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Mongolia: 2008 Article IV Consultation—Staff Report; Staff Supplement; Public Information Notice on the Executive Board Discussion

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2008 Article IV consultation with Mongolia, the following documents have been released and are included in this package:

- The staff report for the 2008 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on March 11, 2008, with the officials of Mongolia on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on May 6, 2008. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- A staff supplement on the joint IMF/World Bank debt sustainability analysis.
- A Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its June 4, 2008 discussion of the staff report that concluded the Article IV consultation.

The document listed below has been or will be separately released.

Selected Issues Paper and Statistical Appendix

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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MONGOLIA

Staff Report for the 2008 Article IV Consultation

Prepared by the Staff Representatives for the 2008 Consultation with Mongolia

Approved by Steven Dunaway and Michael Hadjimichael

May 6, 2008

- The 2008 Article IV consultation discussions were held in Ulaanbaatar during February 27–March 11. The staff team comprised Messrs. Kronenberg (Head), Feridhanusetyawan, S. Lee, J. Kang (all APD), and Kim (FAD), and was assisted by Mr. Jang (Resident Representative). Mr. O’Brien (FSAP Mission Chief, MCM) and Mr. Yoon (OED) also participated in some of the discussions. The staff team closely liaised with overlapping MCM and FAD technical assistance (TA) missions.
- The 2006 Article IV consultation was concluded on January 10, 2007, and the PIN and Board documents have been published (<http://www.imf.org/external/pubs/cat/longres.cfm?sk=20334.0>).
- The joint IMF-World Bank Financial Sector Assessment Program (FSAP) missions took place in Ulaanbaatar in May and September 2007.
- Mongolia accepted the obligations under Article VIII, Sections 2, 3, and 4 on February 1, 1996, and has maintained an exchange system that is free of restrictions on the making of payments and transfers for current international transactions.
- Mongolia’s statistical framework is generally adequate for surveillance. However, further improvements are needed, especially on national accounts and government finance statistics.
- The authorities are expected to approve the publication of the Staff Report and all accompanying documents, as in the previous consultation.

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EXECUTIVE SUMMARY

Background

- **Mongolia's economy has performed very well in recent years.** Aided by the sustained run-up in copper and gold prices, real GDP growth has averaged 9 percent over the past four years, and per capita income has more than doubled. The external position also remains comfortable, with gross international reserves reaching a record level of US\$1 billion (4½ months of nonmining imports) and the net present value (NPV) of external public debt declining to 24½ percent of GDP at end-2007.
- **Inflation has increased sharply from 6 percent (y/y) in June 2007 to 21 percent in March 2008, posing a risk to macroeconomic stability.** The rise in inflation has been spurred by rapid growth in government spending (particularly for wages and transfer payments), credit to the private sector, and import prices. Transportation bottlenecks and other capacity constraints have added to the price pressures.
- **Although the budget recorded significant surpluses over the past three years, fiscal policy has become increasingly expansionary as government spending has accelerated.** The overall surplus narrowed from 8 percent of GDP in 2006 to 2 percent in 2007, and the 2008 budget projects a deficit of 2½ percent.
- **Monetary conditions have added to inflationary pressures.** Broad money increased by 57 percent in 2007, while domestic credit expanded by 67 percent.

Key Issues and Policy Discussion

- **Both fiscal and monetary policies need to be tightened to contain inflation.** The authorities should aim at achieving a modest budget surplus in 2008 by avoiding further wage increases, consolidating welfare programs, and eliminating low priority capital projects. Monetary policy should aim at containing the growth of reserve money to 12 percent in 2008.
- **The real exchange rate is currently somewhat undervalued.** Greater exchange rate flexibility is crucial to help lower inflation and maintain external stability.
- **The authorities should move cautiously in tapping nonconcessional sources of external financing.** Nonconcessional borrowing should be considered only for projects with clear economic viability that cannot be financed from concessional sources, and only when inflation is under control.
- **Transparent, stable, and internationally competitive fiscal and investments regimes need to be put in place in the mining sector to take full advantage of Mongolia's vast mineral wealth.**

I. BACKGROUND AND RECENT ECONOMIC DEVELOPMENTS

1. **Mongolia's economy has performed very well in recent years.** Aided by a sharp run-up in the international prices of copper and gold, real GDP growth has averaged 9 percent since 2004, while per capita income has more than doubled. Although the upturn in performance was initially driven by developments in the mining sector, growth has spread over time to other sectors, including construction, financial services, and other private sector activities. High minerals prices and improvements in tax administration have generated rapid growth in government revenues, and the budget recorded significant surpluses over the past three years.
2. **Growth picked up to 10 percent in 2007, while signs of overheating became increasingly apparent in the second half of the year.** Inflation rose from 6 percent (y/y) in June 2007 to 21 percent in March 2008. The inflationary pressures reflected a relaxation of monetary and fiscal policies, large increases in import prices for food and fuel, and transportation capacity constraints (Box 1).
3. **Monetary aggregates have been growing rapidly.** Reserve money grew by 39½ percent in 2007, driven by a large increase in net foreign assets of the Bank of Mongolia (BOM). With strong domestic demand and a cut in the reserve requirement, broad money increased by 57 percent (y/y) at end-2007, while credit to the private sector increased by 75 percent.
4. **The overall fiscal surplus declined from 8 percent of GDP in 2006 to 2 percent in 2007, as spending increased by 10 percentage points of GDP.** The growth in spending reflected a proliferation of overlapping and virtually universal social welfare programs (the child money program, newly-wed benefits, and a newborn child allowance), a 49 percent increase in the civil service wage bill, and more than a doubling of capital spending.
5. **Budget revenues also increased relative to GDP, although not as rapidly as expenditure.** In particular, minerals revenues rose from an average of 2½ percent of GDP in 2001–05 to 10½ percent in 2006 and 14½ percent in 2007, reflecting the increase in copper and gold prices and the impact of the Windfall Profits Tax (WPT) on these products that was introduced in June 2006.¹ With improvements in tax administration and compliance, nonmining revenues remained at 26 percent of GDP in 2007, virtually unchanged from 2006 despite significant cuts in the VAT, personal income tax, and corporate income tax rates at the beginning of 2007.²

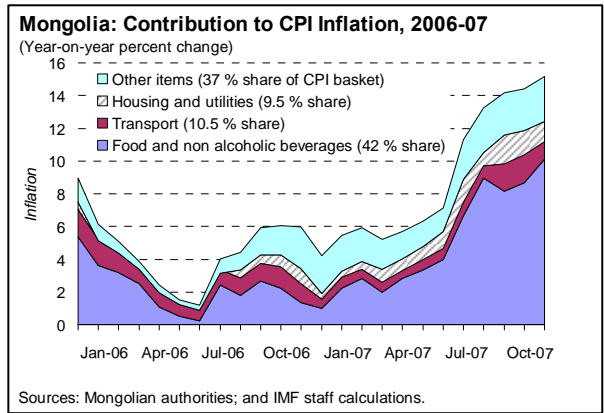
¹ A WPT of 68 percent was introduced on copper revenue from prices exceeding the sum of a base price (\$2,600 per ton) and smelting costs, and gold revenues from prices exceeding \$500 per ounce.

² The 2007 tax reform package included reductions of 5 percentage points in both the VAT and corporate income tax rates and unification of the personal income tax at a 10 percent rate.

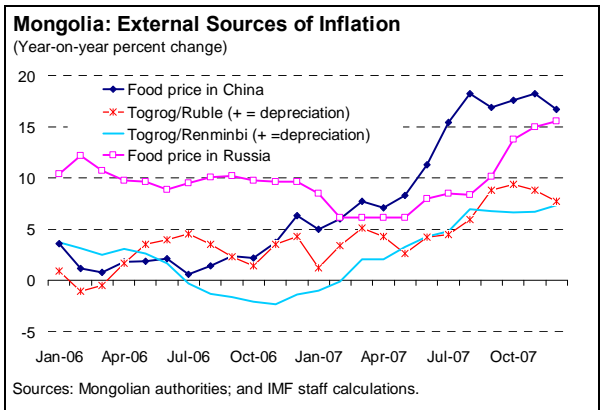
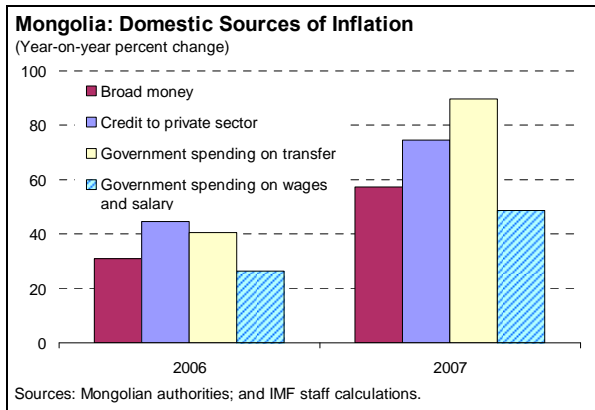
Box 1. Mongolia: The Sources of Rising Inflation

CPI inflation increased rapidly in the second half of 2007, rising from 6 percent (y/y) in June to 15 percent in December.

In terms of contributions, food prices accounted for two third of inflation, with prices of bread and meat products rising by 38 percent and 20 percent, respectively, at end-2007, contributing to nearly half of inflation. Prices of utilities, transport, education, services, as well as housing rents also increased at double-digit rates.



Several factors have contributed to the rise in inflation. Rapid growth in government transfer payments (90 percent in 2007) and the wage bill (49 percent) stimulated domestic demand, as did rapid growth in broad money (57 percent) and credit to the private sector (75 percent). On the supply side, the pick up in inflation reflected rising prices of food and fuel products in China and Russia (Mongolia’s largest trading partners) and the depreciation of the togrog against the Chinese renminbi (7 percent in 2007) and Russian ruble (8 percent). In addition, capacity constraints due to transportation bottlenecks put additional upward pressure on prices.



