GOVERNMENT OF MONGOLIA

MINISTRY OF ECONOMY AND DEVELOPMENT

MACROECONOMIC REPORT

2024 Q1

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TOWARD STEADY GROWTH

JULY 2024

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ABBREVIATIONS

FDI	Foreign direct investment
GDP	Gross domestic product
GIR	Gross international reserves
HSES	Household socio-economic survey
MED	Ministry of Economy and Development
MCGA	Mongolian Customs General Administration
NEER	Nominal effective exchange rate
NSO	National Statistical Office
PMI	Purchasing Managers' Index
REER	Real effective exchange rate
TPP	Thermal power plant

EXECUTIVE SUMMARY

The economic growth accelerated to 7.8 percent in the first quarter of 2024, driven by resilient domestic activity and robust external demand. Mining production continued to expand, and all sectors contributed positively to growth except the agricultural sector. The mining sector expanded by 13 percent, contributing 1.9 percentage points to overall growth. Coal production increased by 25 percent to 22 million tons, while iron ore production reached 1.5 million tons, marking a 63 percent increase from the same period last year. The positive spillovers from the mining sector supported the transportation sector while construction and manufacturing sectors maintained growth momentum with increased general engineering construction and food production. However, the agricultural sector exerted a drag on overall GDP growth, reflecting declines in the sector's production, exports, capital formation, and the number of workers due to harsh winter and spring conditions, which resulted in the loss of 6.3 million adult livestock as of the first quarter of 2024.

Domestic demand was the main driver of economic growth in the first quarter of 2024, after four consecutive quarters of external demand-led growth. Stronger household consumption and rising real incomes fueled growth in trade and service sectors. However, real income growth remained subdued in rural areas despite accelerating in the capital city. The workforce grew with the increased number of employees and the share of active enterprises in the total registered enterprises reached a 5-year high.

The budget balance recorded surplus for five consecutive quarters as mining revenue growth remained strong. The budget balance was in a surplus of MNT 1.6 trillion at the end of the first quarter of 2024, reflecting positive effects of series of policy measures aimed at boosting exports that include the promotion of the Mining commodity exchange, infrastructure enhancements at border ports, and improvements in tax registration and coverage. The Government of Mongolia successfully repaid the remaining USD 53 million of Khuraldai bond in March 2024, easing debt-service pressures on budget.

Inflation remained within the target range and total savings and newly issued loans increased. Inflation declined to 7 percent in the first quarter of 2024 with moderation in both domestic and import price growth, and the central bank cut the policy rate for the first time in 15 months. Real income and savings grew, owing to higher real interest rates and a stable exchange rate. Banks' newly issued loans surged and the share of non-performing loans in total loans decreased to 7.1 percent, and capital adequacy and profitability indicators improved.

Gross international reserves rose, and the exchange rate appreciated, even though import growth outpaced export growth. Despite higher export volumes of coal, copper concentrate, and iron ore, total exports recorded a slight decline due to falling coal prices and decreased agricultural exports due to adverse weather conditions. On the other hand, robust domestic demand along with credit expansion boosted demand for imports, leading to the growth in trade turnover. Even though import growth led to a deterioration in the current account balance, the balance of payments improved with the increased net inflow of FDI and government loans, contributing to further accumulation of gross international reserves and appreciation of the exchange rate.

NEAR-TERM OUTLOOK

Economic growth is expected to be around 6.0 percent at the end of 2024. Continued production of Oyutolgoi underground mine with higher copper and gold contents along with increased production of coal, gold, and iron ore are expected to support the mining sector. The transportation sector growth is projected to continue reflecting positive spillovers from the mining sector while measures aimed at attracting tourists are expected to stimulate the tourism and service sectors in the latter half of 2024. Manufacturing production is expected to be boosted by the surge in imports of industrial machinery and equipment in 2023 following the decision to exempt food and agricultural production equipment and machinery from customs duties. However, the agricultural sector is expected to experience a contraction in 2024 as the number of losses of adult livestock is likely to be higher compared to 2023 due to adverse weather conditions. Trade and service sectors are projected to support overall growth as household consumption growth continues to spur domestic demand.

The trade balance is expected to record a surplus of USD 6.1 billion at the end of 2024. Total exports is set to reach USD 17.4 billion with the continuation of policy measures aimed at improving border port infrastructure, export transportation, and the Mining commodity exchange. Particularly, Mongolia expects to export 78 million tons of coal, 1,560 thousand tons of copper concentrate, 8.4 million tons of iron ore, and 4.2 million barrels of crude oil. Total imports are expected to increase to USD 11.3 billion with robust economic activity, higher household income along with credit growth. However, imports could be disrupted if the congestion at Tianjin port worsens.

Inflation remains within the central bank's target range. Inflation from imported goods is projected to be moderate, reflecting stronger exports and a stable exchange rate. However, upside risks to supply-driven inflationary pressure stemming from harsh winter conditions remain.

Economic outlook remains subject to both domestic and external downside risks. The severe winter conditions observed in most provinces could cause food price spikes, reduce household income in rural areas, and lead to contraction in the agricultural sector. Furthermore, further worsening of congestion at Tianjin port could disrupt flows of container imports. Uncertainty in the global economic outlook could weigh on the demand and prices of the main exporting commodities. Rising geopolitical tensions could put upward pressure on global prices of fuel, grain, food, and energy, which could add to domestic inflationary pressures.

POLICY OBJECTIVES

The Government of Mongolia remains committed implementing policies aimed at ensuring stable economic growth and enhance economic competitiveness. The Law on Budget framework for 2025 and budget projections 2026-2027 was developed within the following policy objectives.

To maintain stable economic growth of more than 6 percent. Policies aimed at boosting mining and agricultural exports, promoting activities and liberalization of sectors including transportation, tourism, and service sectors will be implemented. The increased production of mining products including Oyutolgoi's copper concentrate with higher copper and gold contents, along with steady growth in investments and exports within the framework of trade agreements with partner countries, will support the mining sector.

To reduce inflation to approximately 3 percent in the medium term to enhance economic competitiveness and boost households' real income. This will be achieved through comprehensive reforms in the agricultural sector, improved food supply, optimization of export and import regulations, increased international reserves, reduced import inflation and budget deficits.

