CHAPTER 4

EXTERNAL SECTOR

4. EXTERNAL SECTOR

OVERVIEW

Although the export volumes of key mining products such as coal, copper concentrate, and iron ore increased, the decline in coal prices limited the growth of export revenues. Imports of investment and consumer goods remained high, reflecting expansion in economic activity. The annual growth of international reserves slowed in the third quarter of 2024, and the nominal effective exchange rate depreciated due to increased import growth and payments related to the central bank's swap agreements.

CHAPTER 4

4.1 FOREIGN TRADE

55. The export volumes of main commodities increased but coal prices declined. As of the third quarter of 2024, exports increased by 4.3 percent year-on-year to to USD 11.7 billion, primarily driven by higher export volumes of coal, copper concentrate, and iron ore. Coal export volumes grew by 25 percent year-on-year to 61.2 million tons, but export prices dropped by 18 percent compared to a year earlier. Continued growth in coal and copper concentrate exports, along with higher global prices for pure copper and gold, will further support the expansion of exports.

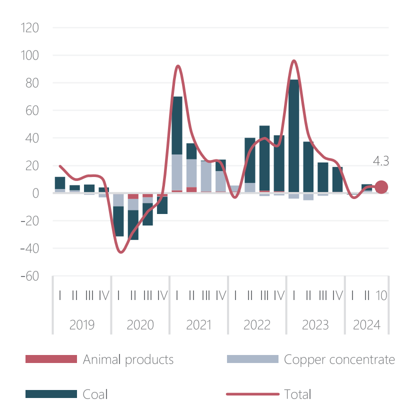
56. Copper concentrate and iron ore exports increased. Fueled by production from Oyutolgoi's underground mine, copper concentrate exports reached 1,186 thousand tons in the third quarter of 2024, marking a 3 percent increase compared to the same period last year. Iron ore exports also surged by 29 percent, reaching 5,466 thousand tons, driven by higher production levels. Moving forward, both copper concentrate and iron ore extraction are expected to continue growing, while the global price of refined copper is anticipated to rise.

57. Exports of agricultural products declined due to the severe winter and spring seasons. By the third quarter of 2024, meat exports fell by 28 percent, cashmere exports by 2 percent, and hides and skins exports by 24 percent, primarily due to severe weather conditions affecting most parts of the country.

58. Trading activity on the Mining Commodity exchange weakened. By the first nine months of 2024, a total of 17.8 million tons of coal were traded on the Mining Commodity exchange for USD 2.1 billion, 1,779 thousand tons of iron ore and concentrate for USD 125 million, 5.4 thousand tons of copper concentrate for USD 12 million, and 15.4 thousand tons of fluoride ore for USD 2.4 million. The number of trades dropped to 112 in the third quarter of 2024, from 127 and 212 trade in the first and second quarters of 2024, respectively. Notably, the number of coal trades steadily declined, from 55 in May 2024 to just 12 in September 2024.

Figure 4.1. Exports

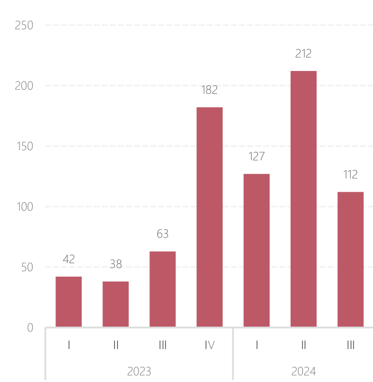
1. **Export growth**
(percent)



2. **Export volumes of main commodities**

Product	2023.09	2024.09	Growth
Copper concentrate /thousand.ton/	1,151	1,186	3.0 %
Coal /million ton/	48.9	61.2	25.2 %
Gold /kg/	5,398	5,048	-6.9 %
Iron ore / thousand.ton/	4,221	5,446	29.0 %
Crude oil / thousand.bbl/	3,540	3,100	-12.4 %

3. **Coal trades at the Mining commodity exchange**



Source: MCGA

59. Imports surged due to sustained economic growth. As the economy grew for the tenth consecutive quarter, imports reached USD 8.6 billion in the third quarter of 2024, marking a 27.4 percent increase compared to the same period last year (Figure 4.2). According to the input-output table published by the NSO, total imports are categorized into three areas: intermediate consumption, final consumption, and capital accumulation. Notably, approximately 60 percent of imported goods are used for production.

