses holders are waiting on a final decision on their licenses, including Boroo gold deposit miner Centerra Gold for its Gatsuert deposit.

The government is showing its support for investors with its proposed amendment to the 2007 Minerals Law. The government passed its Minerals Policy last January as a precursor meant to set the agenda for all following legislation related to mining, including this latest proposed amendment.

"In 1872, the United States first approved its Minerals Law. In the meantime, it has been amended 10 times," said N. Alгаа, executive director of the Mongolian National Mining Association.

"When it comes to Mongolia, we still cannot reach a deal that resources are going to be public and government property," he added. The policy is a set of regulations and standards for the law. Mongolians are confused between the law and the policy."

The amendment seems to be changing week by week, so how exactly it matches up with the Minerals Policy is unclear. Mining professionals argue that the mining ministry did not welcome the feedback they gave. And although the Minerals Policy calls for the establishment of a Minerals Council to debate just this sort of amendment, no such institution has been established yet.

Politicians insist that the amendment would not have a negative impact on the mining industry if passed in the current session of parliament, but miners are not ready to take their word for it. Foreign investors are already on the fence about »



▶ investing in Mongolia any further, and another misstep would have even longer-impacting consequences.

Attracting investment will take time. N. Alгаа said that Mongolia can attract investment after it cuts down on the

bureaucracy and begins to support business more readily. Yet the country cannot wait much longer for the State Great Khural to bring the stability investors need to bring capital back to the country. ■

## MINING

# OYU TOLGOI'S ENDLESS NEGOTIATION

BY B. TOGTOKH

The delay to construction for the underground mine shaft at Oyu Tolgoi is wreaking havoc on Mongolia's economy. Mongolia's mining industry needs rejuvenation. It needs continued construction of vital infrastructure. Instead, it stagnates.

The economic trouble Mongolia is experiencing is evident by the depreciation of tugrug against the U.S. dollar all year long, reaching a high of MNT 1,800.

The state budget revenue fell USD 4 billion short last year and the tugrug weakened 30 percent against the dollar. The Bank of Mongolia has followed a quantitative easing strategy, injecting USD 1.7 billion into the economy. One aim of this strategy has been to prevent huge swings in the exchange rate caused by the outflow of foreign currencies. However, despite the millions spent, these efforts have had little long-term impact.

Foreign direct investment too has declined, by 40 percent. Export revenue declined USD 800 million last year. Export revenue collected from the first quarter this year was a fifth as much as the year before. Mongolia's currency reserves are dwindling and are unlikely



to be replenished in the near term. S. Bold, a senior economist at the Bank of Mongolia and advisor to the central bank governor, said that the economic situation would improve if Oyu Tolgoi introduced the investment for the next stage of the mine.

Oyu Tolgoi appears to be the only way for Mongolia to earn the revenues it budgeted for as long as the coal market remains soft.

Turquoise Hill released a statement on April 16 saying that construction for the underground mine, where it says 80 percent of the wealth will come from, will be been delayed further until September 30. Beforehand, the deadline for the USD 4.2 billion in project financing to fund the construction was set at March 30, but parties were unable to reach a consensus.

A letter dated March 27 from Prime Minister Norovyn Altankhuyag was leaked by Mongolian Mining Journal. The letter was for Sam Walsh, chief

executive of Rio, pleading that it accept the project financing. Davaajav Ganbold, chief executive at Erdenes Tavan Tolgoi, sent a follow-up letter to Rio Tinto, too. Yet neither convinced the mine's operators to move forwards with the second phase.

Nearly a year has passed since the delay was first implemented by Rio Tinto and some 1,700 contractors lost their jobs. Prime Minister Norov Altankhuyag made publicly announced in March that the delay to the underground mine was not its fault.

Neither the 66 percent stake holder in Oyu Tolgoi, Turquoise Hill Resources, nor Turquoise Hill's majority owner Rio Tinto has made a clear statement on the fate of the project. The only answer given by Turquoise Hill Chief Executive Kay Priestly was that the negotiations were ongoing. Saying the delay would continue further until September does not provide any concrete resolution either. As a result the Mongolian economy suffers still.

The Bank of Mongolia has projected the production of 93,200 tonnes of copper concentrate this year, and the export of 57,200 tonnes. It has also projected gold production and export of 9.9 tonnes and four tonnes, respectively. That would mean 10 percent growth for exports and 5.7 percent of real GDP.

Oyu Tolgoi's open pit mine is operating normally.

The export of 700,000 tonnes of copper concentrate from Oyu Tolgoi this year would represent some 26 percent of total mining revenue and 5 percent of budget revenue. The mine is expected to produce 692,000 tonnes of copper concentrate this year. So far, it has produced 98,300 tonnes of copper concentrate.

But despite these benefits, today's economic troubles have Mongolians struggling now more than ever before, especially if their livelihoods are in any way connected to Oyu Tolgoi. The delay has prevented some 50 percent of expected foreign currency inflows to reach the country.

The open pit mining production is just the beginning. The real engine to fuel Mongolia's economy is the launch of Oyu Tolgoi's underground mine shaft. ■

## COOPERATION

# EXPECT MORE FROM TURKEY



BY B. ENKHTSETSEG

This year is the 45th anniversary of diplomatic relationship between Turkey and Mongolia, established in 1969. *Mongolian Economy* spoke to Turkish Ambassador Murat Karaguz about the development and future of Mongolia-Turkey relations.

## What is special about the relationship between Turkey and Mongolia?

Today's Turkey and Mongolia are inheritors of multi-ethnic and multi-cultural [characters]. Mongolia is the inheritor of the great Chinggis Empire whereas modern Turkey is the successor of the Ottoman Empire. Moreover, the very first Turkish states in history were established on this territory. The Turkish inscriptions carved on stones are spread widely in Mongolia.

When I'm on the street in Mongolia, I notice many Mongolians speaking Turkish who studied Turkish in Mongolia or Turkey or finished their universities in Turkey. That feature connects us as well. There are a many common words

in our languages because the Turkish and Mongolian do belong to the same language family, called Altai.

We definitely increased our cooperation throughout the last 45 years. We achieved a lot and I guess we are achieving more – day by day. Our relationship will be more intense, more robust marching towards strategic partnership.

## How can we cooperate in the tourism sector?

Mongolia is an exotic and beautiful country. Don't take it as a compliment. It is a reality. Territory-wise Mongolia is a huge country and it has a rich culture and landscape.

Mongolia is not only composed of Ulaanbaatar. It has 21 aimags and each and every one offers great variety of opportunities. In my judgment, Mongolia has great potential in tourism. It is important to recognize this richness and to combine it with good know-how and experience. Through sustainable with good cooperation and investment one will also invest in the bright future of the country.