To boost export income and bring gross international reserves to USD 10 billion in 2026. Measures such as increasing exports and transportation, ensuring transparency in mineral extraction, processing, and transportation, and continuously promoting the activities of the Mining commodity exchange will be implemented.

To lower the budget balance-to-GDP ratio to -2.0 percent in 2025, -1.5 percent in 2026, and -1.0 percent in 2027, with a policy of maintaining budget balance in surplus thereafter. According to the Law on Fiscal Stability, the structural balance of consolidated budget must be in a deficit of no more than two percent of GDP or be in surplus. The structural balance will be in deficit equal to two percent of GDP in 2025, with deficits gradually reduced according to the adopted reduction policy.

To gradually reduce the ratio of the present value of government debt-to-GDP to 50 percent in 2025, 45 percent in 2026, and 40 percent in 2027. The Law on Fiscal Stability specifies that the present value of government debt should not exceed 60 percent of GDP. Due to the recovery of the mining sector and the accompanying growth of the transport and service sectors, the budget has been in surplus, creating conditions to reduce debt level. To reduce debt burden and avoid credit rating downgrade, the objective to reduce the government debt-to-GDP ratio to 40 percent by 2027 was included in the Law on Budget framework for 2025 and budget projections 2026-2027.

CHAPTER I

REAL SECTOR

I. REAL SECTOR

OVERVIEW

Although the growth was largely driven by external demand in 2023, the stronger-than-expected domestic demand dominated the growth in the first quarter of 2024. The economic growth was in line with the projection, helped by all economic sectors, except agriculture. The mining output and export increased due to the higher production of key commodities, which spurred transportation activity. The construction and manufacturing sectors sustained growth as engineering infrastructure and beverage production increased. Meanwhile, rising household real incomes and private consumption, which are largely supported by the wage and social benefits increase, fueled the domestic demand for trade and services sectors. The output gap is approaching zero, reflecting the combined effect of an increase in employment and higher capital formation due to an influx of loan financing and foreign direct investment.

CHAPTER I

1.1 AGGREGATE SUPPLY

1. Growth accelerated to 7.8 percent in 2024Q1 due to the expansion in all economic sectors, except agriculture. Nominal GDP increased by 19 percent to MNT 16.4 trillion, and real GDP by 7.8 percent to MNT 6.1 trillion in the first quarter of 2024. Except agriculture, all economic sectors contributed positively to the growth. The growth is projected to be robust. In terms of economic composition, mining sector accounts for 28 percent, followed by wholesale and retail trade at 16 percent, agriculture at 10 percent, manufacturing at 9 percent, transportation at 6 percent, construction, electricity, and water supply at 5 percent, while the remaining 26 percent is attributed to other service sectors.

2. As coal and iron ore production increased, mining output grew in line with the projection. The mining sector expanded by 13 percent year-on-year, contributing 1.9 percentage points to overall growth. Coal production was the main driver of growth, which reached 22 million tons and increased by 25 percent. Iron ore production amounted to 1.5 million tons, rising significantly by 63 percent from the same period of the previous year. While copper concentrate production was almost at the same level as a year ago, gold and crude oil production decreased by 5 percent and 10 percent, respectively.

3. The transportation sector expanded as coal export volume escalated. The transportation sector expanded by 27 percent, contributing 1.3 percentage points to overall growth as carried freight increased by a 42 percent year-on-year, with volume reaching 34.3 million tons. Higher exports of coal, iron ore, and copper concentrates and import growth led to an increase in carried freight. Regarding the Government Resolution No. 362 of 2022, aimed at bolstering gross international reserves, 16 categories of domestic freight tariffs, 2 categories of passenger transport tariffs were adjusted, and the discount on the tariff for transit cargo transport between China and Russia was reduced from 61 percent to 51 percent. As a result, total carried freight increased, and the rail tariff reached a profitable level, leading to a 41 percent increase in transportation revenue.

4. The manufacturing sector sustained its growth momentum, supported by beverage production. The manufacturing output expanded by 6.3 percent year-on-year, contributing 0.4 percentage point to overall growth. The growth was driven by the 43.5 percent growth of beverage production[1] , which makes up about 30 percent of the sector, and the 0.1 percent growth of milk production, which accounts for about 7 percent of the sector. However, meat manufacturing declined by 9 percent year-on-year as a result of livestock losses from adverse weather conditions in 2023-24. Furthermore, electricity, gas, steam, and air conditioning supply increased by 7.7 percent, contributing 0.4 percentage point to growth.

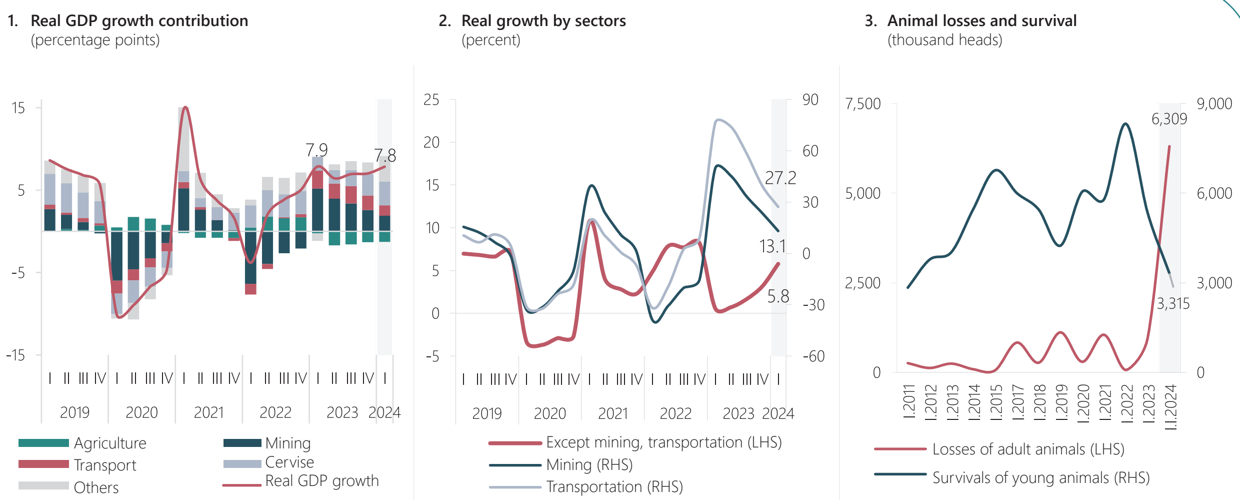
5. The completion of large infrastructure projects supported the construction output. Constructions of Amgalan TPP and Choibalsan TPP reached 93 percent and 94 percent of completion, respectively, by April 2024, compared to 56.3 percent and 81.3 percent of completion as of October 2023. Subsequently, construction activity grew by 27.7 percent, contributing 0.2 percentage point to overall growth. The major contributor was engineering infrastructure construction, which surged by 4.5 times, while non-residential construction increased by 30 percent year-on-year.