6. **With domestic demand accelerating, the external current account surplus narrowed from 7 percent of GDP in 2006 to 2½ percent in 2007.** Imports increased very rapidly, reflecting the run-up in food and fuel import prices and large imports of capital equipment for the mining sector, while export growth slowed as copper prices and export volumes reached a plateau. However, the overall balance of payments position remained comfortable, as imports of capital goods were largely financed by foreign direct investment in the mining sector.
7. **The nominal effective exchange rate (NEER) depreciated by 4 percent in 2007.** While the bilateral exchange rate with the U.S. dollar has been largely flat since mid-2006, the togrog depreciated by 7 percent vis-à-vis the Chinese renminbi and 8 percent vis-à-vis the Russian ruble in 2007. However, the real effective exchange rate (REER) appreciated by 6 percent in 2007, reflecting the pick up in inflation relative to trading partners.
8. **The strong economic performance of recent years has helped reduce Mongolia’s vulnerability to severe shocks, such as large swings in the terms of trade and periodic episodes of drought and devastating cold.** The net present value (NPV) of external public debt was cut from 51 percent of GDP at end-2004 to 24½ percent at end-2007, while international reserves of the Bank of Mongolia (BOM) have increased almost fivefold since 2003 to US\$1 billion (4½ months of nonmining imports).³ External debt is almost entirely concessional, and the debt service burden is low.
9. **The authorities have made progress in implementing recommendations made by Directors in the 2006 Article IV consultation, particularly with respect to establishing a sustainable debt position, strengthening central bank governance, and improving financial sector soundness.** However, further progress is needed to contain the growth in government spending and ensure greater exchange rate flexibility, which are important to help reduce inflation.

II. POLICY DISCUSSIONS

A. Medium-Term Outlook and Main Policy Challenges

10. **Mongolia’s medium-term economic outlook is favorable.** High minerals prices have spurred minerals exploration and re-energized plans to exploit very large untapped deposits of copper, gold, coal, uranium, and other minerals. With the expected opening of the new Oyu Tolgoi copper and gold mine in 2011, the staff’s baseline scenario envisages that real GDP growth will pick up from around 7–9 percent in 2008–10 to 12–14 percent in 2011–12. Other large mining projects, including the development of huge coal deposits near China, are on the drawing boards but not yet incorporated in the baseline scenario, giving

³ Nonmining imports of goods and services are approximated by total imports minus foreign direct investment.

significant further upside potential to the outlook. With strong policy implementation, it should be possible to bring inflation down to a single digit by end-2008 and to maintain a rate of 5–6 percent over the medium term. The external current account is expected to move into deficit during 2008–11, reflecting expected declines in copper prices and large FDI-financed imports of capital equipment for the mining sector, but it is projected to move back into surplus in 2012, after the Oyu Tolgoi mine comes on stream. The NPV of public debt, the debt service burden, and international reserves are expected to remain at comfortable levels.

11. **However, the mission team and authorities agreed that major policy challenges need to be addressed if Mongolia is to fully exploit this potential.** In the near term, rapidly rising inflation poses the biggest risk to sustainable growth, and both fiscal and monetary policies need to be tightened to maintain macroeconomic stability. The approach of parliamentary elections in June 2008 could add to the political difficulty of this task. Looking ahead, it will be crucial to put in place a medium-term fiscal framework that can contribute to the maintenance of low inflation and fiscal sustainability, without sharp disruptive swings in government spending. To take full advantage of Mongolia's vast mineral wealth, it will be equally important to have transparent, stable, and internationally competitive fiscal and investment regimes. Continued progress in strengthening the financial sector will also be critical for sustained growth.

B. Fiscal Policy

12. **The budget calls for the overall balance to swing from a surplus of 2 percent of GDP in 2007 to a deficit of 2½ percent of GDP in 2008.** Despite a cut in the employer social security contribution rate, revenues are budgeted to reach a record 44½ percent of GDP, reflecting

continued high minerals prices, ongoing improvements in tax administration, and continued strong growth. However, spending is expected to increase even more rapidly to a record

Mongolia: Consolidated Budget Nominal Growth					
	2005	2006	2007	2008	
				budget	recom.
	(Annual percentage growth)				
Total Revenue and Grants	17.5	62.4	36.1	30.9	25.6
Current revenue	17.9	62.6	36.2	30.5	25.2
Total Expenditure and Net Lending	1.6	38.6	65.3	46.2	28.0
Current expenditure	11.4	34.1	49.4	45.8	36.6
Wages and salaries	13.0	26.5	48.8	91.4	74.0
Transfers	23.9	40.4	89.8	35.1	27.0
Capital expenditure	-23.1	55.0	115.8	46.9	9.1

Sources: Ministry of Finance; and Fund staff estimates and projections.

47 percent of GDP. The growth in spending would be associated with large nominal increases in the wage bill, social welfare spending, and capital expenditure, following earlier large increases in each of those categories in 2007. In March 2008, a tax amnesty program was put into effect, which provides an opportunity for taxpayers to correct their tax information without penalty.

13. **The mission team argued that the fiscal stimulus in the 2008 budget risked further aggravating inflation.** To prevent higher inflationary expectations from getting entrenched, the mission recommended maintaining a surplus of about 1½ percent of GDP in 2008. Such a target could be achieved, even with the civil service wage increases granted at the beginning of the year, by (i) strictly avoiding any further increases in civil service employment and wages during the remainder of the year; (ii) reducing overlapping social spending and improving its targeting; and (iii) curtailing low priority capital spending. The mission also advised the authorities to avoid recourse to fiscal measures to control inflation.⁴ Investment spending should be prioritized to ensure there is adequate room for investment in human capital and basic infrastructure to help avoid the emergence of “Dutch Disease” as the mining sector grows.

14. **The authorities shared the staff’s concerns about the potential impact of fiscal policy on inflation.** Although the scope for maneuver is limited in the run-up to elections, the government decided to cancel plans already underway for further spending increases in an amended budget. In addition, line ministries had been instructed in recent weeks to identify cuts in their purchases of goods and services that could be implemented in the second half of this year. On price stabilization measures, the authorities terminated subsidies for petroleum importing companies after the small budget allocation (0.2 percent of GDP) was spent. The temporary VAT and customs duty exemptions on wheat and flour imports have also been lifted, and an agreement was recently reached with Russia that will ensure wheat supplies at a stable price.

15. **Parliament has authorized the government to issue commercial foreign debt of up to US\$1.2 billion (25 percent of GDP).** The mission stressed that borrowing and spending on this order of magnitude could further aggravate inflationary pressures and, as indicated in the Debt Sustainability Analysis (DSA), cause Mongolia’s debt burden indicators to breach their indicative thresholds in the medium term (see Supplement on DSA). The mission and the authorities agreed that Mongolia should continue to rely primarily on concessional borrowing in the near term, while recognizing that Mongolia’s infrastructure investment needs were very large and that the country’s eligibility for concessional lending facilities would likely taper off in the coming years as per capita income continues to rise. The authorities also indicated that capacity needs to be strengthened and a comprehensive risk management framework needs to be put in place. Any foreign financing should be fully consolidated with the general budget to ensure fiscal

⁴ Measures for price stabilization include a temporary exemption of VAT (10 percent) and customs duties (5 percent) on wheat and flour imports, building up of wheat and flour reserves, and subsidies to reduce interest expenses of petroleum importing companies.

transparency. The mission encouraged the authorities to continue the negotiations of overdue obligations with bilateral creditors.⁵

16. **The staff encouraged the authorities to strengthen the macro-fiscal framework to help cope with the inherent volatility and uncertainty of a large mining sector.** The government's current practice essentially targets a constant overall budget balance in percent of GDP over the medium term, which can lead to highly procyclical spending. The mission suggested that the authorities aim at reducing the nonmineral deficit (overall balance minus mining taxes, dividends, and royalties) from 12½ percent of GDP in 2007 to 8 percent of GDP by 2010 and thereafter. This fiscal target would ensure intertemporal smoothing of spending and result in a gradual further reduction in the NPV of public debt to 18 percent of GDP over the medium term (see Supplement on DSA). In addition, the authorities should consider setting a separate overall limit on the growth of spending or the expenditure-to-GDP ratio, reflecting the absorption capacity of the economy, to avoid overheating pressures. This rule would provide an additional anchor to ensure macroeconomic stability when total spending supported by the nonmineral balance targeting exceeds the economy's absorption capacity. The mission stressed that the tax amnesty granted in early 2008 could adversely affect incentives for future tax compliance, and it advised the authorities to strengthen tax enforcement to help achieve the intended goal of tax base broadening.

17. **The authorities agreed that fiscal policy rules should be refined over time to ensure macroeconomic stability and fiscal sustainability, although the formal adoption of these rules would be difficult in the near term.** The authorities agreed about the need for transparent, stable, and internationally competitive fiscal and investment regimes for the mining sector. On the issue of state equity participation in the mining sector, they stressed that public opinion was strongly in favor of greater state ownership, but they believed that increased state equity in large strategic deposits could be acquired gradually over time.

C. Monetary and Exchange Rate Policies

18. **The authorities and mission team agreed that the growth in monetary aggregates should be slowed to help bring inflation down.** Toward this end, the mission recommended that growth in reserve money should be slowed to about 12 percent in 2008, which should be consistent with bringing inflation down to about 9 percent by end-2008 and 5–6 percent thereafter. Given the fiscal target suggested by the mission, this would require an increase in the volume of central bank bills (CBBs) equal to about ½ percentage point of GDP during the year. Towards this end, the BOM raised the policy interest rate on seven-day bills to 9.75 percent in March 2008, bringing the cumulative increase since July

⁵ Negotiations to settle overdue obligations with bilateral creditors (Bulgaria, China, Finland, Romania, and Russia) are underway.

2007 to 335 basis points, and reserve money growth slowed sharply in the first three months of the year. Should inflation not show clear signs of declining in the near future, the mission argued that further increase in the policy interest rate would be appropriate. To help contain liquidity expansion, the mission advised to put a hold on plans to transfer deposits of the Social Security system from the BOM to commercial banks.

19. **With the level of international reserves now broadly comfortable, the mission argued that a further large increase in international reserves was not needed and could, indeed, complicate the task of reducing inflation.** A flexible exchange rate policy would, therefore, be an important component of a tightening of monetary policy. In line with the recommendations of a concurrent TA mission by Monetary and Capital Markets Department, the team recommended that the BOM widen its bid-offer spread, reduce the scope of transactions taking place at the BOM's reference rate, and require that a share of mining taxes by the largest copper mine be paid in local currency.

20. **The authorities argued that Mongolia already had a floating exchange rate regime.** They explained that the situation in 2006-07 was atypical because some large mining companies had decided to pay some of their sharply increased tax liabilities in foreign currency. In terms of its operations in the foreign exchange market, the BOM had been a significant net seller of international reserves. However, the authorities agreed that, particularly with the structural changes that were taking place in the economy, there was a need to strengthen the interbank foreign exchange market. Towards this end, they were giving consideration to limiting the payment of taxes in dollars. They also noted that a screen-based foreign exchange trading system is under development by the BOM and the commercial banks, which should facilitate development of market.