I firmly believe that in the not-too-distant future, tourism will become one of the leading sectors of the economy in Mongolia.

## What do you think Turkish people think about when they choose a travel destination? What are their preferences?

Of course, visa- free travel regime, direct THY [Turkish Airline] flights, low-travel expenses and cultural richness are main motivations in choosing destinations.

Mongolia can be one of the most attractive destinations for the Turks to rediscover their own history. They can visit Mongolia and smell the roots of the first Turkish states. Besides, it would be also interesting for them to get acquainted with the culture, history and natural beauties of Mongolia.

As of April 11, there is a visa-free travel regime between both countries, so both Turkish and Mongolian people can travel to each other's countries without any visa for 30 days.

## What is the secret to Turkey's successful tourism sector?

Starting from the mid 80s, the successive Turkish governments invested in tourism in a quite-smart way. Laws were issued, investments were promoted, exemptions were granted, and the private sector was encouraged in this respect. It was not a problem-free process, but in the »

▶ final analysis plausible policies were deployed.

And tourism has been diversified in Turkey. Today, people can enjoy Turkey's sea, sun, sand, culture, health, religion, and winter sport tourism. It should not just come as an accident that Istanbul became the number-one tourist destination for travelers' choice polls.

Only last year, Turkey attracted USD 33 billion from tourism. Nearly, 35 million tourists visited this beautiful Mediterranean country. There are two Turkish cities in the top 10-destinations – the one Antalya; the other one Istanbul. Let me only remind you that Antalya has a population of two million but hosts yearly 11 million tourists. These are just a couple of figures which can be interesting for Mongolian authorities while focusing on this domain in advancing bilateral cooperation.

**We can see a lot of students going to Turkey to study higher education. What are the main majors Mongolian students are studying in Turkey?**

I am proud to announce on this occasion as the Turkish ambassador to Mongolia that education constitutes one of the strongest pillars in our relationship. Starting in early 90s, Mongolian students keep coming to Turkey. Currently there are nearly 900 Mongolian students who study in Turkey. 340 of them are getting their scholarships from the government of Turkey.

For the higher education scholarships at the graduate level this year, we received 180 applications. Their interviews were held last week here in Ulaanbaatar. As for undergraduate students, the application will expire mid-May and their interviews will be held in June. This year we wish to increase [enrollment] by 8 percent. Their majors vary from medicine to agriculture, from computer technology to linguistics. Basically, they do study on every field.

Mongolian students who study in Turkey can work later on for Turkish companies here in Mongolia as assistants, project managers, finance directors, economists or translators. I believe in the near future there will be great opportunity for Mongolian citizens to work with Turkish contractors.

**Turkish companies are some of the best contractors in the world. Let's**

**talk about possible cooperation in the construction sector?**

According to the recent published statistics among the top 235 construction companies in the world, 33 of them are Turkish. Turkish companies come in at number two all over the world, and Turkish entrepreneurs are conducting projects all over the world. They do important construction projects in Russia, throughout Eurasia, the Middle East, and Northern Africa, in the Balkans and in Asian countries. So, now they have every reason to prove their capacity here in Mongolia.

I am glad to inform you that some serious Turkish companies have started to enter the Mongolian market. Is it enough? Certainly, not. But, it is just the beginning. I believe, you should expect more from the Turkish entrepreneurs.

**Do the Turkish companies have their own standards to do construction? What's the difference between Turkish construction companies and the other construction companies around the world?**

I guess in a short period of time Mongolia will get to know how to work with the Turkish construction sector. Their working habits will also change the mentality of how to conduct business in this country. This is the most important difference in my judgment because to fulfil the requirement of an undertaking it needs courage, [and] discipline. It needs hard dedication and hard working.

All these professional skills are there for Turkish companies. I fully rely on them. They are trustworthy companies. Once they enter into the project, they will do the job even before the envisaged time frame. They work hard, sleep less.

The Turkish construction sector is one of the leading sectors in the Turkish economy. Companies with a high reputation know very well how to conduct business. They are highly successful in completing turn-key projects.

Turkey's got a strong growing private sector as well – we can see that most of the large companies belong to banking and telecommunications – so are there any specific areas where Mongolia and Turkey can cooperate in the near future?

The Turkish economy has achieved

outstanding performance with its steady growth over the last 10 years. Sound macroeconomic strategies, prudent fiscal and monetary policies, structural reforms that the Turkish government has been pursuing in the last decade resulted in high rates of growth and increased confidence in the Turkish economy. As structural reforms have strengthened the macroeconomic fundamentals of the country, the economy grew with an average annual real GDP growth rate of 5 percent between 2002 and 2013.

A country which cannot produce cannot reach much. So I very much agree with the target that Mongolia has to start producing. But to do so, you need know-how, you need experience and you need good partners. In that respect, Turkey is a very good, tailor-made partner for Mongolia.

I know that mining is the leading sector in Mongolia, but for a sustainable economy you need to diversify it. Therefore agriculture, animal husbandry, food, cashmere, and leather are all important sectors for the Mongolian economy where Turkey can contribute immensely in sharing its experience.

**You share a border with Syria, Iran, Iraq and Jordan. What's the foreign policy like for a country with such an interesting geopolitical position?**

Turkey is strategically located at the epicenter of Eurasia. It is surrounded by three continents – Europe, Asia, and Africa. Its geo-strategic location belongs with its cultural and historical depth, giving the country its uniqueness. This has been an asset in forging economic partnerships with its neighborhood. Turkish membership in regional organizations such as BSEC, D-8, and ECO are a reflection of the multi-pronged character and regional orientation of Turkish foreign policy in the economic sphere. On the other hand, its membership in G-20 is an indicator for its growing role as a responsible stakeholder in the global economic governance.

Turkey sits in a tough neighborhood surrounded by hotspots but serves as an island of stability.

Of course, day-by-day the soft power of Turkey is growing. Maybe throughout the Cold War we were relying mainly on armed forces and our relationship with ▶

► allied nations. But, particularly in the last 10 to 15 years, Turkey emerged as a regional power whose actions may create certain global consequences.

Turkey has various assets and capabilities. When it comes to conducting foreign policy, certainly my ministry, the Ministry of Foreign Affairs, plays the central role in shaping the policy. However, there are other agencies and institutions which contribute to the successful implementation of that policy.