[1] Including alcoholic beverages

6. The service sector expanded by 7.7 percent. The service sector includes wide range of activities, including wholesale and retail trade, transportation, information and communication, and consulting services. The wholesale and retail trade is largest activity in the sector, and it grew at an annual rate of 6.5 percent, which is higher than expected, reflecting strong household consumption. Households expanded their consumption of non-food goods, resulting in a 19 percent increase in sales of non-food products, which further fueled sales growth. Besides, the information and communication sector expanded by 26.3 percent, while other service sectors grew by 3.7 percent.

7. Agricultural output contracted, reflecting a significant loss of adult livestock. The loss of adult livestock surged by 5.4 million to 6.3 million heads, leading to the agricultural sector's contraction of 31.3 percent, which reduced overall growth by 1.3 percentage points. (See Box.1)

Figure I.1 Real GDP growth



Source: NSO
Note: Contributions of sectors to the cumulative growth of real GDP.

Source: NSO
Note: Cumulative growth of real GDP.

Source: NSO
Note: Animal losses of the first quarter of each year.

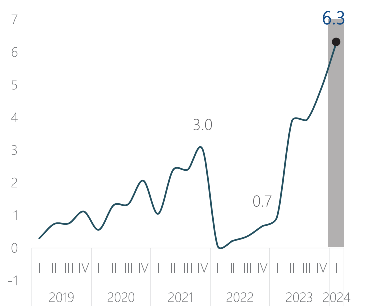
BOX 1. AGRICULTURE INDUSTRY AND ADULT LIVESTOCK LOSSES

CURRENT CIRCUMSTANCES

The agriculture sector contracted by 31.4 percent year-on-year and lowered overall growth by 1.9 percentage points. Agriculture production constitutes 13 percent of Mongolia's economy, following the mining sector, and its 91 percent consists of livestock industry and rest 9 percent is crop production. Livestock production is highly volatile and dependent on climate conditions. During the winter of 2023-2024, over 90 percent of the territory was covered with snow. Severe cold weather resulted in ice (iron) dzud in 46 soums across 14 provinces, and black dzud in some soums of Gobi province due to summer drought, despite relatively low snow thickness and density. By the end of 2023, the number of livestock had decreased by 6.4 million, reaching 64.7 million. In the first quarter of 2024, the loss of adult livestock reached 6.3 million head, equal to 9.8 percent of the total number of livestock at the beginning of the year. Losses in Arkhangai, Tuv, Sukhbaatar, Khentii, and Dornogovi provinces (account for 30 percent of the total number of livestock) composed 65.7 percent of the overall adult animal losses.

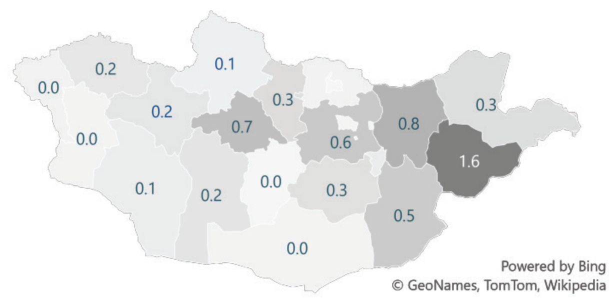
Figure I.2 The losses of adult livestock

1. **Cumulative number of adult livestock losses** (million heads, by quarterly)



Source: NSO

2. **The losses of adult livestock,** (by provinces, million heads)



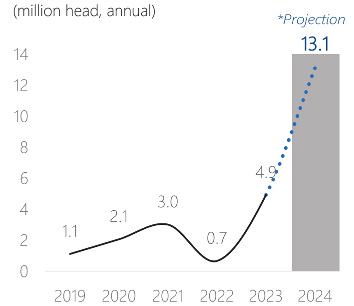
Source: NSO

PROJECTION

The number of adult livestock loss is projected to reach 13.1 million heads by the end of 2024, bringing the total number of livestock to the same level as in 2015-2016. By location, high number of losses expected in Sukhbaatar, Khentii, Uvurkhangai, Gobi-Altai, Hovd, and Uvs provinces, which will be the highest in the past 50 years.

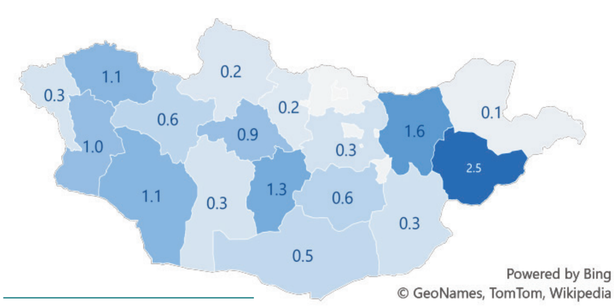
Figure I.3 Projection of adult livestock losses

1. **Adult livestock losses** (million head, annual)



Source: NSO, MED estimation

2. **The expected losses of adult livestock** (by province, million head)



Source: NSO, MED estimation

Note: The total precipitation from January to March of 2008-2023 is used as a proxy for the impact of weather conditions on losses of adult livestock, and the total number of livestock loss was projected by calculating herd turnover.