60. Considering the growth of imports by group, of the total increase in imports, 12.4 percentage points were attributed to machinery and equipment for investment purposes and building materials, 10.2 percentage points to consumer products, and 4.8 percentage points to industrial inputs.

61. Imports of intermediate products for mining production increased. As of the third quarter of 2024, coal extraction rose by 29 percent, and export volumes increased by 25 percent, leading to a higher demand for intermediate products used in the mining sector. Imports of excavators and backhoe loaders totaled USD 264 million, doubling from the previous year. Imports of heavy vehicles increased by 85 percent, reaching USD 570 million, while diesel fuel imports amounted to USD 990 million, marking a 23 percent rise compared to the same period last year.

62. The growth in passenger car imports was the main driver of the increase in consumer goods imports. The growth in imports of durable goods, particularly passenger cars, was a major factor driving the increase in consumer goods imports. As of the third quarter of 2024, consumer credit growth reached 37.3 percent, driving an increase in the import of durable goods. In particular, imports of passenger cars reached 93.6 thousand, a 75.8 percent increase compared to the same period last year. Compared to the same period last year, when imports of large passenger cars with engine capacities exceeding 3,501 cm^3 were prominent, this year has seen a significant increase in the import of medium and small passenger cars with engine capacities under 3,500 cm^3. Driven by the high imports of passenger cars and the increased number of anniversary events in the provinces, gasoline imports totaled USD 464 million, marking a 15.9 percent increase.

63. Imports of food products increased. Real household incomes have increased for five consecutive quarters, resulting in higher household consumption. Food imports reached USD 840 million, reflecting a 24.7 percent rise compared to the same period last year. Wheat flour imports reached 38 thousand tons, a nine-fold increase compared to the previous year, following the decision to exempt wheat from customs duties starting May 1, 2024, and lift import limits.

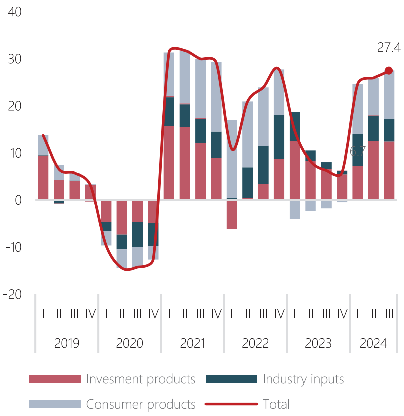
64. Imports of construction materials increased due to higher funding for mortgage loans and a reduction in customs duties on cement. The constuction sector expanded by 7.8 percent in the first three quarter of 2024, while imports of construction materials reached USD 1,028 million, marking a 17 percent increase compared to the same period last year. The Savings Fund allocated MNT 0.5 trillion to the mortgage concessional loan program, increasing the outstanding mortgage loan by MNT 1.8 trillion compared to the same period last year, which in turn boosted housing demand and increased imports of construction materials. To mitigate construction material price inflation, the government lifted restrictions on cement imports and reduced the customs duty from 20 percent to 5 percent until October 1, 2024, leading to a 12 percent year-on-year increase in cement imports, reaching 86 thousand tons. Growth in construction material imports is expected to continue in the fourth quarter of 2024, driven by the construction projects outlined in the 2024 budget amendment and the increase in mortgage lending.

65. The increased capacity and extended working hours at Zamyn-Uud Port enhanced the flow of imported goods. With over 50 percent of total imported goods passing through Zamyn-Uud Port, the Government of Mongolia extended the operating hours of the Zamyn-Uud-Ereen border crossing to 24 hours a day from April 1 to September 30, 2024. As a result, the number of vehicles crossing the border reached 135,300 between April and August 2024, marking a 44 percent increase compared to the same period last year. During this period of high economic activity, ensuring the continuous flow of imports is crucial to maintaining price stability.