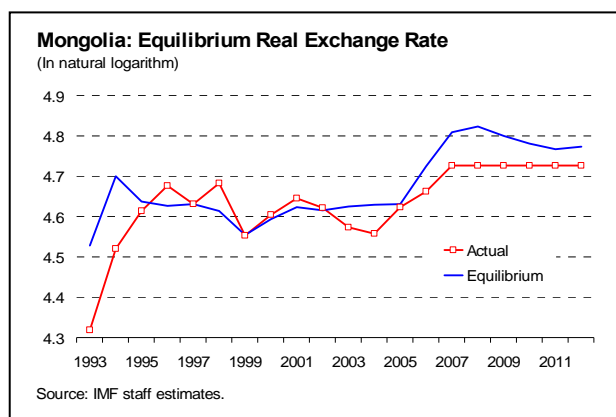
21. **The staff's assessment indicates that the real effective exchange rate may currently be somewhat undervalued.** In this connection, the mission reiterated the importance of exchange rate flexibility to facilitate the maintenance of external stability (Box 2).

D. Preserving Financial Sector Soundness

22. **The recent joint IMF/World Bank Financial Sector Assessment Program (FSAP) found that the BOM's framework for bank supervision is generally well developed and that the BOM is aware of the risks faced by some individual banks.** The banking system's risk-weighted capital adequacy, return on assets, and return on equity were all at comfortable levels in 2007, and the share of nonperforming loans in gross loans has been cut from 5.6 percent at end-2005 to 3.2 percent at end-2007. Nevertheless, the authorities recognized that measures of loan quality could be distorted in the current environment of rapid credit growth and said they would be vigilant in this regard. A few small banks, which did not pose a systemic risk, were considered more vulnerable and remained under an enhanced supervisory regime. The FSAP team advised the BOM to

Box 2. Assessment of Mongolia's External Stability

Staff estimates using the reduced-form equilibrium real exchange rate approach of the CGER indicate that the togrog is currently somewhat undervalued. The estimated vector error correction model based on 1992–2007 data shows that the coefficients of all fundamentals have the expected signs and are statistically significant.¹ The results suggest that the togrog may be somewhat undervalued in relation to the medium term level of its fundamental determinants. These results are consistent with the depreciations of the togrog's bilateral exchange rates against the Russian ruble (12 percent) and the Chinese renminbi (6 percent) over the past two years, while the bilateral exchange rate with the U.S. dollar has been largely flat for most of the period since June 2006. The rapid increase of international reserves for last two years, from US\$333 million at end-2005 to US\$1 billion at end-2007 is also consistent with these results.



While the current account is expected to be subject to significant fluctuations over the medium term, this reflects the time profile of large mining projects and is not expected to result in external instability. The current account balance is projected to swing from a surplus of 2½ percent of GDP in 2007 to a deficit of 9–13 percent of GDP in 2008–10, reflecting large-scale imports of capital equipment for new mining projects financed by foreign direct investment. When the mine subsequently comes on stream, the current account would be expected to revert to a large surplus. Despite these swings in the current account, however, international reserves would remain comfortable and stable in terms of months of next year nonmining imports.

Under these circumstances, the exchange rate should not be expected to eliminate fluctuations in the current account. Therefore, it would be inappropriate to draw conclusions about the equilibrium exchange rate from the external sustainability approach, which implicitly makes such an assumption. Likewise, the macroeconomic balance approach, in which the estimated current account norm would be largely unaffected by the mining projects, could provide misleading results in the Mongolian case. The large structural changes underway highlight the importance of a flexible exchange rate regime both to promote macroeconomic stability and to support long-term structural adjustment to a growing mining sector.

¹ The fundamentals are: 1) previous year's net foreign asset (scaled by the sum of exports and imports); 2) productivity differential between the tradable and nontradable sectors, relative to trading partners; 3) commodity terms of trade; and 4) government consumption, measured as purchase of goods and services plus government wages relative to GDP. Increases in values of these fundamentals imply real exchange rate appreciation.

closely monitor the suitability of bank shareholders and managements in light of the recent changes at some banks.

23. **The supervision of nonbank financial institutions is at an earlier stage, but progress is being made.** The Financial Regulatory Commission (FRC), established in 2006, has been working to relicense savings and credits cooperatives (SCCs), insurance companies, and other nonbanking financial institutions. With that process under way, the mission advised the authorities to provide no further bailouts to SCCs. Significant steps have been taken to strengthen the framework for Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT), including the establishment of a Financial Intelligence Unit in the BOM. Remaining gaps, particularly with respect to the reporting of suspicious transaction by banks and the capacity constraints in law enforcement, still need to be addressed. The mission encouraged the authorities to proceed cautiously with proposals to establish a development bank to avoid the risk of political interference. The operations of the Mongolian Mortgage Corporation should remain narrowly focused so that they do not impede the development of private sector housing finance.

24. **The BOM has made important strides in strengthening its own risk management and governance structures by strategically managing and controlling exposure to financial and operational risks.** These efforts include the creation of an investment committee in the BOM as well as a risk management unit responsible for identifying and managing the BOM's financial and policy risks. Since September 2007, the risk management unit calculates the Value-at-Risk of its portfolio on a daily basis to monitor market risks. Foreign reserves are divided into short-term and long-term portfolios to manage liquidity risk, and the State Foreign Exchange Reserve Management Regulation, revised in January, requires that counterparties are rated "AA-" or higher. By order of the Governor, the BOM has discontinued dealing in gold and currency options for commercial purposes, and all outstanding positions were closed upon expiration.

E. Other Issues

25. **The recent Review of Standards and Codes conducted by the IMF's Statistics Department found that Mongolia meets most of the recommendations of the General Data Dissemination Standards.** However, the scope and coverage of the national accounts and government statistics need further improvement and the authorities need to broaden the dissemination of macroeconomic data to the public. The staff welcomed Mongolia's participation in the Extractive Industry Transparency Initiative, and encouraged the authorities to make progress in publishing government's and companies' reports and completing the audit of government revenues from extractive industries.

III. STAFF APPRAISAL

26. **Mongolia's economic performance in recent years has been impressive.** GDP growth has averaged more than 9 percent per annum since 2004, and per capita income has more than doubled. The budget has recorded three consecutive years of surplus, the public debt burden has been cut sharply, the external current account is in surplus, and international reserves have reached record levels.
27. **Medium-term prospects are favorable, as high minerals prices have spurred exploration and re-energized plans to exploit large untapped deposits of copper, gold, and other minerals.** However, major challenges need to be addressed for Mongolia to fully exploit this potential. Inflation has risen sharply over the past year and is now posing a threat to macroeconomic stability. In addition, delays have been experienced in finalizing some new investment agreements in the mining sector. In this environment, policies should focus on reducing inflation, keeping fiscal policy on a sustainable track, establishing a transparent, stable, and internationally competitive mining regime, and continuing to strengthen the financial sector.
28. **Fiscal policy should be promptly tightened to contain inflationary pressures.** The staff welcomes the authorities' decision not to proceed with plans for substantial additional spending in an amended budget. Nevertheless, given the continued high level of copper and gold prices, the authorities should aim at maintaining a modest fiscal surplus in 2008, instead of the 2½ percent of GDP deficit that is budgeted. This could be achieved by containing the wage bill, curtailing low priority capital spending, and taking initial steps to reduce the overlapping coverage and improve the targeting of social welfare programs. Consolidation and improved targeting of welfare programs could facilitate the protection of the vulnerable groups from the impact of food price hikes.
29. **Mongolia's medium-term fiscal framework should help the authorities cope with the uncertainty and volatility of a large mining sector.** Taking a conservative view of the timetable for bringing large new mining projects on stream, the staff recommends that the authorities reduce the nonmineral deficit from 12½ percent of GDP in 2007 to about 8 percent of GDP over the medium term, with a separate limit on the growth in nominal expenditure or the expenditure-to-GDP ratio. To maintain macroeconomic stability and debt sustainability, the authorities should be cautious about tapping nonconcessional sources of external finance. Such borrowing should be considered only for projects with clear economic viability that cannot be financed from concessional sources, and only when inflation is under control.
30. **Monetary policy should also be directed at reducing inflation.** The staff welcomes the BOM's recent decision to raise the yield on CBBs and encourages the BOM to consider a moderate further increase in order to reduce the possible need for a more abrupt tightening in the future. The real exchange rate is currently somewhat undervalued,

and greater exchange rate flexibility would facilitate the tightening of monetary policy and enhance the economy's resilience to external shocks. Toward this end, the BOM should reduce the use of the reference rate for its transactions with market participants and foster the development of an interbank foreign exchange market.

31. **The staff welcomes the progress made by the BOM to strengthen its risk management and governance structures.** Looking forward, the BOM should continue to strengthen the management of international reserves, particularly the gold reserves, reduce its role in domestic gold market, and improve the transparency of its operations.

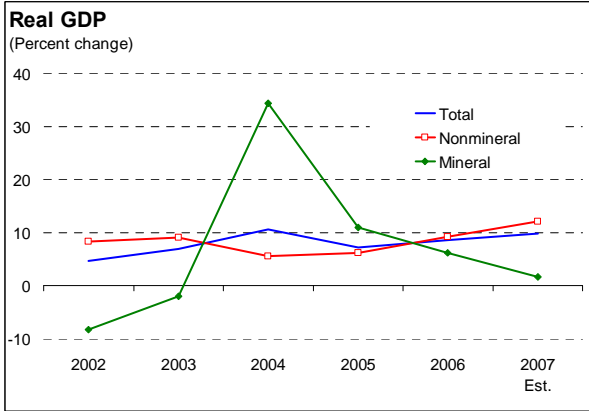
32. **The BOM's framework for banking supervision is generally well developed, and the condition for the banking system as a whole is generally comfortable.** In addition, the FRC has made progress in the supervision of nonbank financial institutions, by conducting offsite examinations of the savings and credit cooperatives, requiring their relicensing, and closing insolvent institutions. However, the rapid growth in banking system credit and the rollover of loans could make it difficult for the BOM to spot emerging problems in the banking system. Going forward, the authorities should continue to upgrade the supervisory framework by monitoring large exposures and improving the supervision of liquidity and operational risks of banks, enacting draft laws to support the supervision of nonbank financial institutions, and continuing to develop tools for consolidated supervision. If the authorities proceed with plans to introduce a deposit insurance system, payments into the system should reflect the condition of individual banks, and the system should not be extended to any nonbank financial institutions.

33. **The staff welcomes the authorities' efforts to improve data quality for surveillance and encourages the authorities to make further progress in completing the GFSM 2001 pilot study and reconciling the discrepancies between fiscal and monetary data on domestic financing.** Considering the increasing role of private capital flows in the economy, the staff encourages the authorities to monitor the size and nature of private capital flows, while maintaining an open capital account regime.