CHAPTER I

1.2 AGGREGATE DEMAND

8. In the first quarter of 2024, economic growth was largely explained by stronger than expected domestic demand. Final consumption expanded by 25.6 percent year-on-year, exceeding the gross domestic production for the first time since 2020Q1. The Government of Mongolia introduced hikes in minimum pension, social benefits, and 26 to 50 percent increase in average wages of public workers starting July 1, 2023, which was the key driver of the 47.1 percent increase in government consumption, which supported the 20.1 percent increase in private consumption and activated further domestic demand. Domestic demand is expected to remain strong in the near-term, reflecting policy rate cuts, continuation of state capital spending for big projects, and if macroeconomic stability maintains.

9. Simultaneously, private consumption and saving grew, strengthening demand prospects further. While private consumption saw an increase, private savings, which dropped to MNT 15.0 billion in 2022, reached a record high of MNT 18.8 billion in the first quarter of 2024, increasing by 18.7 percent year-on-year. Also, newly issued individual loans recorded a significant increase of 38.2 percent, reaching MNT 17.0 billion, and fueling private consumption.

Households' consumption of non-food items such as clothing and furniture expanded by 32.1 percent, and spending for services including education, utilities, transport and communication increased by 29.7 percent, while food consumption rose by 3.3 percent, indicating growing consumer confidence. Particularly, in the first quarter of 2024, household transport, accommodation, travel related expenditures significantly increased. Moreover, the number of outbound tourists surged by 64 percent or 220 thousand, which reflects higher propensity to travel during the harsh winter season as well as long holidays throughout the Lunar new year.

10. On a year-over-year basis, real income growth accelerated to 19.8 percent. The burden on household income is likely to ease, reflecting the slowdown in inflation, which remained under the Central bank's target range since the beginning of the year, and stronger MNT against USD. The average household nominal income amounted to MNT 2.4 million as household wage income increased by 21.9 percent. The sizeable government support measures to increase social transfers, public officials' wages, coupled with the 1.0 percentage point year-on-year increase in employment rate supported the household income.

The share of salary in total household income which declined to 48 percent during the pandemic from 54 percent on average during 2018–2019, due to increased social welfare support, rebounded to 57.4 percent by the first quarter of 2024. Wage income is expected to sustain momentum toward the end of the year because of the recent wage increase for public employees that came into effect on April 1st, 2024.

11. In Ulaanbaatar and its suburbs, household real income growth accelerated, while in other areas it decelerated, and income inequality is widening. Overall 983 thousand households registered, around 47 percent of households are in Ulaanbaatar, 21 percent are in other urban areas, and the remaining 32 percent live in the countryside. In urban areas, salary earnings make up 60 percent of households' income, whereas more than half of households' income comes from livestock production in rural areas. Livestock income is vulnerable to weather-related shocks and highly volatile through the seasonal changes. As a way to overcome the Dzud disaster with lower losses, herders substantially butchered their livestock. As a result, meat preparation income temporarily alleviated the burden of herders for the last half of the 2023, and the livestock income started to drop in the first quarter of 2024, reflecting significant contraction in livestock production. Herder families suffer from revenue instability since they lack stable source of wage income.

BOX 2. POVERTY

The household real income and state of poverty were weighed down from the end of 2021 to the second half of 2023 by stubborn inflation, weaker domestic currency due to the geopolitical conflict in line with employment losses due to restrictions on business activities during the pandemic.

In Mongolia, 27.1 percent of the population lived below the national poverty line[1] in 2022, which was 11.7 percentage points lower than in 2010, 1.3 percentage points lower than in 2018, and 0.7 percentage point lower than in 2020, respectively. Global poverty is declining in the long run, however, the pace of reduction is relatively diverse among countries. In 2022, 45.5 percent of the global population is living in poverty, on less than USD 6.85 per day. This indicator accounts 24.7 percent in China, 4.1 percent in Russia, 19.7 percent in Vietnam, 10.6 percent in Kazakhstan and 22.1 percent in Mongolia.[2]

Table I.1 Poverty rate of Mongolia

	2010	2012	2014	2016	2018	2020	2022*
National average	**38.8**	**27.4**	**21.6**	**29.6**	**28.4**	**27.8**	**27.1**
Urban	33.2	23.3	18.8	27.1	27.2	26.5	23.0
Rural	49.0	35.4	26.4	34.9	30.8	30.5	35.6
Regions							
Western	52.7	32.3	26.0	36.0	31.8	31.5	36.5
Khangai	51.9	38.5	25.3	33.6	30.8	31.4	33.5
Central	29.9	28.2	22.2	26.8	26.1	25.2	24.6
Eastern	42.3	33.4	31.4	43.9	37.4	33.3	35.3
Location							
Ulaanbaatar	31.2	19.9	16.4	24.8	25.9	25.4	21.6
Aimag center	37.3	30.4	23.8	31.8	30.1	29.1	26.1
Soum center	39.7	27.5	24.7	32.3	28.9	30.5	30.6
Countryside	56.1	39.6	27.9	38.0	32.9	30.5	41.2

Poverty remains uneven across the country. Somewhat worryingly, poverty worsened in rural areas whereas it is alleviating in urban areas. By 2022, out of every 100 people - in Ulaanbaatar 22 people, in aimag center 26 people, in soum center 31 people, in countryside 41 people are living in poverty. During 2020-22, poverty in the capital city and aimag center decreased, while poverty in soum center and countryside increased. The poverty is even higher in remote areas, where people are more prone to poverty due to a low standard of living, reflecting limited business activities and a lack of engineering supplies such as drinking water supply, internet connections, and heating systems, etc. Livestock income is the main source of income for herder families and highly dependent on weather conditions as mentioned before.

Income inequality is increasing. Economic growth is concentrated in a few sectors and regions, leading to a large development disparity within the country. The far western region had the highest poverty rate of 36.5 percent, whereas the central region had the lowest rate of 24.6 percent, reflecting a greater share of economic activity. Moreover, according to the national HSES-2018, the richest income group has 5.6 times higher earnings than the lowest-income group; in 2022, the ratio increased to 7, indicating increased inequality.