“TIKA” is one of them, Turkey’s cooperation and coordination agency. Yunus Emre Turkish Cultural Centers are another asset. Turkish Airlines, Turkish companies, TRT [Turkish Radio and Television Corporation], Anatolian Agency and the Turkish movie sector are yet other examples which play a central role in this field. ■

#### General outlook for the Turkish economy

Economy ranking	World's 17th largest, Europe's 6th largest
Population	76 million
Unemployment	9.7 %
Labor force	28 million
GDP	820 billion USD
GDP growth	4 %
GDP average growth	5.2 % /2002-2012/
GDP per capita	10.782 USD
Inflation	7.40%
Budget deficit	1.1 % of GDP
FDI inflow	12.7 billion USD
FDI outflow	3.2 billion USD
Trade volume/ growth % annual increase	403.5 billion USD / 3.7
Export	151.8 billion USD
Import	251.6 billion USD
Tourism	39 million visitors
-Revenue	32.3 billion USD
-World ranking	6th largest
Neighbors / 8 countries	Bulgaria, Greece, Georgia, Armenia, Iran, Azerbaijani exclave of Nakhchivan, Iran Syria

## RAILWAY

# ALL ABOARD FOR THE GROWING RAILWAY NETWORK

BY TERRENCE EDWARDS

**A** lack of planning has meant the softening global coal market has put Mongolia through the wringer.

Mongolia's policymakers failed to get to grips with developing the country's rail network while the economy was booming. Now the economy is slowing and coal prices are falling, the government is finding it can't make up the difference by boosting export volume because of bottlenecks in the transportation network.

Mongolia in April continued construction of its railway network as it attempts to boost exports of minerals, such as coal from its enormous Tavan Tolgoi coal mine, which is currently serviced by truck. The nation sandwiched between Russia and China plans to quadruple the size of its railway network to a total of 5,600 kilometres, starting with 265 kilometres from Hong Kong-listed Mongolian Mining Corporation's Ukhaa Khudag mine in the Gobi Desert to the Chinese border, says Yondon Manlaibayar, director general of the department of railway and maritime transportation at Mongolia's Ministry of Roads and Transportation.

Mongolia's cabinet in March approved the state-owned Erdenes Tavan Tolgoi's participation in a consortium of miners operating in the Tavan Tolgoi coalfields. Called Gashuun Sukhait Railway, the joint venture plans to launch construction of 13 kilometres of rail from the Gants Mod border port,

said Manlaibayar, to where a temporary offloading port will be built for trucks to unload their coal hauls.

“They don't want to wait for us to complete the whole line,” said Manlaibayar. “They want to start loading from here immediately, this year.”

It makes good economic sense to do so, he said. The limited number of truck drivers with the permissions to travel to the board zone to unload coal exports onto Shenhua's railway line in China allows them to call the shots and ask for exorbitant pay. A temporary offloading point would allow more drivers to make the deliveries and reduce deliveries until the full train line is finished.

Although the ownership structure of the Gashuun Sukhait Railway joint venture is not yet finalized, the Chinese-owned energy company Shenhua Group is expected to own 49%. State-owned miner Erdenes Tavan Tolgoi, local miner Tavan ►



► Tolgoi and Mongolian Mining's unit at Ukhaa Khudag, Energy Resources, would each own 17 percent. Shenhua is willing to put up 70 percent of the financing for the project, but that could give the Chinese state-owned operator more control than Mongolia may like down the road, says, Nick Cousyn, chief operating officer of Ulaanbaatar-based brokerage BDBSec.

"While Mongolian companies will have 51 percent of the equity, financing of the project would put Chinese SOEs [state-owned enterprises] at the top of the capital structure," said Cousyn, commenting on the fact that in the event that a company folds the corporate debt holders are the first to receive a return on their investment.

## The gauge debate

The miners at the Tavan Tolgoi coal deposit have long argued for a direct rail line to China. After years of waiting, Hong Kong-listed Mongolian Mining in June 2012 signed a concession agreement with the government and even held a ground-breaking ceremony a few days later. But that plan was rejected in May the following year. Instead, the government contracted Korea's Samsung C&T to do the job. The 217 kilometres of railway will be installed as soon as the embankment is finished, which is expected to happen by July, says Manlaibayar.

One reason the government has dragged its feet is the issue over what standard of gauge to use. China's railways utilise what is considered to be the international standard. However, Mongolian rail policy, implemented in 2010, requires Russia's wider gauge. Some have fretted about the added costs of having to move

tonnes of coal from one carriage to the next for the gauge transfer as well as the environmental toll from all the dust kicked up from moving such large cargoes of coal.

Many, however, are losing patience. "Currently the Mongolian coal industry is on the brink of survival essentially, with huge structural and competitive issues... It can hardly afford this gauge debate," Dale Choi, head of Independent Mongolian Metals & Mining Research, wrote in an email.

The rail line that Shenhua has promised to help build will use the Chinese gauge, while the Samsung C&T line will use the Russian gauge. Prime Minister has also stated that legislation brought to the State Great Khural for his 100-days economic stimulus program may allow for some Chinese gauge rail on Mongolian soil.

Meanwhile a railway station for gauge transfer will be built 40 kilometres north of the Chinese border is the current plan. An additional 27 kilometres of rail heading south to join the Samsung and Shenhua rail lines, explained Manlaibayar, would have to be built to create a complete route to China. He said the current projected cost of having to change gauges would be an added USD 3 to every tonne of coal.

## Transit is profitable

Now that developing the railways is gaining some traction, land-locked Mongolia also has plans to build a more comprehensive railway network to the east and west of the country. It plans to expand its rail freight capacity by 60 percent to 33 million tonnes a year by 2015, with an eventual target capacity of

100 million tonnes. "The rail was built in the 1950s – it needs a major upgrade," says Manlaibayar.

Last year, Mongolia saw the transit of 2.2 million tonnes compared with 15 million tonnes from neighbouring Kazakhstan. Manlaibayar reckons that transit of 10 million tonnes would be worth over USD 200 million a year.

Japan's Nippon Koei has 86 percent completed the design of an eastbound rail line that could link to rail lines able to reach ports in China's Bohai region. That would gain Mongolia better access to seaports in China for deliveries of its coal products to markets such as South Korea and Japan. The existing line heading south towards Beijing, says Manlaibayar, was not optimal because of the heavy congestion created by China's own domestic cargo transit.

Profiting from the growing trade within the region is a long-term strategy. One area that the country can look to exploit is the growing volumes of cargo travelling between Russia and China. Russia plans to increase the value of its trade with China by 150 percent from last year to USD 200 billion by 2020, Manlaibayar says.