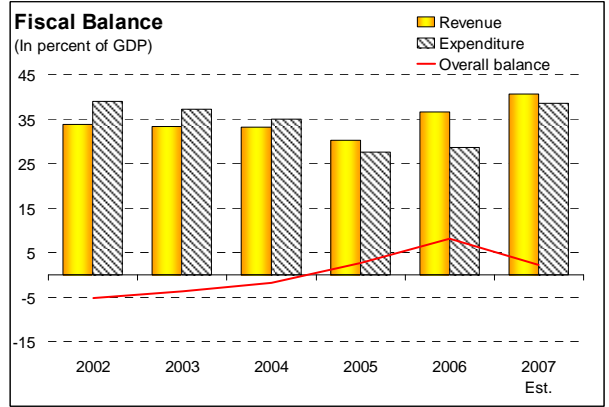
34. The staff recommends that the next Article IV consultation with Mongolia take place on the standard 12-month cycle.

Figure 1. Mongolia: Economic Developments, 2002–07

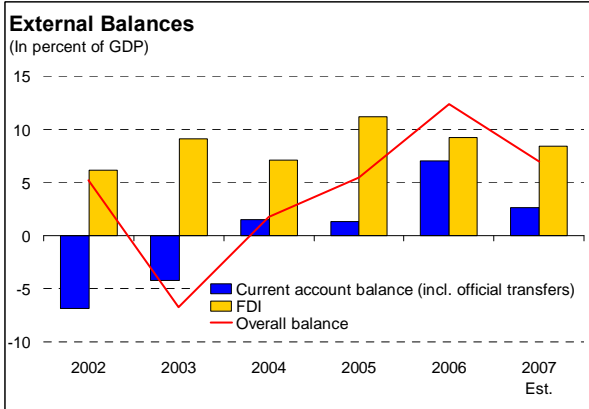
Economic growth has remained strong; Large mining sector expansion created spillover effects on other sectors.



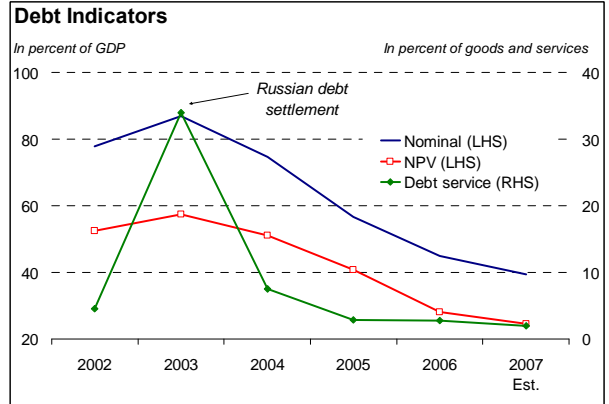
The budget recorded its third consecutive surplus in 2007.



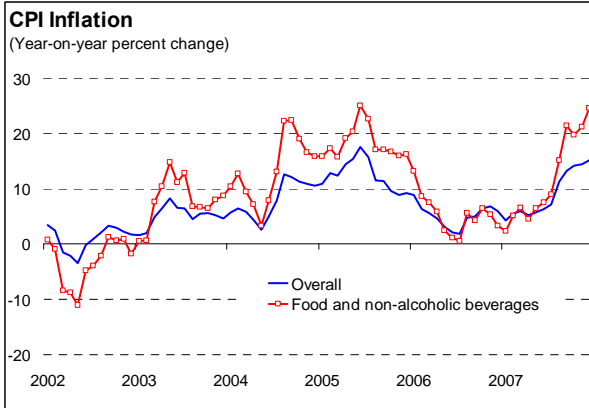
Current account surplus declined in 2007, but the overall balance and FDI remained strong.



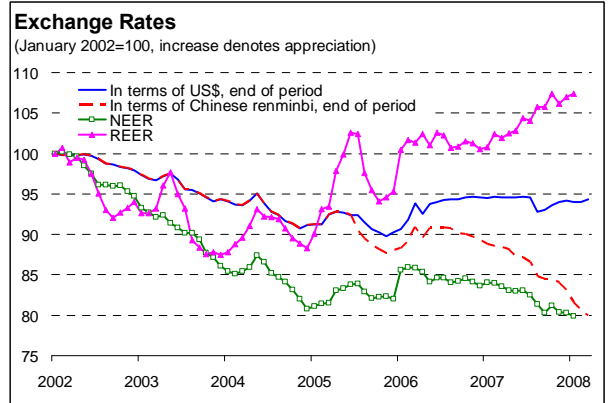
External public debt ratios have declined sharply and are now below the debt-burden threshold.



However, rapid increase in inflation suggests that the economy is overheating and ...



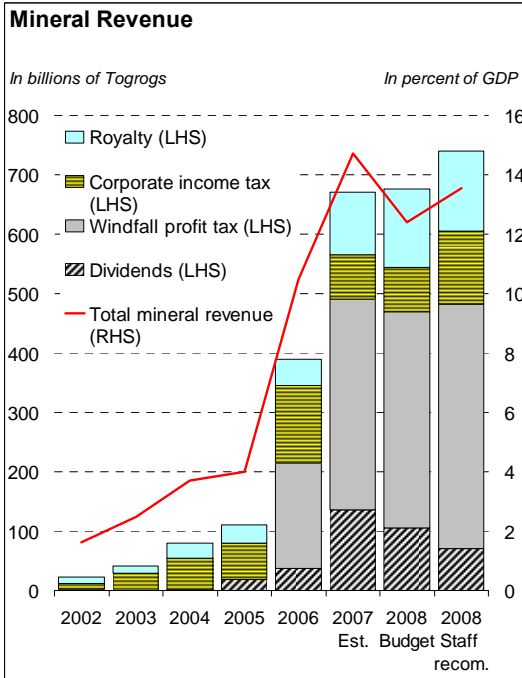
... contributes to rising real exchange rate, while the nominal rate has been stable in terms of US\$ since 2006.



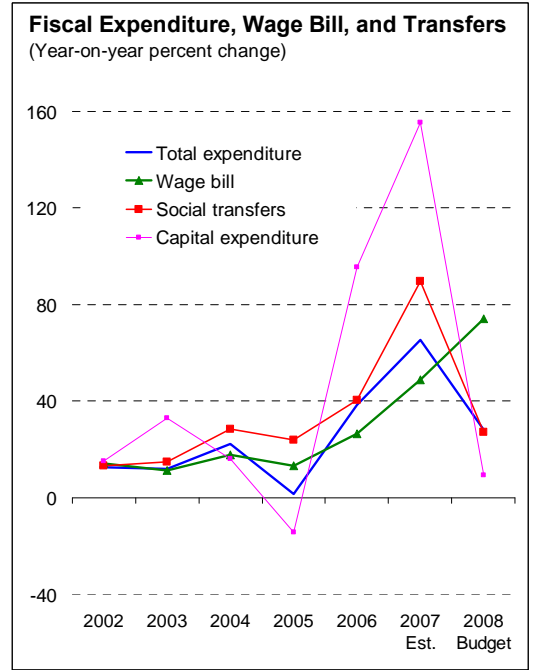
Sources: Mongolian authorities; IMF, Information Notice System, *International Financial Statistics*, and Fund staff estimates.

Figure 2. Mongolia: Fiscal Indicators, 2002–08

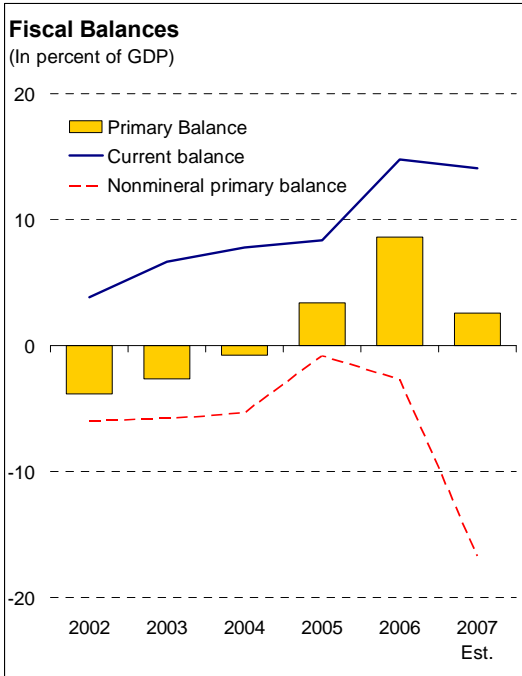
The mining sector has been contributing to rapid growth of budget revenue and ...



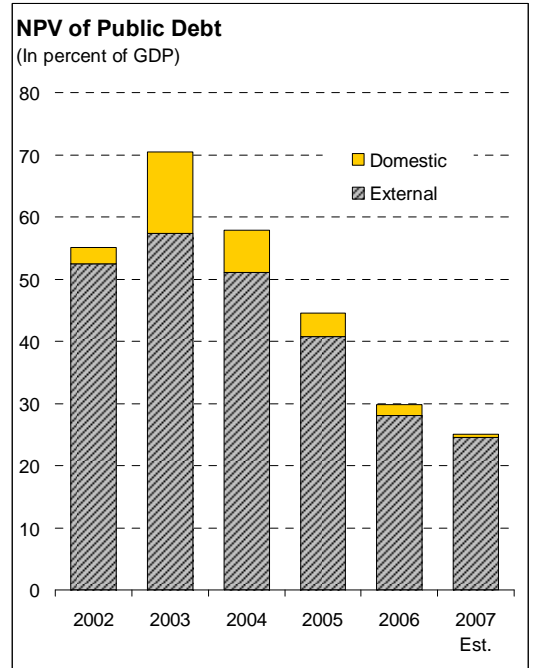
...financing large increases in wage bill, transfer payments, and capital expenditure.



Improvement in current and primary balances mirrors deterioration in non mineral balance.



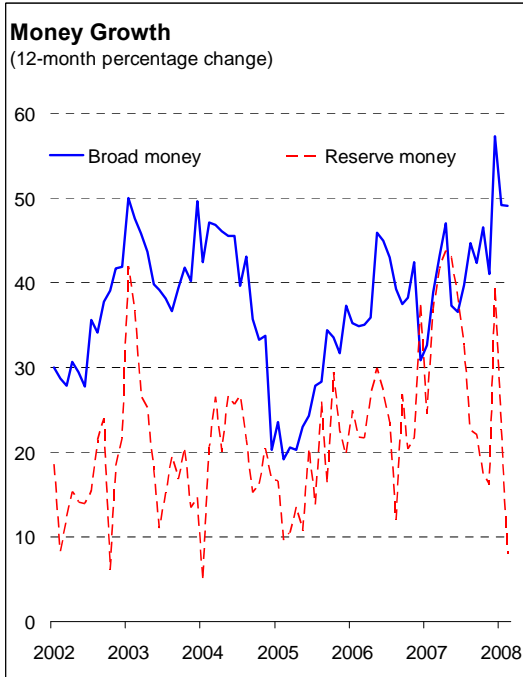
Meanwhile, total public debt has declined remarkably since 2003.