66. Due to a slowdown in the price growth of goods from trading partner countries, the increase in the price of imported goods remained relatively low. In the first three quarters of 2024, imports increased by USD 1.9 billion compared to the same period last year, with approximately 85 percent of this increase attributed to volume and 15 percent to price changes (Figure 4.2). The slowdown in price growth from key trading partner countries kept the increase in import prices at a low level. Specifically, inflation in the People's Republic of China, which accounts for 40 percent of our total imports, averaged 0.3 percent in the first three quarters of 2024. Meanwhile, inflation in the Russian Federation, which makes up 25 percent of total imports, averaged 8.3 percent during the same period. However, 70 percent of the products imported from the Russian Federation consist of petroleum products, with 21 percent being AI-92 gasoline and 45 percent being diesel fuel. Under the agreement signed with Rosneft in 2022, AI-92 gasoline is being purchased at stable prices, and the decrease in the price of diesel fuel from Russia contributed to the low increase in the price of imported goods. Additionally, 10 percent of total imports come from Japan, mainly consisting of automobiles and spare parts, and the depreciation of the Japanese yen against the USD, reaching its lowest level since 1990, helped reduce the cost of goods purchased from Japan.

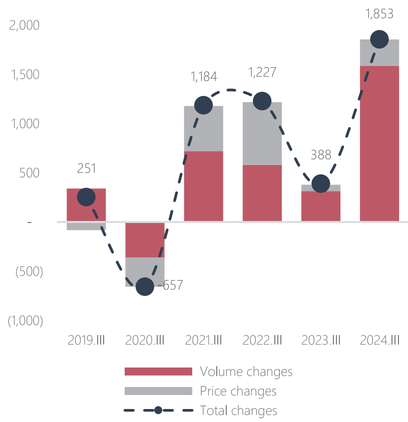
Figure 4.2. Imports

1. Annual growth in imports
(percent)



Source: MCGA

2. Annual change in imports
(USD million)



Source: MED estimates

3. Imports of main products
(USD million)

Products	2023.09	2024.09	Change
Food	673	839	24.7%
Passenger car	507	804	58.6%
Heavy truck	307	566	84.7%
Construction material	877	1028	17.2%
Equipment	1,198	1,599	33.5%
Fuel	1,202	1,452	20.8%
Total	**6,755**	**8,608**	**27.4%**

Source: MCGA

CHAPTER IV

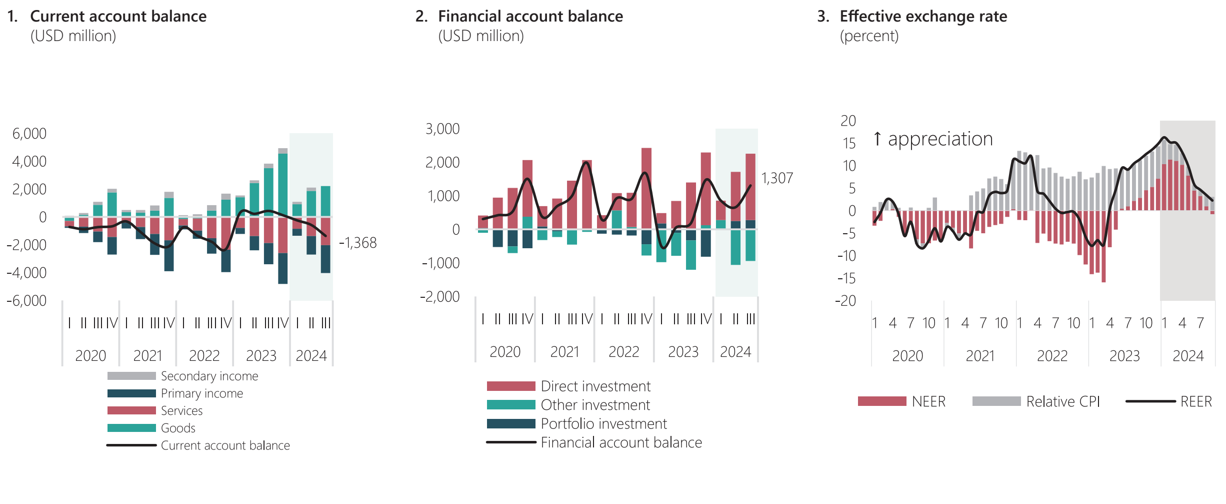
4.2 BALANCE OF PAYMENTS

67. The current account deficit widened, driven by a surge in goods imports. The current account deficit widened to USD 1.4 billion, equivalent to -7.2 percent of GDP, in the third quarter of 2024 as goods imports growth (7 percent) outpaced exports growth (29 percent).