"Obviously, a major part of that will be oil and gas, which won't be transported by rail, but there will be a need to transport these huge amounts of cargo," he said. "That's why we want to increase the capacity of our transit lines. Transit is a profitable thing."

Mongolia could facilitate that trade with its planned route in the east as an alternative to the already congested train lines from China's Manzhouli line to Russia, says Manlaibayar.

Mongolia has plans outside of its two giant neighbours, too. Earlier this year, Mongolia launched a trial run for the transport of goods from Jinzhou in China to Frankfurt in Germany, via Mongolia. He said the trial took 15 days to reach the destination and 14 days to return. "We shipped computer part products and because the product is so expensive itself, a small difference in transportation costs doesn't bother them," says Manlaibayar.

"Time is more important," he adds – a lesson that Mongolia's policymakers would do well to learn. ■



## ECONOMIST'S COLUMN

## MONGOLIA'S ACHILLES HEEL



MASA IGATA

*Founder & Chief Executive Officer, Frontier Securities*

*Mr. Masa Igata, Founder & CEO of Frontier Securities, is a well-known pioneer figure in Asian frontier markets with more than 25 years of professional experience in financial markets.*

Even though the data from the National Statistical Office shows that the trade deficit in the first quarter has improved quite significantly, we maintain our cautious stance on the outlook of the Mongolian economy.

That is based on the conviction that current expansionary monetary policy by the Bank of Mongolia (BOM) is not sustainable. We urge BOM to tighten its stance as early as possible to avoid the "hard-landing" scenario.

After looking at the most updated economic forecast of Mongolia done by the World Bank, Asian Development Bank and International Monetary Fund, we have confirmed that economic slowdown is eminent in Mongolia. Collectively, the outlook for Mongolia is still high, with around 7 to 10 percent of GDP forecast in the next three years. But, if you look at details more closely, they are based on the scenario that the government will take the right measures to cool down the economy.

However, if the government will continue to follow its current expansionary policy, they are more skeptical about the economy, especially after 2015. They are particularly concerned about stimulus measures taken by the central bank, strong balance of payment pressure driven by weak foreign direct investment and current account deficit and weak governance of politically important decisions like Oyu Tolgoi.

We believe this situation is not sustainable. And, some measures should be taken as soon as possible.

This report summarizes the view from foreign donors and investors, and suggests possible measures for the Government.

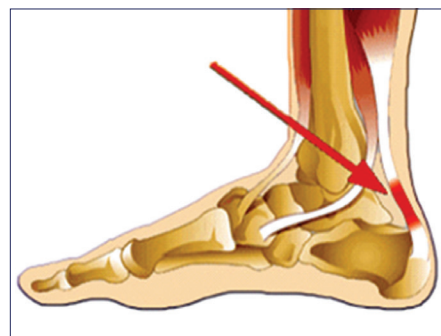
### Mongolia's Economy

The Mongolian economy has grown by 12 percent, on average, in the last three years. And, it is expected to grow another 8 to 10 percent in the next three years according to the Asian Development Bank, World Bank and International Monetary Fund.

However, the pace of growth will slow down going forward in any scenario.

As the current strong economic growth relies on the issuance of the Chinggis Bond and expansionary monetary policy, we believe loose monetary policy will result in a weaker currency, resulting in higher inflation. The International Monetary Fund predicts this occurrence as a risk scenario (see below). Under its weak policy scenario, the fund forecasts that economic growth in Mongolia could be minus two years in a row in 2015 and 2016, which could be more severe than the period in 2009 when Mongolia, and the world, was impacted by the global financial crisis.

Achilles tendinosis tendinitis



This risky scenario mirrors the scenario we predicted 13 months ago. Our report identified the potential risk of the Mongolian economy, which we believed was due to too loose budget controls. But perhaps not many people have paid attention our findings at that time. My current warnings regarding the economy have not changed so much from then. But, the risk of the "hard-landing" scenario, which we predicted, is the most likely to play out. ▶▶

## Strong Policy and Weak Policy Scenarios, 2010-18

2018	2010	2011	2012	Strong policy scenario					Weak policy scenario							
				2013	2014	2015	2016	2017	2018	2013	2014	2015	2016	2017		
Real GDP growth	64	17.5	12.3	11.8	9.6	7.0	5.2	8.5	6.0	11.8	12.1	-2.6	-12	3.2	1.2	
Mineral growth	3.6	7.3	89	16.1	33.4	7.2	-2.1	14.9	1.8	16.1	33.4	7.2-2.1	14.9	1.8		
Non-mineral growth	7.0	197	12.9	11.0	5.0	7.0	7.0	7.0	7.0	11.0	8.0	-5.0	-10	0.0	1.0	
Consumer prices (end-period)	14.3	9.4	14.2	11.7	11.0	7.4	6.7	6.6	5.5	11.7	14.3	11.7	5.0	5.5	5.4	
<b>Fiscal accounts (in percent of GDP, unless otherwise indicated)</b>																
Overall balance (in percent of GDP) 1/	0.5	-4.8	-10.9	-13.5	-7.4	-3.8	-1.7	-1.8	-2.0	-13.5	-13.1	-10.1	-7.6	+5.1	-4.7	
Structural balance (FSL in percent of GDP) V	-6.9	-11.5	-13.7	-7.5	+4.2	-2.0	-2.0	-2.0	-13.7	-13.3	-10.5	+8.0	-5.3	-4.7		
Non-mineral balance (In percent of non-mineral GDP)	-13.6	+17.8	+20.7	-22.8	-15.9	-11.3	-9.6	+10.7	-10.6	-22.8	-23.4	-21.6	-20.3	-19.4	+19.4	
Non-mineral revenue (In percent of non-mineral GDP)	33.8	39.3	36.5	35.1	35.0	34.8	34.0	33.8	326	35.1	34.8	36.0	359	37.0	36.9	
Total expenditure (In percent of non-mineral GDP)	47.4	57.1	57.2	57.9	50.9	46.1	43.6	44.5	43.1	57.9	58.2	57.6	56.2	56.4	56.3	
Total public debt (in percent of GDP)	359	388	63.0	67.3	65.8	60.4	55.9	52.4	50.1	67.3	72.9	78.1	81.1	79.9	79.0	
of which : Domestic debt	5.1	10.9	14.7	15.5	15.1	15.5	16.3	16.2	16.6	15.5	14.7	15.6	16.8	17.5	18.4	
External debt	308	27.9	483	51.8	50.7	44.9	39.6	36.2	33.4	51.8	58.1	62.5	643	62.4	60.6	
NPV of public debt	546	58.6	58.0	53.3	49.5	46.4	44.7	58.6	63.9	68.9	72.1	70.9	70.4			
<b>Monetary accounts (Change in percent)</b>																
Broad money	61.6	29.2	21.5	37.1	755				72.3	18.8						
Reserve money	30.5	24.1	17.1	12.2	40.9				288	11.9						
Credit to the private sector	16.1	29.5	44.7	54.1	30.0				29.1	33.6						
<b>External accounts</b>																
Current account balance (percent of GDP)	-14.9	-31.7	-32.8	-31.6	-20.3	-18.3	-21.5	-15.3	-14.6	+316	-22.2	-14.1	-16.2	-9.9	-8.7	
Gross official reserves (in millions of U.S. dollars)	2,490	2,630	4,126	2,214	2,290	2,178	2,369	2,592	2,821	2,244	755	116	308	532	758	
(in months of imports)	3.9	3.9	6.5	3.4	3.3	3.0	3.0	3.2	32	3.4	1.2	0.20.5	0.8	10		
<b>Memorandum items:</b>																
Nominal GDP (in billions of togrogs)	8,415	11,088	13,944	16,691	20,352	23,513	26,258	30,358	34,125	16,691	21,692	24,167	25,668	28,126	29,952	
Nominal GDP (in millions of U.S. dollars)	6,244	8,709	10,258	10,982	11,417	12,494	13,286	14,701	15,918	10,982	10,927	10,227	10,086	10,586	10,815	
Government expenditure (in billions of togrog)	3,081	4,997	6,494	8,000	8,205	8,636	9,382	10,943	12,104	8,000	9,883	10,468	10,998	11,700	12,439	
Government expenditure (growth in percent)	32	62	30	23	3	S	9	1711	23	24	6	5	6	6		
DBM spending (in percent of GDP)	-	3.4	9.0	5.5	2.2	0.0	0.0		0.0	9.0	11.3	8.55.9	3.3	2.6		