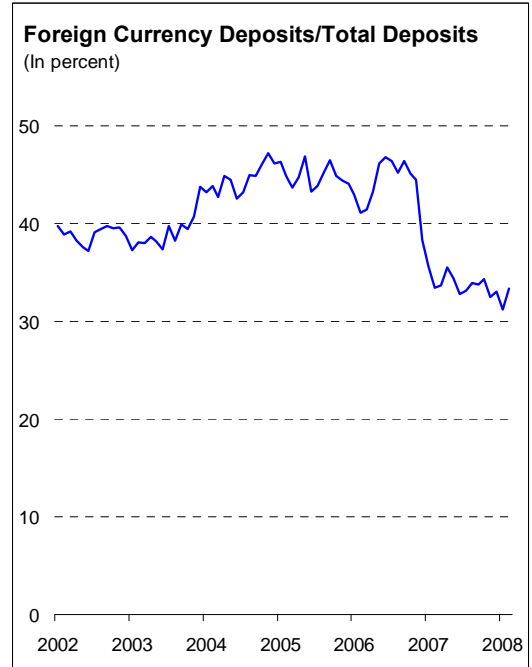
Sources: Mongolian authorities; and Fund staff estimates and projections.

Figure 3. Mongolia: Monetary Developments, 2002–08

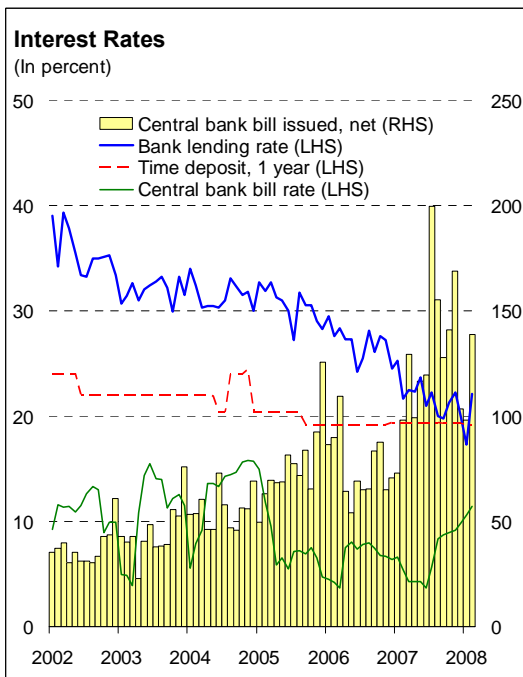
Broad money grew very rapidly, while reserve money remained volatile.



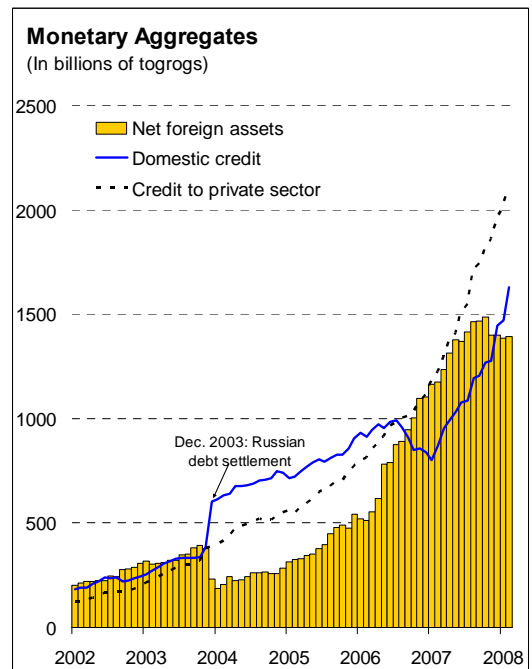
Foreign currency deposit has declined, reflecting stronger confidence in domestic currency.



Interest rate spreads have narrowed...



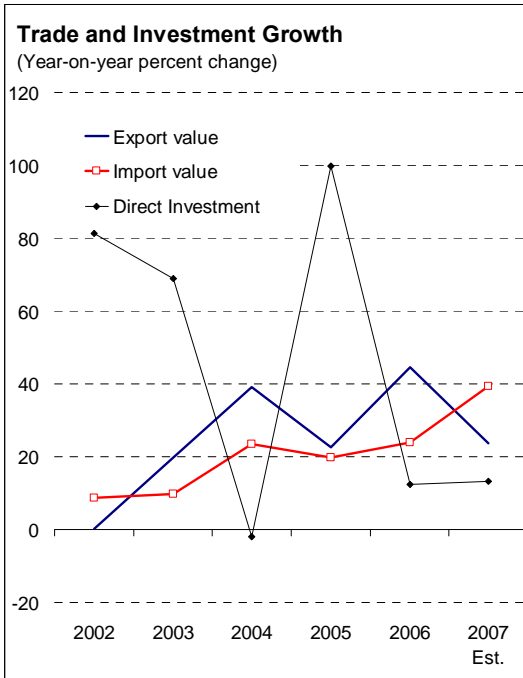
...and credit to private sector has accelerated.



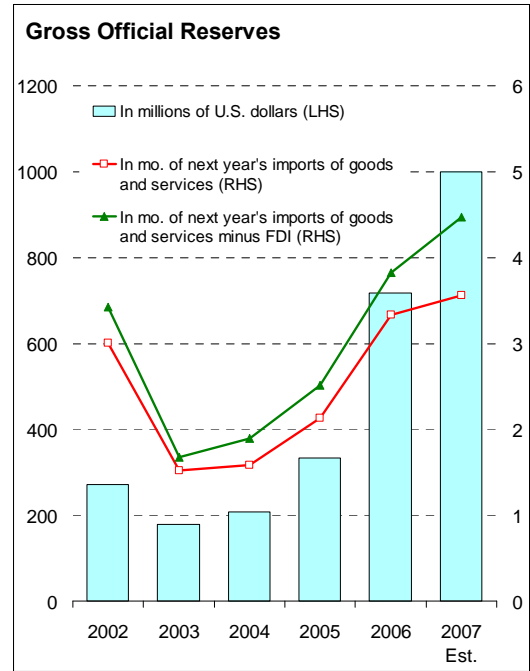
Sources: Mongolian authorities; and Fund staff estimates.

Figure 4. Mongolia: External Developments, 2002-07

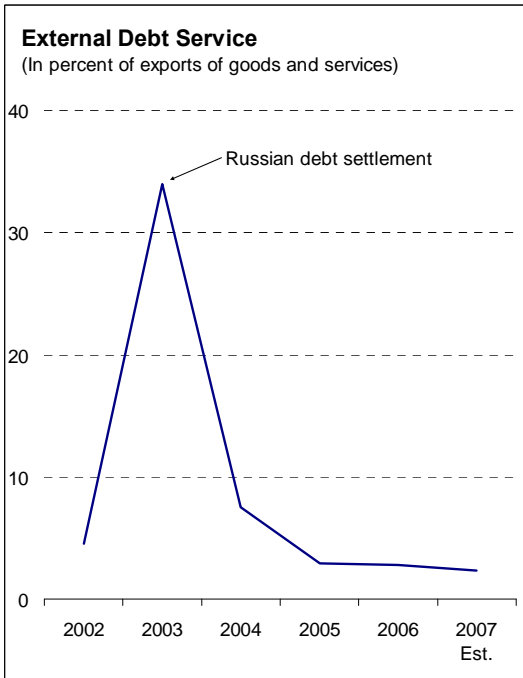
Export, import, and FDI have grown rapidly.



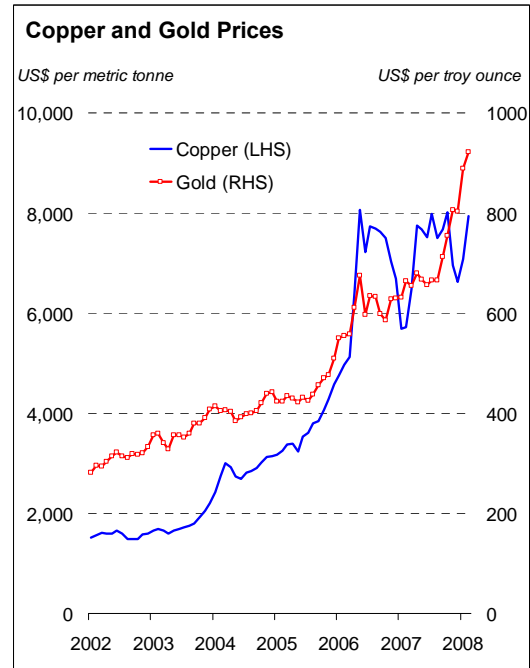
Gross international reserves rose to record levels.



Since the settlement of Russian debt, the debt service has remained low.



Copper and gold prices remained exceptionally high.



Sources: Mongolian authorities; and IMF, *International Financial Statistics*, Commodity Price System, and staff estimates.