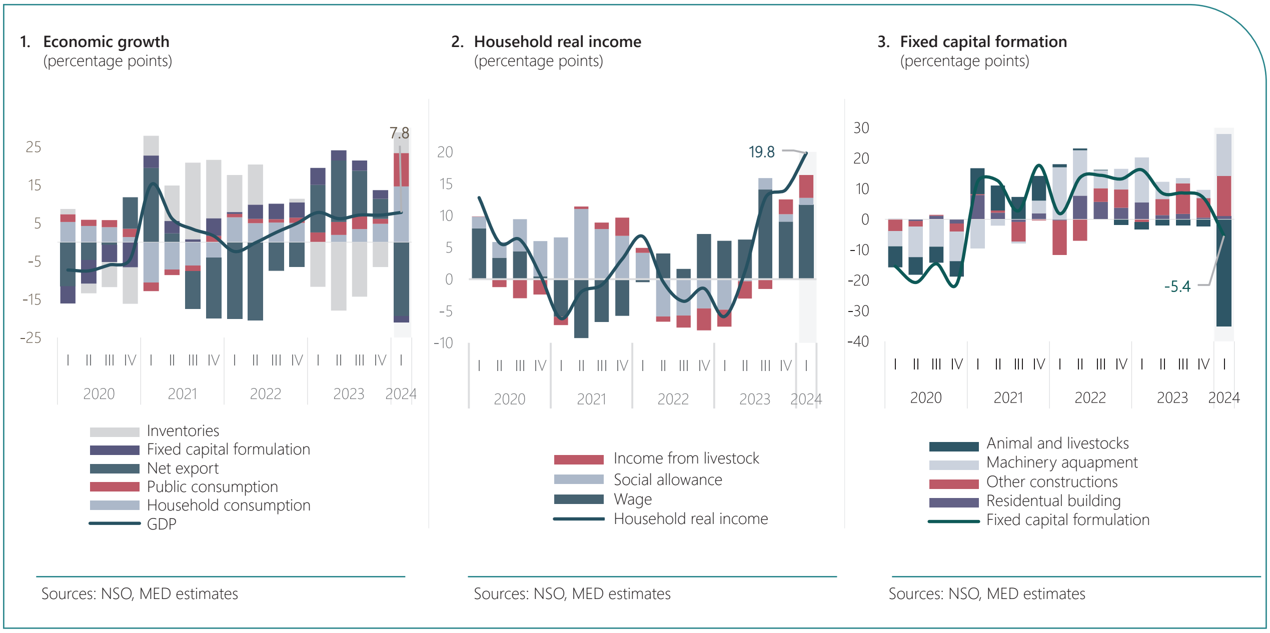
[1] Poverty line is a monetized threshold - determines whether someone is living in poverty through the minimum value of the goods and services needed to sustain one adult. Poverty line in Mongolia, which is 418,090 tugriks in 2022.
[2] USD 6.85 a day in 2017 international (PPP) dollars as per the World Bank and Our World in Data.
* Poverty line 2022 was estimated in accordance with the renewed methodology.

12. Although investment increased, fixed capital formation declined by 5.4 percent due to high loss of livestock. Accumulation in capital formation supports production capacity in the long term. The fixed capital formation includes changes in capital goods stock used to create goods and services, such as residential and non-residential engineering buildings, machinery equipment, adult livestock, and intellectual property. In the first quarter of 2024, loan provision saw a remarkable increase of 37.0 percent, foreign direct investment doubled, and budget investment expanded by 72.3 percent from the previous year. Particularly, in 2024Q1, corporate loan issuance reached MNT 5.2 trillion, up by 42.0 percent, and outstanding corporate loan amounted to MNT 11.5 trillion, increasing by 10.6 percent over a year. As a result, the accumulation of non-residential construction surged by 73.2 percent, residential building increased by 6.4 percent, machinery equipment expanded by 22.1 percent, and stock of intellectual capital doubled in 2024Q1.

Although, the number of livestock declined significantly, as rough dzud weather conditions in majority territory of 14 aimags led to a notable loss of 6.3 million head in adult animals, leading to a contraction in fixed capital formation. The loan provision growth is expected to remain strong, which would support the overall capital accumulation in the medium term.

13. Net exports, led by acceleration in import growth, contributed -19.4 percentage points to overall growth. In the first quarter of 2024, goods imports experienced a notable growth of 24.4 percent, while service imports declined by 3.1 percent. The 30.1 percent year-on-year growth in consumer goods imports, mainly driven by car and fuel imports, was the key contributor of the overall import growth.

Figure I.4 Growth contribution



CHAPTER I

1.3 LABOR MARKET AND BUSINESS

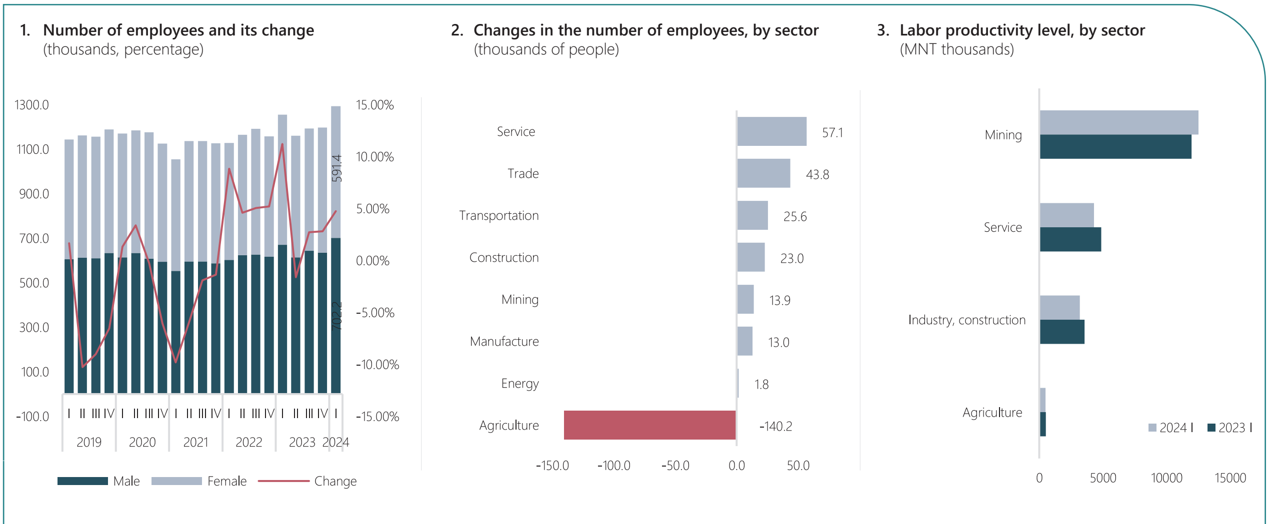
14. Expansion in economic activity supported the labor market. Total employment increased by 3 percent to 1,294 thousand people, while the workforce grew by 2.4 percent to 1,365 thousand in the first quarter of 2024. Subsequently, the labor force participation rate exceeded the expectation by 2.0 percentage points, reaching 59.4 percent.