Sources: Mongolian authorities; and IMF staff calculations.

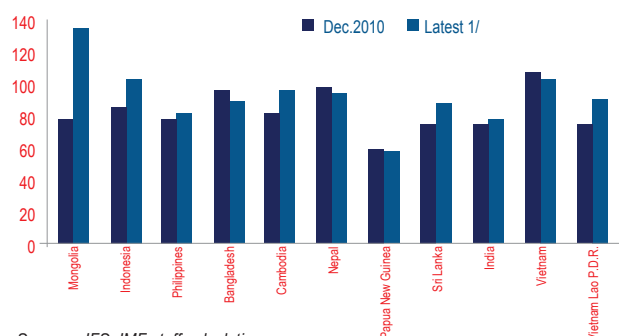
1/ Includes DBM spending.

## Economic Risks

This bar chart shows loan-to-deposit ratios of emerging economies in Asia, including Mongolia. The ratio has increased the most in Mongolia in the last three years.

And the same ratio has continued to increase since December 2010. The ratio is almost equivalent to December 2008, when Mongolia's bubble burst. ►►

### Loan-to-Deposit Ratio (In percent)

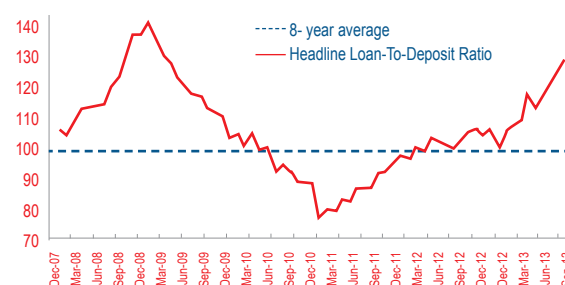


Sources: IFS, IMF staff calculations.

1/ Latest August 2013 (Mongolia), April 201 (Nepal), March 2013 (Indonesia, PNG, Bangladesh, Cambodia, Lao P.D.R.), February 2013 (Philippines), December 2012 (India, Sri Lanka, Vietnam).

### Commercial Banks' Loan-To-Deposit (L/D) Ratio

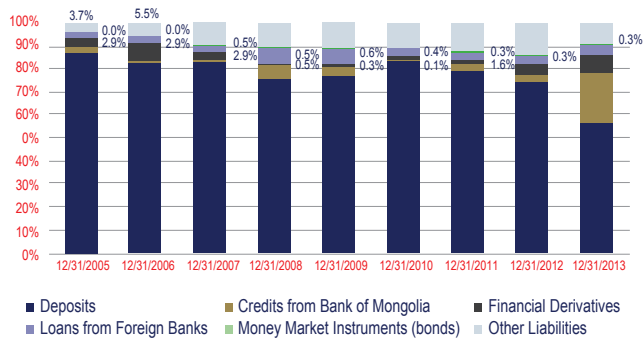
(Dec. 2007-Sep. 2013)



Sources: Mongolian authorities; and IMF staff estimates

▶ The high loan-to-deposit ratio is the result of an expansionary monetary policy by the Bank of Mongolia. As you see below, credit from the central bank now accounts for 22 percent of the bank's liabilities which has increased a mere 3.6 percent from a year ago.

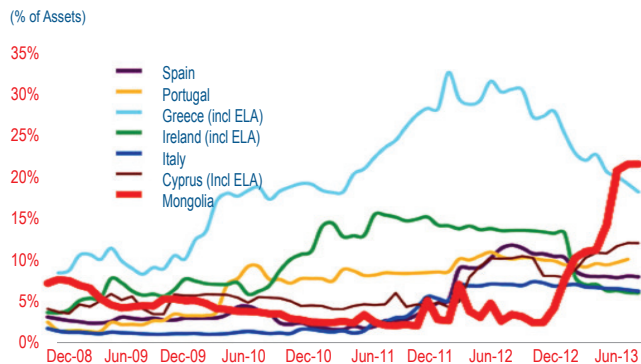
### Breakdown of Bank's Liabilities (2008-2013)



Sources: Bank of Mongolia

As a result, the banking system's reliance on central bank funding has increased dramatically in the last 18 months. As you see on the graph below, the reliance has exceeded that of major weak credit countries like Spain, Portugal, Greece, Ireland, Italy and Cyprus. And now, it looks like Mongolia may be entering a similar insolvent condition.