Table 1. Mongolia: Selected Economic and Financial Indicators, 2004–08

Nominal GDP (2007): \$3,894 million 1/
 Population, end-year (2007): 2.64 million
 Per capita GDP (2007): \$1,489 1/
 Poverty incidence (2006): 32.2 percent 2/
 Quota: SDR 51.1 million

	2004	2005	2006	2007 Est.	2008	
					Budget	Staff Recom.3/
	(Percent change)					
Real sector						
Real GDP growth	10.6	7.3	8.6	9.9	...	8.6
Mineral	34.3	10.9	6.3	1.7	...	1.4
Nonmineral	5.6	6.3	9.2	12.2	...	10.3
Consumer prices (period average)	7.9	12.5	5.1	9.0	...	12.0
Consumer prices (end-period)	10.6	9.2	6.0	15.1	...	8.8
GDP deflator	17.2	20.4	23.1	11.6	...	10.3
	(In percent of GDP)					
General government budget						
Revenue and grants	33.1	30.1	36.6	40.6	44.4	42.6
Expenditure and net lending	35.0	27.5	28.5	38.4	46.9	41.1
Current balance	7.8	8.4	14.8	14.1	12.0	12.2
Primary balance	-0.8	3.4	8.6	2.6	-2.1	1.9
Overall balance (including grants)	-1.8	2.6	8.1	2.2	-2.5	1.5
Nonmineral overall balance	-5.5	-1.4	-2.4	-12.5	-14.9	-12.0
Net domestic bank credit to government	-2.5	-5.9	-11.8	-4.2	-0.9	-3.2
	(Percent change)					
Money and credit						
Net foreign assets	22.0	92.4	103.3	26.7	...	18.1
Net domestic assets	19.5	9.6	-33.0	139.1	...	29.7
Domestic credit	23.0	22.3	-7.5	72.5	...	25.2
<i>Of which: claims on nonbanks</i>	43.7	40.1	41.1	67.2	...	25.4
Broad money	20.3	37.3	30.8	57.3	...	22.9
Reserve money	16.8	19.7	37.7	39.6	...	12.0
Broad money velocity (GDP/BM) 4/	2.5	2.5	2.4	2.0	...	1.9
Interest rate on central bank bills, end-period (percent) 5/	15.8	3.7	5.1	8.4	...	...
	(In millions of U.S. dollars; unless otherwise indicated)					
Balance of payments						
Current account balance (including official transfers)	27	29	222	101	...	-405
(In percent of GDP)	1.5	1.3	7.0	2.6	...	-8.5
Trade balance	-149	-155	30	-218	...	-839
(In percent of GDP)	-8.2	-6.7	0.9	-5.6	...	-17.6
Exports, f.o.b.	872	1,069	1,545	1,952	...	2,163
(Percent change)	39.0	22.5	44.6	26.3	...	10.8
Imports, c.i.f.	1,021	1,224	1,516	2,170	...	3,002
(Percent change)	23.5	19.8	23.9	43.2	...	38.4
Foreign direct investment	129	258	290	328	...	688
Gross official international reserves (end-period)	208	333	718	1,001	...	1,253
(In months of next year's imports of goods and services)	1.6	2.1	3.3	3.6	...	4.0
(In months of next year's nonmining imports) 6/	1.9	2.5	3.8	4.5	...	5.1
Trade prices						
Export prices (U.S. dollar, percent change)	23.1	13.1	38.7	30.5	...	4.0
Import prices (U.S. dollar, percent change)	15.3	9.2	12.2	9.5	...	15.2
Terms of trade (percent change)	6.8	3.5	23.7	19.2	...	-9.7
	(In millions of U.S. dollars; unless otherwise indicated)					
Public and publicly guaranteed debt						
Total public debt (In percent of GDP)	81.4	60.3	46.7	40.0	35.7	34.1
Domestic debt (In percent of GDP)	6.8	3.7	1.7	0.6	0.3	0.3
External debt 7/	1,352	1,306	1,420	1,535	1,687	1,611
(In percent of GDP)	74.6	56.6	45.0	39.4	35.4	33.8
(In percent of total public debt)	91.6	93.8	96.4	98.5	99.2	99.2
NPV of total public debt (In percent of GDP) 8/	57.9	44.5	29.8	25.1	22.6	21.6
NPV of external debt (In percent of GDP) 8/	51.1	40.8	28.1	24.5	...	21.3
(In percent of exports of goods and services)	76.6	63.4	43.6	37.8	...	36.4
External debt service	91	43	57	52	...	61
(In percent of exports of goods and services)	7.5	2.9	2.8	2.0	...	2.1
Exchange rate						
Togrogs per U.S. dollar (end-period)	1,209	1,221	1,165	1,170	...	...
Togrogs per U.S. dollar (period average)	1,187	1,205	1,177	1,170	...	...
Nominal effective exchange rate (end-period; percent change)	-6.1	1.5	1.9	-4.0	...	...
Real effective exchange rate (end-period; percent change)	0.9	8.0	5.5	6.4	...	...
Nominal GDP (billion togrogs)	2,152	2,780	3,715	4,558	...	5,456
Nominal GDP (million U.S. dollars) 1/	1,814	2,307	3,156	3,894	...	4,759

Sources: Data provided by the Mongolian authorities; and Fund staff estimates and projections.

1/ Based on period average exchange rate.

2/ Share of households below national poverty line, based on The Millennium Development Goals Implementation 2007.

3/ Fund staff projections based on policy recommendation.

4/ Seasonally adjusted figures for broad money velocity.

5/ Yield of 14-day bills until 2006 and of 7-day bills for 2007.

6/ Nonmining imports of goods and services are approximated by total imports minus foreign direct investment.

7/ Includes IMF loans, guarantees, and arrears.

8/ Based on 5 percent discount rate from 2004 onwards.

Table 2. Mongolia: Summary Operations of the General Government, 2004–08

	2004	2005	2006	2007		2008	
				Amended Budget	Est.	Budget	Staff Recom.
(In billions of togrogs)							
Total revenue and grants	713.1	837.9	1,360.4	1,699.3	1,851.2	2,423.2	2,325.0
Total expenditure and net lending	752.5	764.6	1,059.5	1,847.1	1,751.6	2,560.1	2,242.0
Overall balance (incl. grants)	-39.4	73.3	300.9	-147.7	99.6	-136.9	83.0
Nonmineral overall balance	-119.2	-37.9	-88.3	-764.5	-571.7	-813.4	-656.4
Financing	39.4	-73.3	-336.4	147.7	-99.6	136.9	-83.0
Foreign (net)	77.4	89.9	87.1	78.2	79.9	169.6	93.3
Domestic (net)	-38.0	-163.2	-423.5	69.5	-179.5	-32.7	-176.4
(In percent of GDP)							
Total revenue and grants	33.1	30.1	36.6	37.3	40.6	44.4	42.6
Current revenue	32.8	30.0	36.4	37.2	40.5	44.1	42.3
Mineral revenue	3.7	4.0	10.5	13.5	14.7	12.4	13.6
Nonmineral revenue	29.1	26.0	26.0	23.6	25.7	31.7	28.8
Tax revenue and social security contributions	27.1	24.9	30.4	29.6	32.9	38.1	36.8
Income taxes	6.7	6.4	12.8	12.6	14.2	14.8	15.9
Enterprise income tax	4.6	4.3	6.0	5.1	4.8	6.6	6.7
Personal income tax	2.1	2.1	2.1	1.5	1.6	1.6	1.6
"Windfall" tax	0.0	0.0	4.8	5.9	7.8	6.7	7.5
Social security contributions	3.8	3.4	3.0	3.1	3.5	4.4	3.6
Sales tax and VAT	7.6	6.5	6.5	5.0	5.8	8.3	6.6
Excise taxes	3.3	2.8	2.7	2.4	2.9	3.1	3.2
Customs duties and export taxes	2.1	2.0	1.9	2.1	2.2	3.1	2.8
Other taxes	3.7	3.6	3.4	4.4	4.3	4.5	4.6
Nontax revenue	5.7	5.1	6.1	7.6	7.5	6.0	5.5
Capital revenue and grants	0.3	0.2	0.2	0.1	0.2	0.3	0.3
Total expenditure and net lending	35.0	27.5	28.5	40.5	38.4	46.9	41.1
Current expenditure	25.0	21.6	21.7	27.0	26.4	32.1	30.1
Wages and salaries	6.4	5.6	5.3	6.7	6.4	10.3	9.3
Purchase of goods and services	10.1	8.3	8.6	8.2	8.4	8.8	8.5
Subsidies to public enterprises	0.5	0.3	0.3	0.3	0.3	0.4	0.4
Transfers	6.9	6.6	7.0	11.1	10.8	12.2	11.5
Interest payments	1.1	0.7	0.5	0.5	0.4	0.4	0.4
Contingency allocation	...	0.0	0.0	0.0	0.0	0.0	0.0
Capital expenditure and net lending	9.9	5.9	6.9	13.6	12.1	14.8	11.0
Capital expenditure	4.9	3.2	4.7	11.3	9.8	12.6	9.0
Domestically-financed	3.8	2.9	4.5	10.5	9.5	11.5	8.2
Foreign-financed	1.0	0.4	0.2	0.8	0.4	1.2	0.8
Net lending	5.1	2.7	2.1	2.2	2.2	2.2	2.0
On-lent foreign project loans	4.9	3.2	2.4	2.0	1.4	3.0	2.0
Domestic lending minus repayments	0.1	-0.5	-0.3	0.0	0.8	-0.8	0.0
Current balance (excl. privatization receipts)	7.8	8.4	14.8	10.2	14.1	12.0	12.2
Primary balance	-0.8	3.4	8.6	-2.7	2.6	-2.1	1.9
Overall balance (incl. grants)	-1.8	2.6	8.1	-3.2	2.2	-2.5	1.5
Nonmineral overall balance	-5.5	-1.4	-2.4	-16.8	-12.5	-14.9	-12.0
Discrepancy between deficit from above and below the line	0.0	0.0	-1.0	0.0	0.0	0.0	0.0
Financing	1.8	-2.6	-9.1	3.2	-2.2	2.5	-1.5
Foreign (net)	3.6	3.2	2.3	3.5	1.8	3.1	1.7
External borrowing (net)	3.0	3.0	2.3	1.0	1.8	3.0	1.7
Disbursements	4.3	4.0	3.0	2.1	1.8	4.1	2.5
Amortization	1.3	0.9	0.6	1.1	0.0	1.1	0.8
External arrears	0.6	0.2	0.0	0.0	0.0	0.0	0.0
Domestic (net)	-1.8	-5.9	-11.4	1.5	-3.9	-0.6	-3.2
Banking system (net)	-2.5	-5.9	-11.8	0.8	-4.2	-0.9	-3.2
Nonbank	0.7	0.0	0.4	0.7	0.2	0.3	0.0
Privatization receipts	0.8	0.2	0.4	0.7	0.4	0.3	0.2
Other nonbank (net)	0.0	-0.2	0.0	0.0	-0.1	0.0	-0.2
Memorandum items:							
Mineral revenue/total revenue and grants (in percent)	11.2	13.3	28.6	32.2	36.3	27.9	31.8
Total public debt (incl. IMF)/GDP	81.4	60.3	46.7	41.0	40.0	35.7	34.1
Foreign debt (incl. IMF)/GDP	74.6	56.6	45.0	40.4	39.4	35.4	33.8
Domestic debt/GDP	6.8	3.7	1.7	0.6	0.6	0.3	0.3
Governments deposits	4.5	5.3	14.5	10.0	15.0	13.1	15.4
Net public debt	76.9	55.1	32.2	31.0	25.0	22.6	18.7
NPV of total public debt	57.9	44.5	29.8	25.7	25.1	22.6	21.6
Nominal GDP (in billions togrogs)	2,152	2,780	3,715	4,558	4,558	5,456	5,456
Copper price per ton	2,863	3,676	6,731	7,132	7,132	6,800	7,000

Sources: Ministry of Finance; and Fund staff estimates and projections.