15. Employment improved throughout the sectors, except agriculture. The number of workers in the trade and service sectors went up synchronously to the activation in those sectors, by 15.2 percent and 31.3 percent, respectively. Also, in parallel with the mining and transportation sectors' growth, employment grew by 20.4 percent and 56.8 percent. However, the number of agricultural workers declined by 31 percent to 312 thousand due to harsh weather conditions.

16. Female labor participation remains low. The number of male employees went up by 32 thousand and reached 702 thousand, while female employees' number increased by 5.9 thousand, totaling to 591 thousand. Activities in the mining, transportation, and manufacturing sectors were stronger than other sector, contributing to the higher growth rate of male employees.

17. Unemployment declined at the national level but went up in rural areas. The unemployment rate fell to 5.2 percent, dropping by 1.4 percentage points from the same period last year, while the number of people outside the labor force decreased by 6.7 thousand to 933.3 thousand. In Ulaanbaatar, employment increased by 73.5 thousand, while unemployment and the people outside the labor force declined by 14.8 thousand and

Figure I.5. Labor market



Source: NSO

Source: NSO

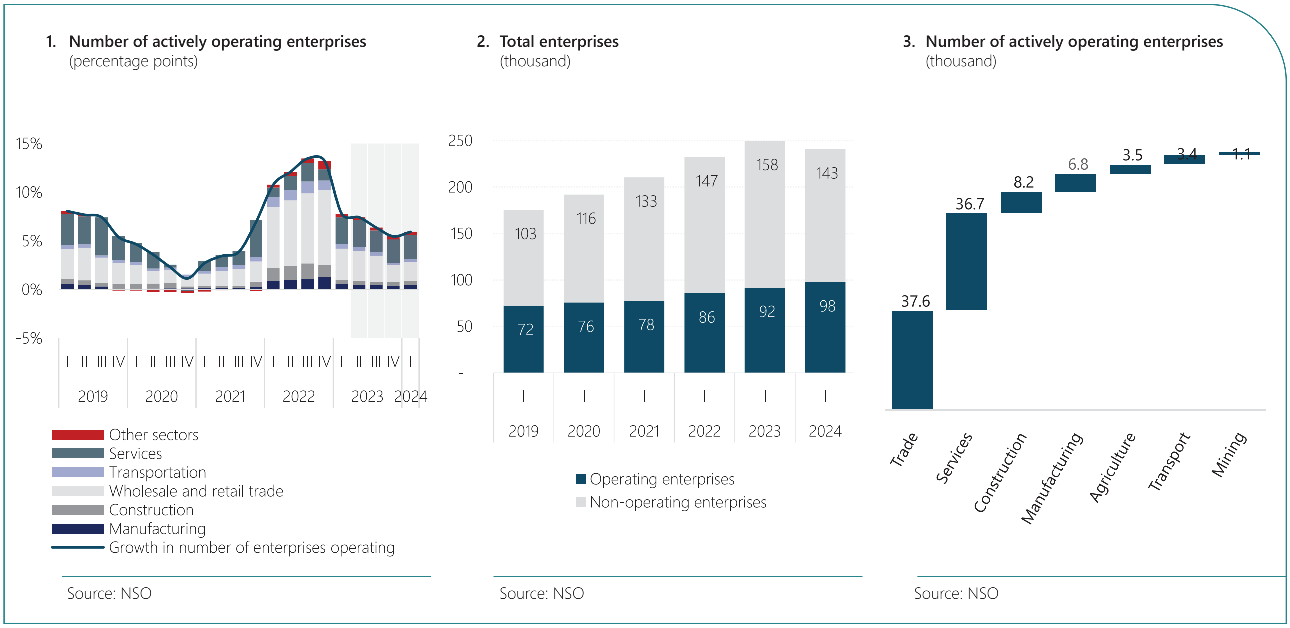
Source: NSO

29.2 thousand, respectively. Conversely, in rural areas, employment decreased by 8.9 thousand, unemployment increased by 9.2 thousand, and the population outside the labor force grew by 22.5 thousand.

18. The labor productivity growth was mainly driven by the mining sector. Labor productivity, measured as gross domestic product per employee, increased by MNT 217 thousand or 5 percent to MNT 4,436 thousand. Mining productivity increased by 4.4 percent, agricultural productivity fell by 3.1 percent, manufacturing productivity worsened by 10.6 percent, and the service sector productivity declined by 11.6 percent, respectively.

19. Business operations strengthened, largely due to domestic activation. As of the first quarter of 2024, there were 97,800 actively operating enterprises, marking a 6 percent increase over a year. As domestic economic activation and purchasing power improved, the number of enterprises operating in the service sector increased by 2.2 thousand. Particularly, the number of enterprises in the wholesale and retail trade sector, which makes up 76 percent of total service sector, increased by 1.8 thousand. The number of actively operating entities in the mining, transportation, agriculture, manufacturing and construction sectors increased by 41, 258, 248, 403 and 454, respectively.