68. The reduction in freight transportation payments contributed to a slowdown in the growth of the service account deficit. As a result of government measures, including the sale of mineral products at border prices, improved organization of export transportation operations, and enhanced efficiency, the debit for freight transportation services decreased by 20 percent year-on-year in the first three quarters of 2024**.** The reduction in the freight transportation debit contributed to a slowdown in the growth of the service account deficit, which decreased to 8 percent, down from 21 percent in the same period last year.

69. Net outflow of the travel account remains high. As of the third quarter of 2024, travel expenditures recorded an increase of 34 percent or USD 0.3 billion year-on-year, while inflows from travel services rose by only USD 55 million. The increase in travel expenditure was primarily driven by a 24 percent rise, or 221 thousand more people, in the number of citizens traveling abroad for personal reasons and tourism, along with a 22 percent increase in tuition fees paid by students studying abroad. On the other hand, the tourism service revenue growth remained subdued at only 12 percent, despite a 22 percent increase in the number of incoming foreign tourists.

Figure 4.3. Current and financial account balances, exchange rate



Source: MED calculation

Source: MED calculation

Source: MED calculation

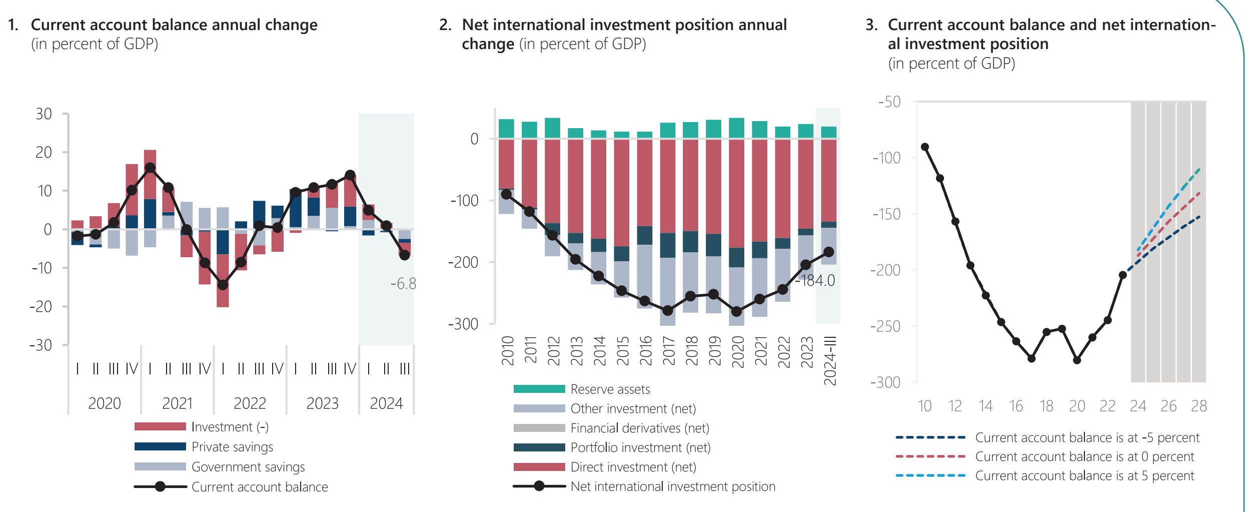
70. The financial account surplus expanded, reflecting increased FDI and portfolio inflows. Foreign direct investment inflow rose to USD 2.9 billion as of the third quarter 2024, up by USD 0.6 billion or 27 percent from a year earlier. According to the statistics of the General Authority for State Registration, the number of companies with foreign investment registered as of September 2024 reached 349, marking a 2.3-fold increase compared to the same period last year. Compared to the same period last year, direct investment in the mining sector increased by USD 0.6 billion, while investments in the trade, transportation, and financial sectors decreased by a total of USD 84 million. Furthermore, the issuance of new international bonds by "Mongolian Mortgage Corporation HFC" LLC, the Development Bank of Mongolia, and Golomt Bank boosted portfolio inflows, contributing to a USD 1.1 billion increase in the financial account surplus.

