EXECUTIVE SUMMARY

The economy expanded by 5.6 percent in the first half of 2024, supported by the mining sector growth and solid domestic demand. The transportation sector was the second-largest contributor to growth, following robust mining sector growth of 15.4 percent, driven by higher production of coal, iron ore, and copper concentrate. Growth was also supported by the construction and manufacturing sectors, primarily due to new road construction and increased beverage production. Trade and service activities remained strong, with robust domestic demand. However, agricultural output shrank by 25 percent due to significant livestock losses from severe weather events.

On the demand side, growth is fueled by the expansion of consumption and inventory. Private consumption was the main growth driver, supported by an increase in consumer credit and higher household incomes related to public sector wage hikes. In addition, large inventory accumulation—boosted by a rapid increase in imports and an expanding corporate credit supply—played a significant role in overall growth.

The fiscal surplus narrowed to MNT 57.9 billion at the end of the first half of 2024. The fiscal surplus narrowed to MNT 57.9 billion at the end of the first half of 2024. Government revenue amounted to MNT 6.4 trillion as coal exports reached 40.6 million tons due to increased external demand. While the overall fiscal balance was in surplus, the seasonally adjusted fiscal balance was estimated at a deficit of MNT 40.4 billion. The growth in the public sector wage bill—aimed at supporting civil servants, encouraging regional development, and creating a favorable living environment in rural areas—stimulated domestic demand. Although government debt dynamics remain sustainable, it is expected to rise in the medium term due to pending issuances of new external and domestic bonds by Ulaanbaatar City.

Inflation remained at the lower end of the central bank's target range at 5.1 percent, and credit growth accelerated with further policy cuts. Deposit growth was supported by rising household real incomes, as real interest rates increased with disinflation and the exchange rate remained stable. While foreign currency deposits and current accounts fell, domestic currency deposits and current accounts rose. Additionally, credit growth accelerated, and the share of non-performing loans in total loans fell to 5.9 percent, hitting an eight-year low.

Export growth is attributed to an increase in the export volume of key commodities. Export growth is attributed to an increase in the export volume of key commodities. Exports rose by 4 percent in the first half of 2024, primarily driven by increases in the export volumes of coal, copper concentrate, and iron ore. Imports surged due to strong domestic economic activity and robust credit growth, contributing to an increase in trade turnover. The balance of payments recorded a deficit, reflecting import growth and the central bank's partial repayment of its swap line. Gross international reserves declined and the exchange rate depreciated compared to the end of the first quarter of 2024.

Policies aimed at ensuring macroeconomic stability are critical for improving the sovereign credit rating and enhancing economic resilience. Recent changes to the fiscal rules outlined in the Law on Fiscal Stability, which are crucial for ensuring macroeconomic stability, could pose several risks to the economy. First, introduction of a new fiscal rule based on a budget 'core' balance—which excludes expenditures financed by securities and external loans—could lead to a rapid expansion in capital expenditure, a deterioration in budget accountability, constrained private sector activity, and increased public sector intervention in the economy. Furthermore, this rule change could substantially incentivize new issues of securities to finance the excessive capital spending demands of central and local governments, potentially leading to financial sector imbalances and macroeconomic instability. Second, allowing current expenditure to expand up to 30 percent of nominal GDP could result in a procyclical fiscal policy in response to commodity price fluctuations, raising risks of macroeconomic instability and potential downgrades in sovereign credit ratings.