Figure I.6.Bussineses



CHAPTER I

1.4 BUSINESS CYCLE

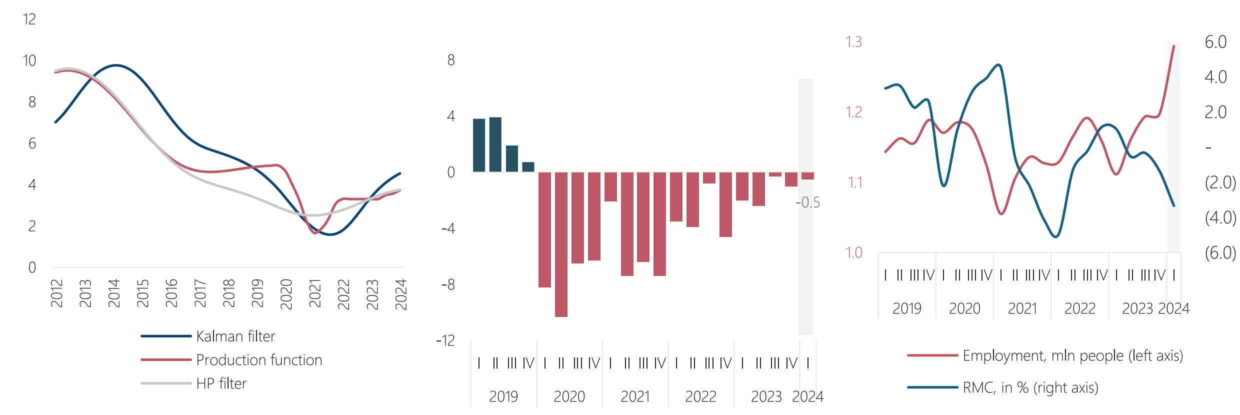
20. The potential output growth sustained momentum, driven by investment growth. Even though overall fixed capital formation contracted due to a sizeable number of adult animal losses, the potential growth remained at around 4 percent, supported by accumulation in other capital stocks, such as machinery and equipment, reflecting improved financing.

21. The negative output gap is approaching zero, reflecting the impact of domestic activity. As a result of domestic economic activity and increase in manufacturing and service sectors, the output is estimated just below its potential level by 0.5 percentage points, and the output gap is gradually narrowing.

22. A decline in real marginal costs of production, narrowing negative output gap and domestic currency appreciation, is spurring business activities. The real marginal cost is the cost of using an additional unit of labor or imported and domestically produced intermediate goods that are used in production. There is a negative correlation between the cost of production and the number of employees. For example, a fall in cost of production will create an incentive for manufacturers to hire additional employee[2]. In the first quarter of 2024, MNT appreciated by 3 percent compared to the same period last year, and industrial inputs' import increased by 26 percent. Consequently, the real marginal cost of production decreased by 3.3 percent, the number of operating enterprises increased by 5.9 percent, and the number of employees increased by 3.0 percent year-on-year.

Figure I.7. Output gap

1. **Potential output growth** (percentage)
2. **Output gap[3]** (percent of potential output)
3. **Employment[4] and RMC (real marginal cost)** (left axis: million people, right axis: percent)



Source: Estimation of the MED
Note: Potential output growth is calculated by 3 different approaches HP filter, Kalman filter and Production function

Source: Estimation of the MED
Note: Output gap is calculated by Production function.

Source: Estimation of the MED
Note: RMC is evaluated from the GAP model of Monetary Policy Analysis.

[2] According to the study of (Gali Jordi 1999), (Argia 2002) found empirical evidence that in USA and Euro area are the fit of the NKPC is good if use labor share (real unit labor cost) as the proxy for real marginal cost (RMC).
[3] The difference between actual GDP or actual output and potential GDP
[4] Calculated by methodology for Indicators of Labor Statistics (Order A-09/A-08, Chairperson of NSO and Minister of Foreign Affairs 08 on January 17, 2019)

BOX 3. RELATIONSHIP BETWEEN REAL MARGINAL COST (RMC) AND EMPLOYMENT

The Philips curve

Inflation indicates changes in the general level of prices of goods and services, while employment /number of employed persons/ refers to actively participating people in the labor market. The relationship between these two variables is broadly studied. Among prominent economic theories, the Phillips curve is notable, representing an inverse relationship between inflation and unemployment over business cycles. The Phillips curve reflects the labor market by assuming nominal variables rigidities (price and wage are sticky). Wolman (1999) suggested a concept that *"continued progress in the empirical evaluation of sticky-price models will require intensive study of the factors determining real marginal cost. With more refined estimates of real marginal cost, it may be possible to reconcile a plausible sticky-price specification with data on inflation"* in the NKPC (New Keynesian Phillips curve).

Real marginal cost and employment[1]

There are numerous empirical studies on the real marginal cost, among which the study by the Central bank of Japan, "Estimating a New Keynesian Phillips Curve with a Corrected Measure of Real Marginal Cost: Evidence in Japan" is selected as a basis of this analysis. The study represents the NKPC in the presence of two kinds of labor market frictions (i) labor adjustment costs and (ii) real wage rigidity, and labor adjustment costs are considered as a change in the number of workers.
Since the relationship between the real marginal cost of production and changes in the number of workers is studied on the theoretical side and proved by empirical evidence, a correlation analysis was conducted between number of workers and the changes in real marginal cost[2]. Thus, the analysis will help us better evaluate macroeconomic conditions through inflation and employment and identify sectors that rely more on capital than labor and how much depends on imports and real exchange rates.

Result of the analysis

Marginal cost of production is a variable that represents a change in the total cost of domestic and imported goods and services. In Mongolia, change in RMC (real marginal cost) and number of employments have a strong inverse linear relationship of -64 percent[3]. The following sectoral estimates determine the relationship between changes in employment and changes in RMC and aim to investigate the labor market prospect regarding macroeconomic outlooks such as the real exchange rate gap and output gap. The results suggest that sectors including construction, transportation, mining, processing, accommodation, and catering services, information and communication, and education have a high sensitivity. In other words, the number of jobs in these sectors, where more than 35 percent of total employees' work, is highly dependent on exchange rate changes.

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[1] Persons in employment are defined as all those of working age who, during a short reference period, were engaged in any activity to produce goods or provide services for pay or profit.

