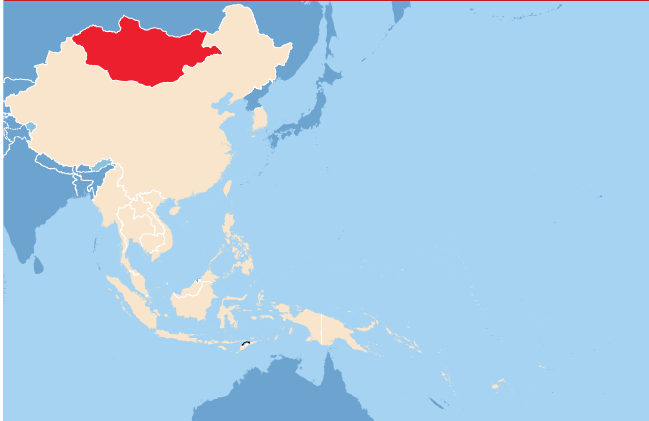


MONGOLIA



Population	2.8 million
Population growth	1.5 percent
GDP (PPP, int'l US\$)	15.0 billion
GDP per capita (PPP, int'l US\$)	5,374
Surface area	1,564,120 sq. km.
Capital	Ulaanbaatar

Source: World Development Indicators.

Summary

Mongolia's economy recorded another period of double-digit growth in 2013. The high economic growth was due to stronger mineral production led by the start of production in the Oyu Tolgoi mine and the government's stimulus policy. Expansionary fiscal policies created an additional off-budget deficit of 9 to 10 percent of GDP on top of the official budget. Monetary policy turned accommodative in 2013, injecting fresh liquidity equivalent to 20 percent of GDP into commercial banks through policy lending programs. The high economic growth buoyed by a policy stimulus was accompanied by rising inflation and growing external imbalances. Inflation accelerated to 12.5 percent at end-2013, while the current account deficit reached 28 percent of GDP. In light of the growing economic imbalances, the primary objective of economic management should be to restore macroeconomic stability, sustainable fiscal policy, and an adequate level of international reserves. Continuous efforts are needed to restore strong and stable foreign capital inflow.

Recent Economic Developments

Mongolia's economy recorded another period of double-digit growth of 11.7 percent in 2013, led by stronger copper and gold production. The economy grew 12.3 percent in the fourth quarter of the year, a slight pickup from 11.9 percent in the third quarter. Accelerating growth in mineral production—amidst the ramp-up of copper and gold production in Oyu Tolgoi (OT) mine—led the double-digit growth of the economy. Mineral GDP growth picked up to 33.8 percent in the second half of the year from 6.1 percent in the first half, registering 20.7 percent annual growth. Mineral GDP accounted for 18.5 percent of total economic output in 2013. Nonmineral GDP growth also remained double digit, buoyed by economic stimulus measures, driven by strong growth in construction (66.5 percent year-on-year) and wholesale and retail (17 percent year-on-year). The robust nonmineral growth was led by large off-budget public infrastructure spending through the Development Bank of Mongolia (equivalent to 9 to 10 percent of GDP) and subsidized lending programs by the Bank of Mongolia (equivalent to 20 percent of GDP).

Economic policies have been focused on growth stimulus through large off-budget spending and loose monetary policy. Fiscal policy remained highly expansionary in 2013 due to continued off-budget spending through the Development Bank of Mongolia (DBM). The structural budget deficit was kept under the 2 percent ceiling of the Fiscal Stability Law. However, a large portion of capital expenditure—which was carried out through the DBM—remained outside the official budget, which is estimated to be around 9 to 10 percent of GDP. Monetary policy also turned accommodative in 2013, through large subsidized lending programs of the central bank. The central bank continued its policy lending programs including the Price Stabilization Program and low-interest-rate mortgage lending, injecting 3.4 billion Tog into commercial banks over the year. Outstanding central bank lending to commercial banks reached 24 percent of GDP at end-2013.

National headline inflation has been accelerating since July, reaching 12.5 percent (year-on-year) in December 2013 and 12.3 percent in January 2014. The price level has been under mounting pressure from expansionary economic policies throughout the year as the central bank implemented aggressive monetary easing programs to spur economic growth. Core inflation—which largely reflects demand-side pressure—increased to 12.7 percent in December 2013 from 7.7 percent in June, the highest level over the last two years.