Table 3. Mongolia: Monetary Aggregates, 2004–08

	2004	2005	2006				2007				2008	
	Dec.	Dec.	Mar.	Jun.	Sept.	Dec.	Mar.	Jun.	Sept.	Dec.	Dec. Auth. 1/	Dec. Staff recom.
(In billions of togrog; end of period)												
Monetary survey												
Broad Money	846	1,162	1,205	1,463	1,528	1,520	1,725	1,998	2,175	2,391	...	2,939
Currency	144	152	145	198	189	185	216	262	267	283	...	342
Deposits	703	1,009	1,061	1,265	1,339	1,335	1,509	1,736	1,908	2,108	...	2,597
Net foreign assets 2/	283	544	555	791	946	1,106	1,237	1,369	1,465	1,401	...	1,655
Net international reserves	294	551	564	782	944	1,118	1,249	1,387	1,479	1,414	...	1,668
Bank of Mongolia	198	364	411	449	596	801	994	1,136	1,241	1,141	...	1,442
Commercial banks	96	187	153	333	347	317	256	250	238	273	...	226
Other foreign assets, net	-11	-7	-9	10	3	-12	-12	-17	-14	-13	...	-13
Net domestic assets	564	618	650	672	582	414	489	629	710	991	...	1,284
Domestic credit	740	904	946	983	910	837	953	1,080	1,204	1,444	...	1,808
Net credit to government	94	-1	-50	-121	-267	-440	-510	-587	-732	-691	...	-868
Claims on nonbanks	646	905	996	1,103	1,177	1,277	1,463	1,667	1,935	2,135	...	2,676
<i>Of which:</i>												
Claims on public enterprises	13	34	29	30	33	36	36	23	22	26	...	26
Claims on the private sector	552	776	858	966	1,011	1,122	1,298	1,511	1,743	1,957	...	2,519
Nonperforming loans	39	49	54	60	68	60	61	62	69	68	...	85
Other items, net	-176	-286	-296	-311	-328	-423	-464	-451	-494	-453	...	-523
Monetary authorities												
Reserve money	235	281	308	376	377	387	436	520	460	540	673	605
Net foreign assets 2/	199	372	415	469	610	801	994	1,136	1,241	1,141	1,642	1,442
Net international reserves	198	364	411	449	596	801	994	1,136	1,241	1,141	1,642	1,442
Other assets, net	1	8	4	20	14	0	0	0	0	0	0	0
Net domestic assets	36	-91	-107	-93	-234	-414	-557	-616	-782	-600	-969	-836
Net credit to government	106	52	-2	-72	-190	-333	-431	-510	-637	-571	-621	-748
Claims on deposit money banks	22	18	18	18	18	18	22	20	22	19	19	19
Minus: Central bank bills (net)	69	126	110	69	84	71	129	120	128	103	407	147
Other items, net	-23	-35	-13	30	22	-28	-19	-6	-38	55	40	40
<i>Of which: precious metals</i>	6	10	11	51	43	11	26	26	45	133	...	...
Memorandum items:												
(In percent; except otherwise indicated)												
Annual broad money growth	20.3	37.3	35.1	45.0	37.4	30.8	43.1	36.6	42.4	57.3	...	22.9
Annual growth of credit to nonbanks 3/	43.7	40.1	46.0	45.7	43.3	41.1	46.9	51.1	64.5	67.2	...	25.4
Annual reserve money growth	16.8	19.7	21.7	27.2	26.8	37.7	41.7	38.4	22.1	39.6	24.5	12.0
Velocity, seasonally adjusted	2.5	2.5	3.0	2.4	2.3	2.4	2.6	2.3	2.1	2.0	...	1.9
Broad money/Reserve money	3.6	4.1	3.9	3.9	4.1	3.9	4.0	3.8	4.7	4.4	...	4.9
Nonperforming loans/total loans (percent)	6.1	5.5	5.5	5.5	5.7	4.7	4.2	3.7	3.6	3.2	...	...
Excess reserves (billions of togrogs)	3.0	15.3	58.0	18.4	24.3	26.0	49.9	83.2	14.0	23.2	...	...

Sources: Data provided by the Mongolian authorities; and Fund staff estimates and projections.

1/ Based on BOM's reserve money and NIR targets and 2008 budget.

2/ Valued at actual exchange rates and gold prices.

3/ Includes nonperforming loans.

Table 4. Mongolia: Balance of Payments, 2004–13

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
				Est.			Proj. 1/			
(In millions of US dollars; unless otherwise indicated)										
Current account balance (including official transfers)	27	29	222	101	-405	-645	-727	-59	400	60
Trade balance	-149	-155	30	-218	-839	-1,125	-1,244	-472	780	99
Exports, f.o.b.	872	1,069	1,545	1,952	2,163	2,237	2,403	2,824	4,425	3,917
Of which: Copper	284	326	635	812	836	789	769	892	1,296	1,354
Gold	240	331	270	235	340	384	415	749	1,890	1,287
Imports, c.i.f.	-1,021	-1,224	-1,516	-2,170	-3,002	-3,362	-3,646	-3,296	-3,645	-3,818
Of which: petroleum products	-210	-272	-423	-551	-804	-859	-909	-1,014	-1,150	-1,211
Services, net	-46	65	122	161	251	293	328	344	349	378
Receipts	338	414	486	574	623	675	733	795	863	936
Payments	-383	-350	-364	-413	-371	-383	-405	-451	-514	-558
Income, net 2/	-48	-106	-144	-79	-91	-105	-124	-253	-993	-663
Private transfers, net	146	134	77	84	91	98	106	113	119	125
Official transfers	87	88	112	133	162	174	186	186	123	97
Other grants	36	3	26	20	21	21	22	23	23	24
Financial and capital account	10	88	110	182	662	780	810	132	-218	19
Direct investment	129	258	290	328	688	823	941	442	663	507
Portfolio investment	-53	0	0	6	8	10	14	18	23	30
Loans	49	-14	37	139	367	370	318	154	-238	-204
Medium- and long-term, net	75	61	39	150	382	391	348	196	-179	-121
Disbursements	157	91	88	237	444	457	468	486	523	584
Public	129	90	88	82	120	124	129	131	135	139
Private	29	1	0	155	324	333	339	355	388	445
Amortization	-82	-31	-49	-86	-62	-66	-119	-290	-702	-706
Public	-18	-22	-38	-29	-39	-42	-44	-49	-49	-49
Private 2/	-64	-9	-11	-57	-23	-23	-75	-242	-652	-656
Short-term, net	-27	-75	-3	-11	-15	-22	-30	-42	-59	-83
Currency and deposits, net 2/	-120	-162	-244	-249	-293	-314	-327	-344	-454	-361
Trade credits, net	4	7	28	-13	-42	-59	-76	-84	-156	106
Other, net	0	0	0	-28	-66	-50	-59	-53	-55	-59
Errors and omissions	-5	8	57	6	0	0	0	0	0	0
Overall balance	32	125	389	289	257	136	83	74	182	79
Financing	-32	-125	-389	-289	-257	-136	-83	-74	-182	-79
Increase in net official reserves (-)	-37	-131	-389	-289	-257	-136	-83	-74	-182	-79
Use of IMF credit (+)	-7	-6	-4	-6	-5	-7	-5	-4	-3	-3
Increase in gross official reserves (-)	-30	-125	-385	-283	-252	-129	-78	-70	-179	-77
Arrears accumulation (+) / payments (-) (net) 3/	5	6	0	0	0	0	0	0	0	0
Exceptional financing / rescheduling	0	0	0	0	0	0	0	0	0	0
Memorandum items:										
Current account balance (in percent of GDP)										
Excluding official transfers	-3.3	-2.5	3.5	-0.8	-11.9	-15.3	-16.0	-3.8	3.8	-0.5
Including official transfers	1.5	1.3	7.0	2.6	-8.5	-12.1	-12.8	-0.9	5.5	0.8
Export volume (annual growth)	0.0	8.3	4.3	-3.2	6.5	11.4	15.4	33.5	60.0	-11.5
Import volume (annual growth)	6.9	8.8	10.5	31.5	23.2	12.1	8.2	-13.1	9.3	4.0
Export price index (annual change)	23.1	13.1	38.7	30.5	4.0	-7.2	-10.8	-8.1	-2.1	0.0
Import price index (annual change)	15.3	9.2	12.2	9.5	15.2	0.2	0.1	0.4	0.5	0.6
Trade balance (in percent of GDP)	-8.2	-6.7	0.9	-5.6	-17.6	-21.1	-21.9	-7.4	10.7	1.3
Gross official reserves (end-period)	208	333	718	1,001	1,253	1,382	1,460	1,530	1,709	1,786
(In months of next year's imports of goods and services)	1.6	2.1	3.3	3.6	4.0	4.1	4.7	4.4	4.7	4.6
(In months of next year's nonmining imports) 4/	1.9	2.5	3.8	4.5	5.1	5.3	5.3	5.3	5.3	5.3

Sources: Data provided by the Mongolian authorities; and Fund staff estimates and projections.

1/ Fund staff projections based on policy recommendations.

2/ Includes estimated payments and capital flows related to Oyu Tolgoi project.

3/ Arrears on post-1991 Russian debt. Excluding disputed amount with Finland.

4/ Nonmining imports of goods and services are approximated by total imports minus foreign direct investment.

