

## Chapter 2

# Current Status of Mongolia's Economic and Social Development and Future Development Trends

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*Editor's introduction:* As the head of the Mongolian government's primary planning and development committee, Mr. Khashchuluun's remarks provide a key perspective on – and bellwether of – the gargantuan and yet uneven economic development that now envelops Mongolia. By some estimates, Mongolian economic growth is poised to increase at an annual rate of more than 20% in the next few years – due largely to the revenue of large mining infrastructure projects in remote areas of the country. From the perspective of herders and rural populations, as well from the economic impact in towns, for the government, and in the teeming capital of Ulaanbaatar, these developments are far from remote. As Mr. Khashchuluun delineates, the Mongolian government has developed a sophisticated and fiscally responsible economic growth and social development plan that combines support for mining development and infrastructure along with economic sector diversification, growth of Mongolian human capital, and business-government partnerships. As he also notes, burgeoning economic growth in Mongolia abuts the fact the Mongolian rate of poverty has been stubbornly high if not rising.

The challenges of pronounced and growing wealth disparity among Mongolians – including between increasing numbers of affluent elites and millionaires vis-a-vis dispossessed rural herders and swelling numbers of impoverished urban squatters in the capital city – emerged in our conference discussions as a key social and political as well as technical economic issue. The great growth of foreign cash influxes and of government expenditures begs questions of wealth distribution, the overall welfare of Mongolians, and the underlying values and purpose of national and social

*development in Mongolia. It was striking how spontaneously and robustly these questions were raised and addressed from multiple vantage points in discussion following Mr. Khashchuluun's presentation. As opposed to the scholarly or professional division of technical economic issues from those of culture, history, meaning, and value, these became quickly and integrally intertwined. Amid his technical expertise, strategic analysis, and detailed economic understanding, it may be noted that Mr. Khashchuluun actively acknowledged and participated in this broader discussion, both after his presentation and later in the conference.*

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## **Current development level of Mongolia**

In 2010, many nations showed signs of growth after having overcome the effects of global financial and economic crises. Mongolia reported economic recovery resulting from the *Stand-by* stabilizing program that was undertaken in cooperation with the International Monetary Fund (IMF). When the figures are all in, we anticipate recording a 6 percent increase of real GDP in 2010. If 2010 was a year of high inflation caused mainly by the increase of major food items, 2011 is expected to be low-inflation year.

The World Bank has placed Mongolia in the group of low-to-middle income countries; while in 2007 Mongolia ranked 115 out of 182 countries by its Human Development Index, having surpassed 67 countries in the world, in 2010 Mongolia secured 100th place and entered the group of countries with a medium level of human development. Last year's high inflation rates associated with food price increases are not expected this year. According to research-based estimates, international ranking and measurement studies should show improved economic competitiveness and business environment indicators for Mongolia.

In 2010, thanks to high prices of main export items on the global market, Mongolia enjoyed an increase in its GDP, reaching USD 2,221.5 in per capita terms. In order to further sustain this growth and development, new national programs were initiated. National programs such as “Mongolian Livestock” and the “Third Campaign to Recover Arable Lands [Atar-3]” target animal husbandry and agricultural sub-sectors and will create foundations for accelerating their development. Also, creation of new factories for meat, milk and leather processing in rural and urban areas that are projected in the implementation plan of the “Mongolian Industrialization Program” will increase output volume of the national processing industry.

Despite fast economic growth and numerous targeted actions and activities, poverty remains high in Mongolia. The poverty level that stood at 38.7 percent in 2009 has increased slightly in 2010, to 39.2 percent. Mongolian national policy documents - including the Millenium Development Goals-based National Development Policy for 2007-2015, and the Mongolian Government’s Action Plan, prioritize poverty reduction and elevation of living standards as their key goals. The Mongolian government provides all support for these activities and actions.

The Mongolian Government has declared the 2011 as the Year of Employment Opportunities, and had intensified its efforts aimed at supporting job placement services, improving the system of training and re-training, and further encouraging on-the-job training and apprenticeship. High economic growth and the policy of supporting employment and job creation has indeed resulted in a drop in the unemployment rate from 13 percent in December 2010 to 8.7 percent as of June 2011.

Average household income is increasing steadily, standing at 263.7 thousand MNT in 2007, 363.6 thousand MNT in 2008, 402.5 thousand MNT in 2009 and 479.2 thousand

MNT in 2010, showing an 26.8 percent annual average increase rate.