71. The growth rate of gross international reserves slowed, and the nominal effective exchange rate depreciated. Gross international reserves reached USD 4.7 billion at the end of the third quarter of 2024, with the annual growth rate slowing to 13 percent, down from 53 percent at the end of the first quarter. The central bank repaid USD 0.6 billion of its PBOC bilateral currency swap line in the second quarter of 2024 and sold USD 4.6 billion to foreign exchange markets in the first 9 months of 2024. The MNT/USD exchange rate stood at 3,381 MNT at the end of the third quarter of 2024, remaining largely unchanged from the previous quarter. However, the nominal effective exchange rate index, weighted against the currencies of trading partner countries, depreciated by 0.8 percent in September, reversing its appreciation since May 2023. In contrast, the real effective exchange rate index was up by 2.2 percent due to higher domestic prices.

72. The current account balance deteriorated due to a slowdown in savings growth and an increase in investment. From a savings-investment perspective, the current account balance reflects a difference between national savings and investment. The current account balance shifted to a deficit of 7.2 percent of GDP by the third quarter of 2024, compared to a surplus of 0.6 percent of GDP at the end of 2023. This shift was primarily driven by higher consumption and lower savings in the public sector, as well as increased investment in both the government and private sectors.

73. Mongolia's net international investment position remains weak. The net international investment position measures the gap between a country's financial assets held abroad and its liabilities to other countries. At the end of the third quarter of 2024, the net international investment position stood at USD -42.9 billion, equivalent to -184 percent of GDP. Financial liabilities totaled USD 51.6 billion, 5.9 times greater than the assets held abroad. It is important for Mongolia to improve its net international investment position and reduce vulnerability to external shocks by improving the current account balance and increasing international reserves.

Figure 4.4. Current account balance and net international investment position



Source: MED calculation

Source: MED calculation

Source: MED calculation

Note: Calculated as rolling sum of four quarters. Investment is displayed as a negative value. In the last figure, real GDP growth and inflation rates are assumed to be constant.

CHAPTER IV

4.3 EXTERNAL DEBT

74. The gross external debt increased in nominal terms, but declined as a share of GDP. Mongolia's gross external debt totaled USD 35.6 billion at the end of the third quarter of 2024, up by USD 2.4 billion or 7.2 percent from a year earlier. On the other hans, the external debt-to-GDP ratio fell to 153 percent, down by 21.7 percentage points from a year earlier, due to the nominal GDP growth.

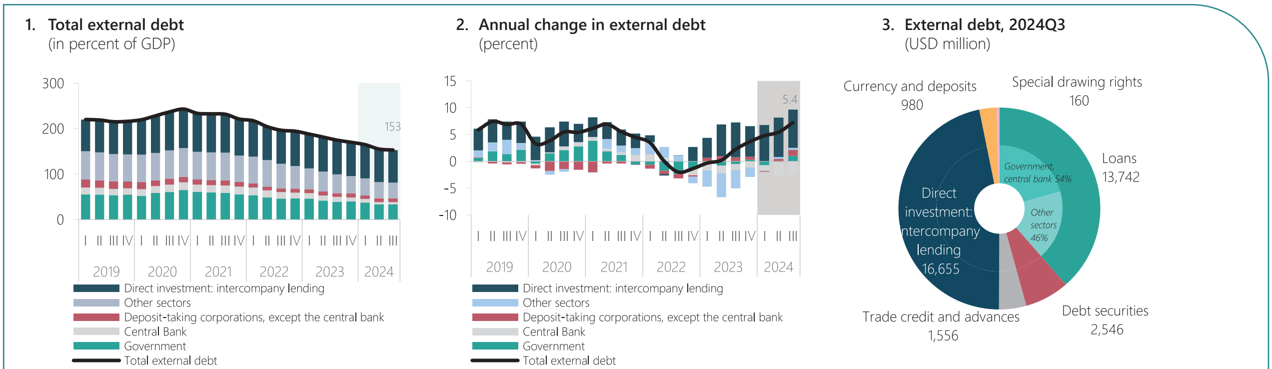
75. The stabilization of international reserves enabled the central bank to repay its swap line debt. Gross international reserves, which had fallen to USD 2.8 billion in 2022, rose to USD 5.2 billion at the end of the first quarter of 2024. This increase in reserves enabled the central bank to repay CNY 4.5 billion of the currency swap facility with the PBOC in the second quarter of 2024, reducing the outstanding balance of the swap line to CNY 6.0 billion. As a result, the central bank's external debt decreased by USD 813 million or 42 percent at the end of the third quarter of 2024, compared to a year earlier.