Table 5. Mongolia: External Debt and Debt Service, 2004–13

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
				Est.			Proj. 1/			
(In millions of U.S. dollars; unless otherwise indicated)										
Nominal Debt Stock	1,395	1,340	1,444	1,657	1,951	2,251	2,507	2,609	2,740	2,925
IMF	44	35	31	25	20	13	9	5	3	0
Non-IMF	1,351	1,305	1,413	1,631	1,931	2,237	2,498	2,604	2,737	2,925
Existing debt	1,351	1,305	1,413	1,631	1,569	1,504	1,384	1,336	1,286	1,237
Public sector	1,309	1,271	1,390	1,510	1,471	1,429	1,384	1,336	1,286	1,237
Multilateral	791	771	853	923	907	889	870	850	827	804
Bilateral	505	487	537	587	564	539	514	486	459	433
Commercial	13	13	0	0	0	0	0	0	0	0
Private sector 2/	43	35	24	122	98	75	0	0	0	0
New borrowing	0	0	0	0	362	734	1,114	1,269	1,451	1,688
Public sector	0	0	0	0	120	244	373	504	639	778
Private sector 2/	0	0	0	0	242	489	741	764	812	910
Total Debt Service	155	52	68	109	92	119	194	380	388	397
IMF	8	6	4	6	5	7	5	4	3	3
Non-IMF	148	46	64	102	87	113	189	376	386	395
Existing debt	148	46	64	102	86	89	141	63	63	63
Amortization	132	31	49	86	62	66	119	49	49	49
Public sector	68	22	38	30	39	42	44	49	49	49
Multilateral	4	6	8	11	16	18	19	20	22	23
Bilateral	14	16	18	19	23	24	25	28	27	26
Commercial	50	0	13	0	0	0	0	0	0	0
Private sector 2/	64	9	11	57	23	23	75	0	0	0
Interest	16	15	14	16	24	23	22	15	14	13
Public sector	16	15	14	16	16	16	15	15	14	13
Multilateral	7	7	7	8	8	8	8	8	8	7
Bilateral	8	8	7	8	8	8	7	7	6	6
Commercial	1	0	0	0	0	0	0	0	0	0
Private sector 2/	0	0	0	0	8	7	7	0	0	0
New borrowing	0	0	0	0	1	24	48	313	323	332
Amortization	0	0	0	0	0	0	0	242	248	252
Interest	0	0	0	0	1	24	48	71	75	80
Memorandum items: 3/										
Total debt service in percent of exports	12.8	3.5	3.3	4.3	3.3	4.1	6.2	10.6	7.4	8.3
Of which: public and publicly guaranteed	7.5	2.9	2.8	2.0	2.1	2.3	2.2	2.1	1.5	1.6
Total debt stock in percent of GDP	76.9	58.1	45.8	42.5	41.0	42.1	44.0	40.7	37.4	37.5
Of which: public and publicly guaranteed	74.6	56.6	45.0	39.4	33.8	31.5	31.0	28.8	26.3	25.9
Net present value of debt										
In percent of exports of goods and services	80.2	65.8	44.8	42.6	48.6	56.2	59.9	54.5	39.6	46.9
Of which: public and publicly guaranteed	76.6	63.4	43.6	37.8	36.4	36.8	36.3	33.4	24.3	28.1
In percent of GDP	53.5	42.3	28.8	27.6	28.4	30.6	33.0	30.8	28.6	29.2
Of which: public and publicly guaranteed	51.1	40.8	28.1	24.5	21.3	20.1	20.0	18.9	17.5	17.5

Sources: Data provided by the Mongolian authorities; and IMF staff estimates and projections.

1/ Fund staff projections based on policy recommendations.

2/ Until 2006, the stock of private debt is derived based on data from the balance of payments.

3/ These figures are calculated in the debt sustainability analysis.

Table 6. Mongolia: Medium-Term Macroeconomic Framework, 2004–13

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
				Est.			Proj. 1/			
(In percent of GDP; unless otherwise indicated)										
Real sector										
Nominal GDP (in billions of togrogs)	2,152	2,780	3,715	4,558	5,456	6,123	6,766	7,886	9,328	10,261
Nominal GDP (in millions of U.S. dollars) 2/	1,814	2,307	3,156	3,894	4,759	5,344	5,690	6,405	7,316	7,787
Per capita GDP (in U.S. dollars) 2/	720	905	1,224	1,489	1,793	1,984	2,081	2,308	2,597	2,723
Real GDP (percent change)	10.6	7.3	8.6	9.9	8.6	8.0	7.2	12.2	13.7	5.3
Mineral real GDP	34.3	10.9	6.3	1.7	1.4	1.2	1.1	37.5	42.2	3.2
Nonmineral real GDP	5.6	6.3	9.2	12.2	10.3	9.6	8.5	7.2	6.6	6.0
GDP deflator (percent change)	17.2	20.4	23.1	11.6	10.3	3.9	3.1	3.9	4.0	4.5
Consumer prices (period average; percent change)	7.9	12.5	5.1	9.0	12.0	7.4	5.8	5.5	5.5	5.3
Consumer prices (end-period; percent change)	10.6	9.2	6.0	15.1	8.8	6.0	5.5	5.5	5.5	5.0
General government accounts										
Total revenue and grants	33.1	30.1	36.6	40.6	42.6	40.8	39.0	35.8	36.5	36.5
Mineral revenue	3.7	4.0	10.5	14.7	13.6	10.6	6.8	5.0	5.7	5.8
Nonmineral revenue	29.1	26.0	26.0	25.7	28.8	29.9	31.8	30.5	30.5	30.4
Capital revenue and grants	0.3	0.2	0.2	0.2	0.3	0.3	0.3	0.3	0.3	0.3
Total expenditure and net lending	35.0	27.5	28.5	38.4	41.1	40.2	40.1	38.8	38.8	38.7
Current expenditure	25.0	21.6	21.7	26.4	30.1	29.3	29.2	28.8	28.8	28.7
Wages and salaries	6.4	5.6	5.3	6.4	9.3	9.3	9.2	9.1	9.1	9.1
Goods and services	10.1	8.3	8.6	8.4	8.5	8.2	8.2	8.2	8.2	8.2
Interest payments	1.1	0.7	0.5	0.4	0.4	0.4	0.4	0.4	0.4	0.4
Other	7.5	6.9	7.3	11.1	11.9	11.5	11.4	11.1	11.1	11.0
Capital expenditure and net lending	9.9	5.9	6.9	12.1	11.0	10.9	10.9	10.0	10.0	10.0
Current balance	7.8	8.4	14.8	14.1	12.2	11.2	9.5	6.7	7.4	7.5
Overall balance (including grants)	-1.8	2.6	8.1	2.2	1.5	0.6	-1.1	-3.0	-2.3	-2.2
Nonmineral overall balance	-5.5	-1.4	-2.4	-12.5	-12.0	-9.9	-8.0	-8.0	-8.0	-8.0
Foreign financing (including gap financing)	3.6	3.2	2.3	1.8	1.7	1.5	1.5	1.3	1.2	1.1
Monetary sector										
Broad money (percent change)	20.3	37.3	30.8	57.3	22.9	23.3	22.1	21.4	19.5	17.0
Velocity (GDP/M2)	2.5	2.5	2.4	2.0	1.9	1.7	1.5	1.5	1.5	1.4
Balance of payments										
Exports (percent change)	39.0	22.5	44.6	26.3	10.8	3.4	7.4	17.5	56.7	-11.5
Imports (percent change)	23.5	19.8	23.9	43.2	38.4	12.0	8.5	-9.6	10.6	4.8
Current account balance (excluding official transfers)	-3.3	-2.5	3.5	-0.8	-11.9	-15.3	-16.0	-3.8	3.8	-0.5
Current account balance (including official transfers)	1.5	1.3	7.0	2.6	-8.5	-12.1	-12.8	-0.9	5.5	0.8
Gross official reserves										
(In millions of U.S. dollars)	208	333	718	1001	1253	1,382	1,460	1,530	1,709	1,786
(In months of next year's imports of goods and services)	1.6	2.1	3.3	3.6	4.0	4.1	4.7	4.4	4.7	4.6
Debt indicators										
Total public debt	81.4	60.3	46.7	40.0	34.1	31.8	31.3	29.1	26.6	26.1
Domestic debt	6.8	3.7	1.7	0.6	0.3	0.3	0.3	0.3	0.3	0.3
External debt	74.6	56.6	45.0	39.4	33.8	31.5	31.0	28.8	26.3	25.9
(in millions of U.S. dollars)	1,352	1,306	1,420	1,535	1,611	1,686	1,766	1,845	1,928	2,015
NPV of total public debt	57.9	44.5	29.8	25.1	21.6	20.3	20.3	19.1	17.8	17.8
Of which: external debt	51.1	40.8	28.1	24.5	21.3	20.1	20.0	18.9	17.5	17.5
Government deposits in the banking system	4.5	5.3	13.9	16.5	16.7	16.9	15.5	11.5	11.5	11.5
External public debt service 3/	7.5	2.9	2.8	2.0	2.1	2.3	2.2	2.1	1.5	1.6
Memorandum items										
Copper prices (US\$ per ton)	2,863	3,676	6,731	7,132	7,000	6,000	4,500	3,500	3,300	3,300
Gold prices (US\$ per ounce)	409	445	604	697	960	985	1,015	1,050	1,080	1,095

Sources: Data provided by the Mongolian authorities; and Fund staff estimates and projections.

1/ Fund staff projections based on policy recommendations.

2/ Based on period average exchange rate.

3/ In percent of exports of goods and services.

Table 7. Mongolia: Indicators for Vulnerability and Financial Soundness, 2004–07

	2004	2005	2006	2007
Key Economic and Market Indicators				
Real GDP growth (in percent)	10.6	7.3	8.6	9.9
CPI inflation (end-period; in percent)	10.6	9.2	6.0	15.1
Short-term interest rate (end-period; in percent) 1/	15.8	3.7	5.1	8.4
Exchange rate, Togrog/US\$ (end-period)	1,209	1,221	1,165	1,170
External Sector				
Exchange rate regime (end-period)	Floating	Floating	Pegged	Pegged
Current account balance (in percent of GDP) 2/	1.5	1.3	7.0	2.6
Direct investment (in percent of GDP)	7.1	11.2	9.2	8.4
Export growth (US\$ value, percent change)	39.0	22.5	44.6	26.3
Real effective exchange rate (end-period; 2000=100)	93.3	100.7	106.2	113.0
Gross international reserves (in US\$ million)	208	333	718	1,001
NPV of external debt (in percent of GDP)	53.5	42.3	28.8	27.6
General Government				
Overall balance (in percent of GDP)	-1.8	2.6	8.1	2.2
Primary balance (in percent of GDP)	-0.8	3.4	8.6	2.6
General government financing (in percent of GDP)				
Foreign (net)	3.6	3.2	2.3	1.8
Domestic (net)	-1.8	-5.9	-11.4	-3.9
Financial Sector (in percent)				
Capital adequacy ratio				
Tier I capital ratio	17.4	15.8	15.6	11.8
Total regulatory capital/risk-weighted assets	20.0	18.2	18.1	14.2
Total regulatory capital/total assets	15.6	13.6	13.6	11.2
Asset quality				
Foreign exchange loans/total loans	45.6	47.0	46.7	33.2
NPLs/total loans	6.0	5.6	4.7	3.2
Provisions/NPLs	97.2	99.2	87.8	87.1
Earnings and profitability				
Return on (average) assets	2.5	2.2	2.7	2.5
Interest margin/gross income	31.5	30.9	27.8	28.3
Non-interest expenses/gross income	58.8	54.3	55.4	46.5
Personnel expenses to non-interest expenses	26.7	28.5	15.5	20.4
Liquidity				
Loans to deposits	91.9	89.7	95.6	101.3
Liquid assets/total assets	31.6	36.0	37.9	28.1
Liquid assets/short-term liabilities 3/	28.8	37.7	38.2	37.0

Sources: Data provided by the Mongolian authorities; and Fund staff estimates.

1/ Yield of 14-day bills until 2006 and of 7-day bills for 2007.

2/ Including official transfers.

3/ Short-term liabilities are defined as the sum of current account and demand deposits.