In line with the plan to start several large mining projects, the Mongolian government is focusing on creating supporting infrastructure and financial systems. While many countries with vast natural resources have been able to effectively manage their revenues, a few examples exist of mismanagement and ineffective policies that resulted in waste of development opportunities. We are carefully studying lessons provided by their experiences to use in the development of our policies and programs. We understand that we will need to mobilize great effort in order to start economically exploiting large mining deposits and transporting, exporting, and selling minerals on the global market.

Mongolia does not want to become a raw-material/minerals supplier or to increase our dependence on any one economic aspect; government policies are essentially aimed in the opposite direction. It is important for Mongolia to develop multiple export items and support production of value-added products as part of our economic diversification policy. Our goal is to see Mongolia develop into an industrial country that can take advantage of (and not be subservient to) developments taking place in the mining sector.

In this respect, Mongolia has reached a new stage in its development. Our most immediate goals include building an industrial center in Sainshand city, creating similar centers in other regions, reforming the infrastructure sector, building new railroad and auto roads, and developing modern communication technologies across the country. Alongside the construction and infrastructure projects associated with the large Oyutolgoi, Tavan Tolgoi and Ukhaa Khudag mining projects, we are planning to launch a large-scale mid-term national infrastructure project titled “New Development.” This project will build south-north and east-west lines of the

Millennium Road project, maintain and rebuild Ulaanbaatar's city road network, and conduct major construction work in relation to the "100 thousand apartments" project. Some of these project and programs have already started demonstrating solid outcomes.

The above remarks alluded to the creation of favorable natural environment. This is key to further economic growth and development in Mongolia, which is beginning to arrive at a phase full of development opportunities. The great interest of large international and transnational corporations in the Mongolian mining sector and in other sectors will be a major factor contributing to Mongolia's future development.

### **Macroeconomic situation**

The Mongolian economy has shown rapid growth in a very short period thanks to a post-crisis external environment that has been very favorable to the Mongolian economy. This includes high-level decisions to launch large-scale national projects, creation of a better domestic business environment, and adoption of policies that support domestic consumption and boost local production. Together, these resulted in increased foreign investment and export growth. The Mongolian economy grew by 7 percent in the first half-year of 2010 and has picked up its growth speed to reach 14.3 percent in 2011. This one of the highest national economic growth rates not only in the region but also globally.

Although government spending in the first half of 2011 has increased by whopping 32 percent, this is only 40 percent of the GDP in nominal terms. Economic growth resulted in the increase of national revenue, which grew by almost 60 percent during the first 8 months of 2011 as compared to the previous year. The national budget has tabled a surplus of almost MNT 226 billion.

Minerals export in the first 8 months of 2011 has increased by about 80 percent, boosting export revenues to MNT 2.9 billion. At the same time, growing investment and construction work and increasing oil product prices and volumes have increased imports to USD 4.2 billion, resulting in foreign trade deficit of USD 1.3 billion. Despite widening this foreign trade deficit, the overall balance of payment in the first 7 months showed a net gain of USD 288 million proving positive balance in the foreign trade sector.

Foreign direct investment of USD 2.2 billion in the first 7 months has contributed to this positive balance of payment.

Due to increased GDP in nominal terms, money supply has increased by 61.7 percent compared to the previous year.

If we look at Mongolian economic structural trends for 2011-2013, we see that mining sector's volume in the GDP has increased as a result of launching the Oyutolgoi, Tavan Tolgoi and other large mining projects. Specifically, opening of a copper processing plant on the territory of the Oyutolgoi deposit in 2013 will result in the three-fold increase of copper mining compared to the current level. Also, it is estimated that coal mining from the Tavan Tolgoi mine will increase in 2012-2013, enabling extraction and export of about 15 million tons of coal annually.

It is a pleasure to note that mid-term real economic growth is estimated to continue at a high rate as a result of increased investment in the expanding mining sector and construction of accompanying infrastructure.

Mongolia's GDP is estimated to grow by 19.4 percent in 2011, by 19.9 percent in 2012 and by 14.8 percent in 2014, which will result in GDP per capita to reach USD 3458 in 2011, USD 5234 in 2012 and USD 6374 in 2013. Trade, transportation, mining, education and construction sectors are expected to be major contributors to this growth.