The annual current account deficit in 2013 was US\$3.2 billion—equivalent to 28 percent of GDP—following the deficit of US\$3.4 billion in 2012. The large current account deficit continued over the last three years as mineral export growth stagnated, while the adjustment of imports was limited due to continuous policy stimulus and slow adjustment of the real exchange rate. Total exports declined by 2.6 percent from a year ago, due to a 41 percent drop in coal exports. As the foreign capital inflow dropped in 2013, the large current account deficit posed a significant challenge to the economy due to a widening gap in the balance of payments. The net foreign capital inflow (US\$1.5 billion) in 2013 slowed considerably from the previous year (over US\$4.9 billion), reflecting a drop in FDI of nearly 50 percent from US\$4.4 billion to US\$2.3 billion.

The large financing gap in the balance of payments has led to a continuous decline in international reserve levels and a sliding exchange rate throughout the year.

The gross international reserves of the central bank fell over 47 percent during the year to US\$2.2 billion in December 2013, from its peak of US\$4.1 billion a year ago. The local currency depreciated 24 percent since July 2013 through February 2014. The slide in local currency value was also fed by loose monetary policy and weak confidence in the local currency amidst the diminishing foreign capital inflow.

Outlook and Emerging Challenges

In 2014, economic policies are likely to repeat the expansionary path of the last year in light of continued political emphasis on double-digit economic growth.

Off-budget spending through the DBM will remain the main financing vehicle for many infrastructure projects, bypassing the control of the Fiscal Stability Law. It would likely create an additional budget deficit of 7 to 8 percent of GDP on top of the official budget. Monetary policy will also likely remain loose, including the Price Stabilization Program and the politically popular housing mortgage program.

Continued economic stimulus relying on external borrowing and liquidity injection will likely add to economic imbalances.

Underlying inflationary pressure is high since the rising cost of imported goods has been only partially reflected in retail prices due to the price control of the central bank. The international reserve level and exchange rate will likely remain under continued pressure from the large gap between the current and financial/capital accounts. The objective of economic management at the current stage should be to ensure a stable and sustainable

growth path, minimizing the possibility of boom-bust cycles and addressing the balance-of-payments situation. The immediate policy priority is to counter rising balance-of-payments pressure and inflation through regaining foreign capital inflow and tighter economic management.

Mongolia: Key Economic Indicators

	2012	2013e	2014f	2015f	2016f
	Year	Year	Year	Year	Year
Output, Employment, and Prices					
Real GDP (% change yoy)	12.4	11.7	11.4	9.2	7.6
Mineral GDP (% yoy)	8.0	20.7	32.4	13.8	1.1
Consumer price index (% change yoy) 1/	14.2	12.3	12.5	9.9	8.0
Public Sector					
Government revenues (% GDP)	35.5	33.8	31.9	31.7	32.4
Government expenditures (% GDP)	46.7	44.7	41.0	37.1	35.6
Government balance (% GDP)	-11.1	-10.9	-9.1	-5.4	-3.2
Total public sector debt (% GDP)	62.7	58.7			
Foreign Trade, BOP, and External Debt					
Trade balance (millions US\$)	-2,354	-2,082	-1,122	-819	-768
Exports of goods (millions US\$)	4,384	4,273	5,366	6,150	6,758
(% change yoy)	-9.0	-2.6	25.6	14.6	9.9
Imports of goods (millions US\$)	6,738	6,355	6,488	6,969	7,526
(% change yoy)	2.1	-5.7	2.1	7.4	8.0
Current account balance (millions US\$)	-3,362	-3,155	-2,435	-2,270	-2,087
(% GDP)	-32.8	-27.5	-20.8	-16.9	-13.7
Foreign direct investment (millions US\$)	4,407	2,342			
Foreign exchange reserves, gross (millions US\$)	4,126	2,242			
(month of imports of g&s)	6.4	3.5			
Financial Markets					
Domestic credit (% change yoy)	-7.5	146.0			
Reserve money (% change yoy)	30.5	54.0			
Short-term interest rate (% p.a.) 2/	13.3	10.5			
Exchange rate (Tugrik/US\$, eop)	1,392	1,674			
Real effective exchange rate (2000=100)	140.0	136.5			
(% change yoy)	5.1	-2.5			
Stock market index (Dec. 2000=100) 3/	17,714	16,736			
Memo: Nominal GDP (millions US\$)	10,067	11,471	11,725	13,398	15,277

Sources: Bank of Mongolia; National Statistical Office; Ministry of Finance; IMF; World Bank staff estimates.

e = estimate.

f = forecast.

1/ Ulaanbaatar.

2/ Base policy rate.

3/ Top-20 index.