76. The external debt stock of the private sector rose. The private sector's external debt increased by USD 2.9 billion, with 83 percent of this rise attributed to intercompany lending. Within the private sector, the external debt of deposit-taking corporations' in the form of debt securities tripled, while loans grew by 12 percent compared to the same period last year, reflecting a greater access to external financing for the private sector.

77. The majority of the external debt is comprised of foreign direct investment and loans. 47 percent of the total external debt, amounting to USD 16.7 billion, consists of intercompany lending, while 39 percent, or USD 13.7 billion, is in the form of loans. Of the total outstanding loan, 54 percent is held by the government and central bank, while 46 percent by the private sector. It is important to maintain macroeconomic stability and improve credit ratings to increase sources and reduce costs of external financing.

78. The medium-term external debt dynamics are expected to be sustainable but remain vulnerable to exchange rate and current account shocks. Under the baseline scenario, the external debt-to-GDP ratio is projected to steadily decline over the medium-term, supported by growth in exports and GDP. However, the ratio remains particularly sensitive to exchange rate and current account shocks. Compared to the baseline, the external debt-to-GDP ratio could increase by 12.3 percentage points when current account balance deteriorates by one standard deviation and 15.2 percentage points if exchange rate depreciates by 10 percent.

Figure 4.5. External debt



Source: MED calculation
Note: The ratio is calculated as rolling sum of four quarters.

Figure 4.6. External debt sustainability

External debt

(in percent of GDP, unless otherwise indicated)

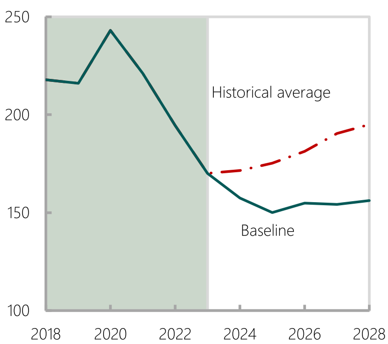
	Actual								Projections					Debt-stabilizing
	2018	2019	2020	2021	2022	2023			2024	2025	2026	2027	2028	non-interest current accoun
External debt: Baseline	217.9	216.1	243.1	221.1	194.4	170.1			157.5	150.0	154.9	154.2	156.2	-2.5
Change in external debt	-21.5	-1.7	26.9	-21.9	-26.7	-24.3			-12.5	-7.5	4.8	-0.6	2.0	
Identified net debt-creating flows	-20.9	-8.6	14.9	-25.3	-11.5	-32.4			-16.4	-13.2	-2.9	-11.2	-4.7	
Non-interest current account deficit	7.7	5.5	-4.9	5.6	4.9	-10.9			-1.4	-3.3	-6.1	-7.1	-2.1	
Net non-debt creating capital inflows	-6.8	-8.1	-4.6	-7.7	-0.9	-1.4			-1.8	-1.2	-1.0	-1.0	-1.5	
Automatic debt dynamics 1/	-21.8	-6.0	24.4	-23.2	-15.6	-20.1			-13.3	-8.7	4.1	-3.1	-1.0	
Contribution from nominal interest rate	9.0	9.7	10.0	8.2	8.5	10.3			10.6	7.9	7.5	6.8	5.8	
Contribution from real GDP growth	-16.2	-11.3	10.5	-3.5	-9.9	-12.2			-8.2	-10.5	-9.5	-9.4	-9.6	
Contribution from price and exchange rate changes	-14.7	-4.5	3.9	-27.9	-14.2	-18.2			-15.6	-6.2	6.1	-0.5	2.7	
Residual	-0.6	6.9	12.1	3.4	-15.2	8.1			3.9	5.7	7.8	10.5	6.6	
External debt-to-exports ratio (in percent)	374.5	364.8	423.3	377.7	303.4	223.0			223.7	207.5	194.3	188.3	192.7	
External debt: Scenario with key variables at their historical averages 2/									171.5	175.3	181.2	190.4	195.0	-4.5
							historical average	standard deviation						
Real GDP growth (in percent)	7.7	5.6	-4.6	1.6	5.0	7.4	4.0	3.9						
Nominal external interest rate (in percent)	4.3	4.8	4.3	3.9	4.3	6.3	4.6	0.6						
Growth of exports (USD, in percent)	12.8	9.7	-9.1	17.1	22.8	41.1	14.5	17.6						
Growth of imports (USD, in percent)	37.5	3.1	-20.6	26.1	30.9	11.8	7.0	21.9						
Non-interest current account balance	-7.7	-5.5	4.9	-5.6	-4.9	10.9	-1.4	6.2						
Net non-debt creating capital inflows	6.8	8.1	4.6	7.7	0.9	1.4	3.2	4.2						