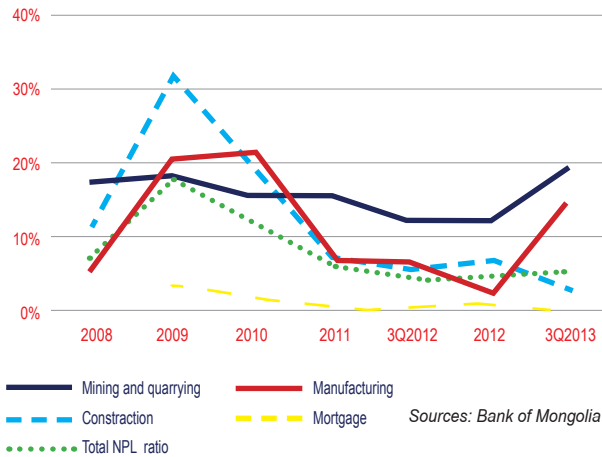
### Bank Systems' Reliance on Central Bank Funding



Speaking on non-performing loans (NPL), the ratio has increased a bit as of the end of September last year at more than 5 percent. This figure is comparatively low to the 20 percent peak after the global financial crisis. However, at a time when credits increase, the ratio tends to be low. So, as the increase of the credit has softened this year, the NPL ratio will increase.

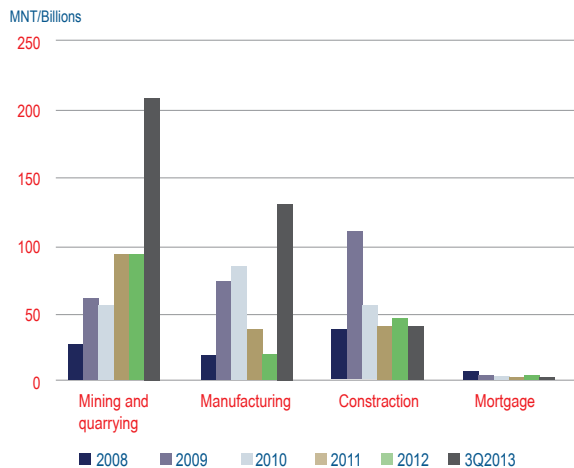
Looking at sectors, we believe that mining, manufacturing, construction and mortgage sectors are the most vulnerable sectors. And, we have already seen some evidence of growing NPLs in these sectors as you see below.

### NPL Ratios by Industries



Sources: Bank of Mongolia

### NPLs in Mining Manufacturing, Trade Construction and Mortgages

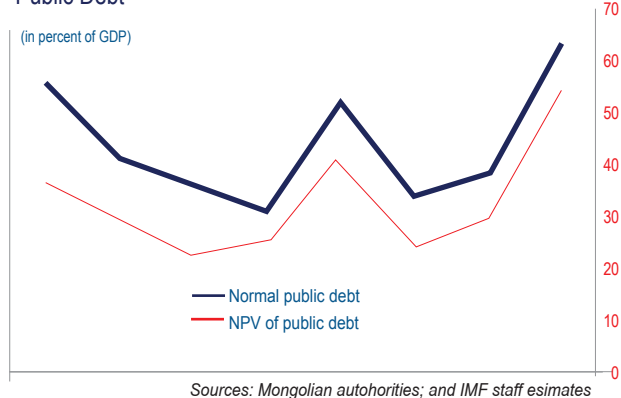


Sources: Bank of Mongolia

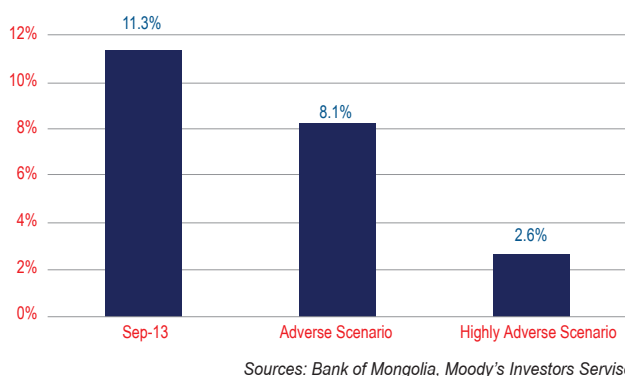
As for the balance sheet of the government, charts below show the recent sharp increase of both nominal and net present value of public debt. As you see the structure of public debt has tripled in just two years. As a result, the public debt in percentage of GDP has increased from 36 percent of GDP in 2011 to 63 percent of GDP in 2013. The government assumes that the ratio will decrease gradually if the economy grows at 12 to 15 percent, just like they did in the past.

However, as the economy will only increase modestly and the currency may be weakened more than expected, the ratio may remain high in the next half a decade. In addition, the maturity of the debt of around USD 1 billion is expected for 2017 and 2022. So, the government needs to finance for those in the future. To repay the debt, exports of mining (especially Oyu Tolgoi and Tavan Tolgoi) are expected to contribute a lot. However, the revenue should be much smaller than previously anticipated because of the delay to production and much weaker copper and coal prices. ▶▶

## Public Debt



## Stress Test Results for Mongolian Banks



Going back to the situation of banks in Mongolia, below are the "Stress Test Results" and "Stress Test Assumptions" made by the credit rater Moody's. Based on the adverse scenario and highly adverse scenario, you

## Stress Test Assumptions

Loan Type (MNT billion)	Adverse Scenario					Highly Adverse Scenario			
	Portfolio Weight	Actual NPL on Sep BO, 2013*	Probability of Default	Loss- Given- Default	Expected Loss	Probability of Default	Loss- Given- Default	Expected Loss	
Agriculture	1.3%	6.8%	8%	40%	15%	50%	50%	25%	
Mining and Quarrying	10.8%	19.1%	16%	60%	12%	28%	80%	22%	
Manufacturing	8.8%	14.8%	4%	50%	4%	20%	70%	14%	
Construction	12.9%	3.2%	8%	50%	5%	30%	70%	21%	
Wholesale and Retail Trade	11.8%	3.8%	7%	50%	3%	16%	70%	11%	
Real Estate	1.1%	8.6%	12%	40%	11%	30%	60%	18%	
Transportation and Storage	1.7%	8.2%	10%	55%	7%	28%	80%	22%	
Financial and Insurance	0.5%	2.4%	5%	50%	1%	8%	70%	6%	
Other Corporate Loans	6.5%	3.5%	8%	50%	3%	13%	60%	8%	
Individual Loans	28.8%	1.6%	4%	40%	2%	10%	50%	5%	
Mortgages	15.8%	0.2%	3%	40%	1%	9%	50%	5%	
Weighted Average	100.0%	5.3%	6.3% <sup>19</sup>	46.6%	4.0%	17.3%	61.6%	11.4%	

## Conclusion

As explained earlier, the bulk of the banking system asset growth is funded by the central bank. If the Bank of Mongolia continues its current strategy, risks of higher inflation and weaker currency will be heightened. The government's balance sheet will deteriorate as well. Hence, a sudden shock coupled with weak balance of payments may lower international reserve and result in the default of sovereign debt in the future. To avoid