Foreign trade volume is estimated to reach USD 11 billion in 2011, USD 15.8 billion in 2012 and USD 18.7

billion in 2013. The foreign trade deficit is projected to be 1.9 percent of GDP in 2012, but in 2013 goods trade will increase to reach possible balance with the estimated surplus of 11-13 percent of GDP in 2013-2014. The main condition for mid-term positive balance of foreign trade is estimated to be faster growth of export volumes, which will surpass import volumes as a result of the launch of large mining exploitation projects. More specifically, it is projected that the goods export will increase by 23 percent in 2012, by 43.4 percent in 2013 and by 18.4 percent in 2014, while import volume will enjoy a steady increase of 11.2 percent throughout this period. As a result, foreign trade is expected to enjoy surplus of USD 1.7-2.4 billion starting 2013.

Balance of payments are expected to show a surplus of USD 1.2 billion in 2011, of USD 2 billion in 2012, and of USD 2.9 in 2013. The foreign currency reserve at the end of 2013 is estimated to reach USD 8.3 billion.

## **Real Sector Development**

The Mongolian economy relies on few sectors, which are low in processing and are dominated by primary production. In other words, Mongolia has poorly developed industrial sectors. More specifically, in 2010 mining and agricultural sectors comprised 38 percent of GDP of Mongolia. Ninety percent of exports are constituted by unprocessed and low-technology products –basically, raw materials. These products are characterised by the highest fluctuation of prices on the global market. Also, agricultural products that make up 15 percent of export (including animal products and meat), are highly susceptible to weather conditions and natural forces, rendering subsistence of herders and agricultural workers highly dependent on climatic conditions.

If broken down by sectors, animal husbandry is the main agricultural sub-sector. It suffered a loss of 10 million

heads of stock during the hard winter of 2009-2010, which reduced the output of this sector by 19 percent. The sub-sector is now recovering, with a total of 12 million heads of stock raised in 2011. This increased the sub-sector production by 14 percent during the first half of 2011.

The “Third Campaign to Reclaim Arable Lands” launched by the Mongolian Government in 2008 has resulted in a substantial increase of crop, potato, and vegetable production. The 343.1 thousand hectares of land harvested in 2011 is expected to produce 419 thousand tons of grain, 174 thousand tons of potatoes, and 90.5 thousand tons of vegetables.

During the first 8 months of 2011, mining sector production has grown by 8 percent in real terms. This growth is mainly due to a 28 percent increase in coal mining and a two-fold increase in iron ore extraction. In order to facilitate further rapid expansion of the mining sector, there is a need to increase capacities of the transportation, energy, water, and infrastructure sectors.

Specific to the mining sector, further issues demanding policy decisions include development of responsible mining, improvement of natural and environmental restoration, and regulation of artisanal (including wildcat or “ninja”) mining activities.

Mongolia is working to launch large-scale industrial projects in the near future that will help diversify the structure of its economy, including programs aimed at wide-scope development of technology application and high-technology use. One of the immediate projects ready for launch is the opening of the industrial complex in Sainshand city. Our ambition is to develop this project into an industrial complex serving the needs of not only Mongolia but North-East Asia generally, including the supply of processed goods to industrial production markets in China, Korea, and Japan. This should

encourage mutually beneficial cooperation with these and other developed countries.

This project includes the creation of a coking coal factory, metallurgical plant, coal handling and preparation plant, copper processing plant, constructions materials factory, oil refinery, a reliable infrastructure and engineering system, and social programs to support the smooth operations of these plants. For instance, building the coking coal plant will be fine-tuned in time and operations with the opening of the Tavan Tolgoi- Sainshand railroad line, and that of oil refinery with the opening of the Tavan Tolgoi-Choibalsan railroad line. This will facilitate uninterrupted transport, export, and distribution of products and goods.

I am confident that the Government's project aimed at supporting the use of advanced and high technology by building the Industrial Complex in Sainshand will increase Mongolia's economic competitiveness, boost our production of value-added end-products through the effective combination of technical and technological solutions, and ultimately speed the economic and social development of Mongolia – becoming in the process an important source of supply for the development needs of the entire region.

Since it is clear that financing numerous large-scale projects cannot rely on a single funding source, given the high risks associated with such reliance, we are planning to mobilize multiple funding sources in a stage-by-stage manner.

The Mongolian government sees private-public partnership as a preferred model in the financing the large investment projects. The government is working to improve and create legal and business environment for attracting private domestic and regional investors, financing joint projects through the recently created Development Bank, and issuing government bonds.

One recent example is the collaboration contract signed by Mongolian Stock Exchange and the London Stock Exchange. This enhances the long-term strategic goal of Mongolia by facilitating the entry of the Mongolian Stock Exchange to the international financial markets.