1/Change in external debt driven by variables including GDP growth, external interest rate, and exchange rate

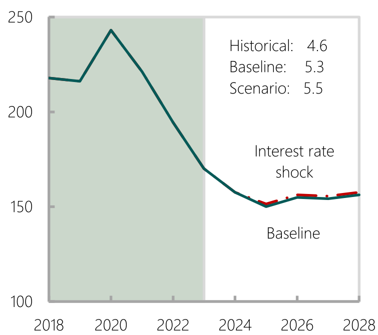
2/The key variables include non-interest current account balance, net non-debt creating capital inflows, real GDP growth, GDP deflator, nominal external interest rate.

Historical averages and standard deviations are calculated over the past 10 years.

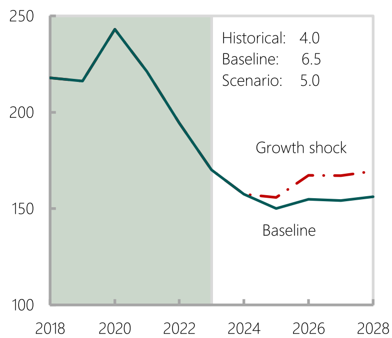
1. Baseline and historical scenarios



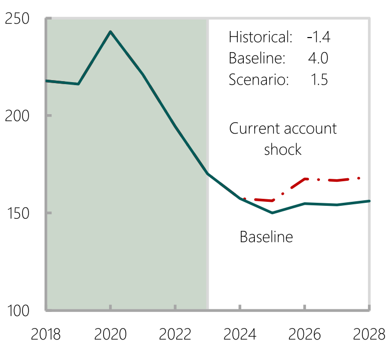
2. Interest rate shock



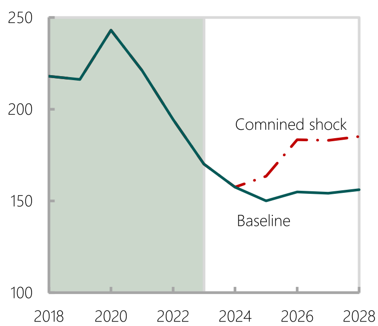
3. Growth shock



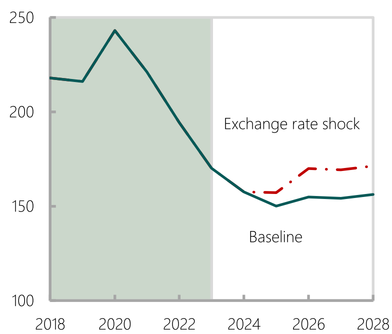
4. Non-interest current account shock



5. Combined shock (interest rate, current account, GDP growth)



6. Exchange rate depreciation shock



Source: MED calculation

Note: Historical averages and standard deviations are calculated over the past 10 years.

Permanent ½ standard deviation shocks applied to current account balance, GDP growth rate, and combined shock assumes ¼ standard deviations.

Permanent increase of 100 bps applied to interest rate and depreciation of 10 percent is applied to exchange rate.