## Mongolia: Structure of Public Debt

	2010	2011	2012
Public debt (in MNT bn)	3,020	4,304	8,790
Public debt (in percent of GDP)	35.9	38.8	63.0
Domestic debt (in MNT bn)	429	1,206	2,055
Domestic debt (in percent of GDP)	5.1	10.9	14.7
Government bonds	200	517	1,280
Bank restructuring bonds	100	80	60
Civil servants housing	95	137	72
Wool, cashmere, SMEs	5	300	197
Other bonds 1/			951
Tax prepayments	229	689	776
OT	229	353	377
ETT		336	399
External debt (in MNT bn)	2,591	3,099	6,735
External debt (in US\$ mn)	2,061	2,219	4,838
External debt (in percent of GDP)	30.8	27.9	48.3
Multilaterals	1,551	1,727	1,706
ADB	797	855	832
World Bank	506	624	653
IMF	247	249	221
Official bilateral	824	1,053	1,635
Paris club	632	676	993
Non-Paris club	193	377	642
Commercial	0	0	2,896
Sovereign "Chinggis" bond			2,088
DBM bond			807
BOM foreign liabilities (excl. IMF) 1/	16	15	484
Other	200	304	14

Source: Mongolian authorities.

1/ Source: Bank of Mongolia and staff estimates.

can see how the profit ratio of the banks will be influenced. Under the highly adverse scenario, the ratio may go down to similar figures which banks in Mongolia experienced at the time of the global financial crisis.

## HYDRO-POWER PLANT

# EGIIN GOL HYDROPOWER PLANT VERSUS POLITICS

BY D. BEKHEE

Several governments have set forth on plans for the Egiin Gol Hydropower Plant project since 1991. Every government has played some role in the decision making for the project because it would be such a huge infrastructure project that could bring a boost to the country's development.

At the beginning of the democratic revolution in 1990, an initial study for

the project was carried out by the Asian Development Bank. The project was delayed, however, due to uncertainties surrounding investment.

Ten years later, in 2000, the government of that time returned to the project and embarked upon developing a feasibility study. It sparked the interest of investors, but, unfortunately, Mongolia's political parties could not reach a deal.

Thirteen years on, in 2013, the

government established a team to make the project a reality. Water experts were pleased by the decisive action. A new feasibility study is under way, with more detailed research being carried out on the environmental impact it would have. It is also seeking out financing opportunities.

Road and electrical construction is planned for the start of this summer. A French company whose name has not yet been publically released has



*Eg River, Zavkhan province*

► been selected through a tender bidding process to act as a legal and general advisor to the project.

There are a number of reasons to favour the development of Egiin Gol Hydropower Plant:

1. It would be a new renewable energy source for the growing demand for energy.
2. It would ease dependence on Russia for energy while Mongolia continues to import USD 25 million worth of energy each year from its neighbour to the north.
3. It would make efficient use of waters leaving the country by river.
4. It would add more humidity and have a positive effect on climate change in the country.
5. It will reduce the consumption of coal by approximately 200,000 tonnes a year, which would result in an enormous reduction of air pollution in Ulaanbaatar and other

urban areas.

## The Project

The hydropower plant would be built upon Eg river, which flows through the territories of Khutag Undursoum and Bulgan province. The 710-metre-long dam would be made of hard concrete stretching 93 metres high. Behind the dam would be a 125 square meter water reservoir. According to the 2007 feasibility study, the hydropower plant would consist of four turbine generators with the capacity of 55 megawatt each for a total 220 megawatts of power generation.

The power generated from the hydropower station would be used for Mongolia's central electric grid, transmitted through a sub-station power plant located at Erdenet. Included in the project is the construction of 70-kilometres of electricity transmission line and a 125-kilometre road to link the station with Erdenet.

Thermo-power plants usually consume up to 20 percent of the energy they produce

while the Egiin Gol Hydropower Plant would consume a mere 1percent of the energy it produces. That would mean 96 million kilowatt energy or USD 4.7 million in savings a year. A preliminary estimate figures that returns on investment would arrive in 10 to 15 years and six-fold profits within 100 years.

Studies between 1993 and 2007 found that the project could be done in an environmentally safe way that would have minimal impact on the soil, forests, and biological diversity of the area.

The hydropower plant will be upstream from the Eg and Selenge rivers. A fisheries study on the Eg River will be conducted by the Institute of Geocology and Taimen Conservation Fund of Mongolia to ensure that the fish that live in these waters are taken care of. Trees and bushes would be planted in a 1,300-hectare area around the hydropower plant.

The Egiin Gol Hydropower Plant is a dream for those who work in the field of renewable energy. Their dreams will hopefully come true. ■





## BCM'S NEWSWIRE HIGHLIGHTS

NewsWire is a weekly news aggregate sponsored by the Business Council of Mongolia. Each week NewsWire delivers breaking and significant news from local and international news sources for a Mongolian and foreign audience alike. The following are news highlights from the month of April:

### BUSINESS

#### MONGOLIA SET TO RESOLVE MINING LICENCE DISPUTE, SAYS KINCORA

Mongolia plans to put a resolution to parliament that will end a dispute between 11 foreign licence holders and the government over the invalidation of 106 mineral exploration licences, one of the companies affected, Kincora Copper Ltd., said on Monday.

The dispute is one of several issues, led by disagreements between Rio Tinto and the government over plans to expand the giant Oyu Tolgoi copper mine, that have soured investor appetite for Mongolia over the past two years. The 106 exploration licences were declared void by a Mongolian court last year after it found the former head of the Mineral Resources Authority guilty of illegally approving the licences

between 2008 and 2009.

Toronto-listed Kincora Copper Ltd, one of 11 foreign investors affected, said the proposed resolution was a "win-win" to end the dispute over its two cancelled licences, on which the company had to take a CAD 7 million writeoff last year.

"This case has had a major, negative impact on investor sentiment towards Mongolia. And the way in which the government responds to investor concerns about the revocation of licences, we hope, will set a positive and visible precedent as to how future investors will be treated," Kincora Chief Executive Sam Spring said in a statement.

*Source: Reuters*

#### MONGOLIA INVESTMENT SUMMIT LONDON RECAP

Mongolia's most profitable sector, mining, was a key topic of discussion during the first day of the Invest Mongolia Summit held in London on May 1. Investors gathered to discuss the improvements made to Mongolia's regulatory system as well as areas still needing attention.

"President Elbegdorj said: 'Mongolia has made mistakes and must take steps to change regulations' and did so in part with the new Investment Law of November

1, 2013. But many points 'still sleeping,' including OT Phase II financing, Chalco, 106 mining licences and Long-name law," said Vice Minister for Economic Development Ochirbatyn Chuluunbat. While 11.7 percent growth in 2013 is still impressive, the country was facing a currency devaluation that was having serious impacts on US denominated loans and the country's growing budget deficit. Attracting foreign investment is imperative, said the vice minister, so treating all investors—"local and foreign"—equally and fairly was a main priority for the government.

Chris Melville, a partner at Ulaanbaatar-based law firm Hogan Lovells LLP, lauded the government's new Investment Law, noting that it was positive that the government recognised the issues with past legislation and made the necessary corrections. Moving forward, however, Mongolia will have to focus on ensuring the laws are implemented as they are intended. Norihiko Kato, chief executive officer of Khan Bank, chimed in on the Investment Law, noting that Mongolia's capital markets were still underdeveloped as long as there was still no custodian services or inter-banking market.

The fine-tuning of legislation

and the time to watch how Mongolia enforces its new laws will mean that investment to Mongolia will not return overnight, according to Elena Clarici, managing director of Meridian Equity Partners in the United Kingdom. Advising that cost focus was key for the mining sector, she said, adding that it was unlikely that investors would invest in large quantities in the next 12 months but the industry could be booming again in three years.

*Source: Business Council of Mongolia*

### ECONOMY

#### MONGOLIA DOWNGRADE WEIGHS ON CHINGGIS BOND

Mongolia has been downgraded by Standard & Poor's, further dimming the allure of one of the more eye-catching bond market debutantes of the emerging markets debt boom.

The U.S. rating agency cut Mongolia's credit rating by one notch to B+, deep in junk territory and just three notches above grades that are sometimes called "extremely speculative". In 2012 Mongolia issued its first Eurobond—dubbed a "Chinggis bond" by wags—raising a whopping USD 1.5 billion for 10 years at below Spain's borrowing costs at the ▶▶

time. The country has been rescued by the International Monetary Fund five times in the past two decades or so, but investors still placed USD 15 billion of orders—equal to 150 percent of its annual economic output.

However, since then investors have become more discerning on emerging market bonds, and Mongolia in particular. The yield of the international bond maturing in 2022 has climbed from 5.62 percent last May to 7.55 percent today.

Economic growth is strong and government debts relatively weak, but Mongolia's macroeconomic vulnerabilities—particularly its dependence on foreign finance—are significant, and government policy has been erratic. Still, one big international investor has kept faith with Mongolia. Franklin Templeton funds—mostly controlled by Michael Hasenstab—own over 14 percent of the Chinggis bond, according to the most recent filings.

*Source: Financial Times*

### **MONGOLIA REQUESTS EXTENSION FOR MNT-CNY SWAP AGREEMENTS**

Prime Minister Norov Altankhuyag requested an extension to Mongolia's currency swap agreements with China while meeting with China's Finance Minister on 29 April.

"Mongolia is willing to extend the validity period, but with an increased volume of national currencies to exchange. We believe the finance minister would pay more attention to resolve this issue on a

timely basis." Altankhuyag said the swap agreement both strengthened Sino-Mongolian relations while providing stability to the Mongolian economy.

Separately, Jiwei thanked Mongolia for accepting Chinese President Xi Jinping's proposal to jointly found the Asian Infrastructure Investment Bank (AIIB). Altankhuyag said Mongolia sees the bank as an opportunity to promote Mongolia's belief that developing infrastructure is crucial to the economic growth of landlocked countries.

*Source: Info Mongolia*

## **POLITICS**

### **MONGOLIAN PREMIER UNVEILS 100-DAY PUSH TO REVIVE ECONOMY**

Mongolia's Prime Minister unveiled a stimulus bill, dubbed a "100-day action plan," that will seek to revive the mineral rich nation's flagging economy.

Prime Minister Norovyn Altankhuyag's 50-point agenda promises to boost infrastructure, mining, manufacturing and the development of small and medium-sized businesses. The bill still needs the approval of parliament and is part of a renewed drive to improve the economy after two years of slowing growth.

"Within these 100 days we believe we should reduce bureaucracy, increase mining, approve the re-issue of exploration licences" and resolve a dispute over 106 canceled mining licences,

Altankhuyag told foreign press and diplomats from nations including the United States, China and Russia, at a briefing in the capital, Ulaanbaatar. Mongolia is seeking to energize an economy that saw growth decline from a world-beating 17.5 percent in 2011 to 11.7 percent last year. The Mongolian tugrik fell to a record low of 1,796 to the dollar on 29 April and has lost 25 percent of its value over the past 12 months.

Altankhuyag's plan broadly seeks to promote foreign investment and reduce Mongolia's reliance on imports. Infrastructure spending proposed includes building a road to connect the landlocked nation's two neighbors, Russia and China; constructing thermal power stations; and developing two free economic zones. It also calls for improved debt management, tax incentives for foreign banks, and raising the amount of Mongolia's currency swap agreement with China.

Mongolia will also offer concession projects worth USD 1 billion "not only in mining but also in the tourism sector," Altankhuyag said. "It's important to focus on local businesses as well as mining and the fact that they are trying to do multiple things simultaneously is a good thing," said U.S. ambassador Piper Anne Wind Campbell, who attended the briefing. "I do think you have to move forward on all these as opposed to looking for one silver bullet."

Altankhuyag, 56, faces public pressure to improve the economy after citizens, numbering many hundreds according to an eyewitness account, rallied at least twice on Ulaanbaatar's Chinggis Khaan Square earlier this month to protest against an inflation rate that's running at 12.4 percent.

*Source: Bloomberg*

### **MONGOLIA TO REVISE MINERAL LAW TO ATTRACT INVESTMENT**

Mongolian Mining Minister Davaajav Gankhuyag Wednesday submitted a draft amendment to the Minerals Law to Parliament Speaker Zandaakhuu Enkhbold, as the country is trying to improve its investment environment.

Despite the adoption of new laws and regulations to make the investment environment favorable, no new international and domestic investment is coming to the exploration sector which is the driving engine of the mineral sector, said the minister, quoted by a press release of the Mongolian parliament.

The draft amendment calls for setting up a database about funds raised from international stock markets, improving agreements between holders of mining licences and the local government, feasibility studies, and making clear the roles and responsibilities of government agencies and mining licence holders. The draft amendment also bans transference of exploration licences wholly or partially within three years since the issuance of the licence. ■

*Source: Shanghai Daily*