[2] Real marginal cost is calculated by the real exchange rate gap and output gap and evaluated from the the GAP model of Monetary Policy Analysis (developed by IMF economists suggested to monetary policy analysis and forecasting)

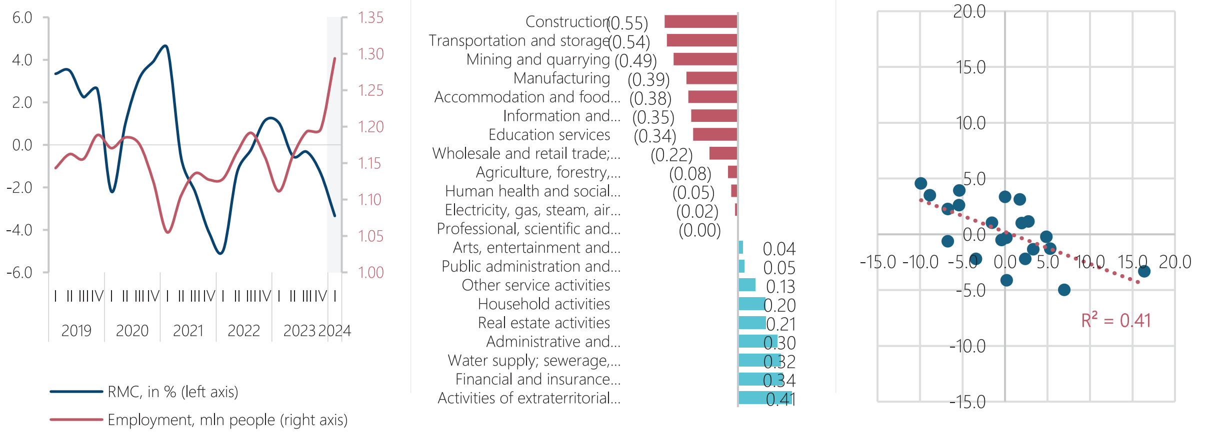
[3] Estimation made on series ranged from the 1st quarter of 2019 to the 1st quarter of 2024.

Figure I.8. Relationship between real marginal cost and employment

1. Real marginal cost and employment dynamic (million people: right axis, percent: left axis)

2. Correlation coefficient of RMC and employment change (between -1 to 1)

3. Scatter plot of change in RMC and employment (percent)



Source: Estimation of the MED
Note: RMC is evaluated from the GAP model of Monetary Policy Analysis.

Source: Estimation of the MED
Note: The correlation coefficient was calculated from the first quarter of 2019 to the reporting quarter

Source: Estimation of the MED

CHAPTER II

FISCAL SECTOR

II. FISCAL SECTOR

OVERVIEW

Increased economic activity positively contributed to the budget revenues, leading to a budget surplus of MNT 1.6 trillion in the first quarter of 2024. Budget expenditures are directed towards safeguarding household income and improving social security for citizens. The government debt-to-GDP ratio, expressed in current values, decreased to 33.7 percent as of the first quarter of 2024, adhering to the limit specified in Article 6.1.4 of the Law on Budget Stability.

CHAPTER II

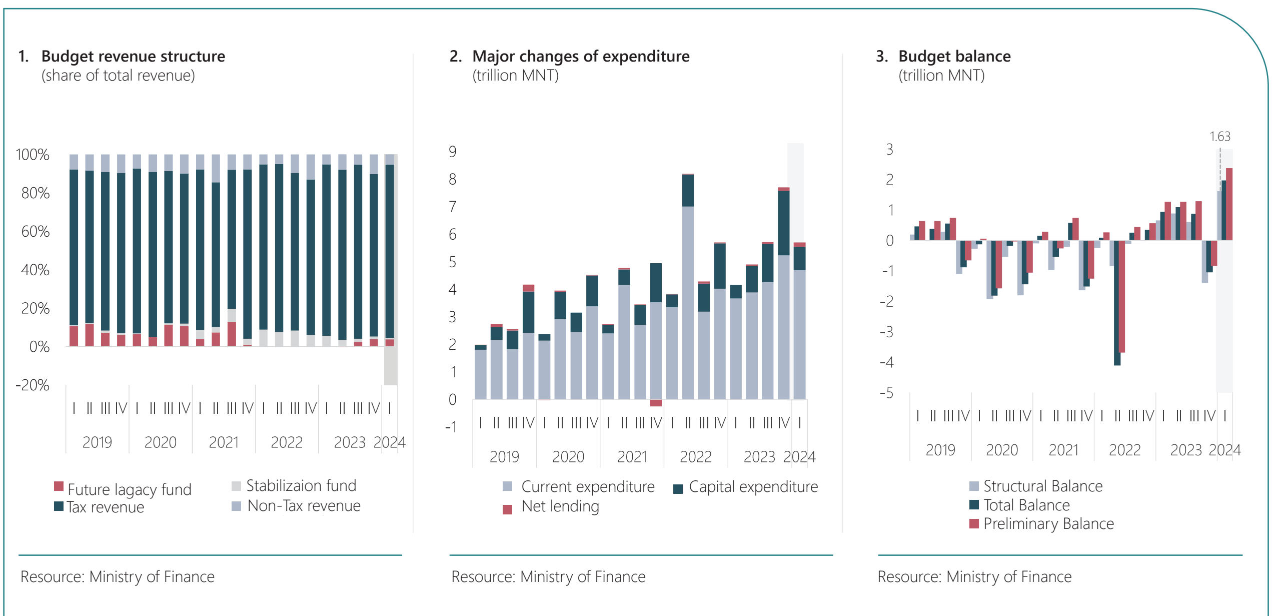
2.1 FISCAL POLICY

23. Due to the positive effects of strong domestic demand and increased mining production, budget revenues rose, resulting in a budget surplus. In the first quarter of 2024, the consolidated budget recorded a surplus of MNT 1.6 trillion, an increase of MNT 970 billion or 47.7 percent from the same period last year. Total budget revenue increased by 51.3 percent compared to the same period last year, significantly contributing to the budget surplus.

24. Budget revenues surged reflecting robust economic activity. The total consolidated budget income reached MNT 7.673 trillion in the first quarter of 2024, achieving 98.1 percent of the planned target. Continued economic activity, increased household real income, higher consumer spending, and improved business activity led to MNT 2.4 trillion or 52.3 percent increase in tax revenue, which was the main driver of the rise in budget revenue. Particularly, personal income tax (PIT) increased by MNT 165 billion or 44.7 percent, and corporate income tax (CIT) increased by MNT 985 billion or 88.3 percent. Additionally, the revenue collected by the royalty on mineral resources (AMNAT) increased by MNT 533 billion to MNT 1.1 trillion reflecting higher export volumes. The total budget revenue in 2024 is projected to be MNT 27.7 trillion, with balanced revenue estimated at MNT 25.9 trillion.

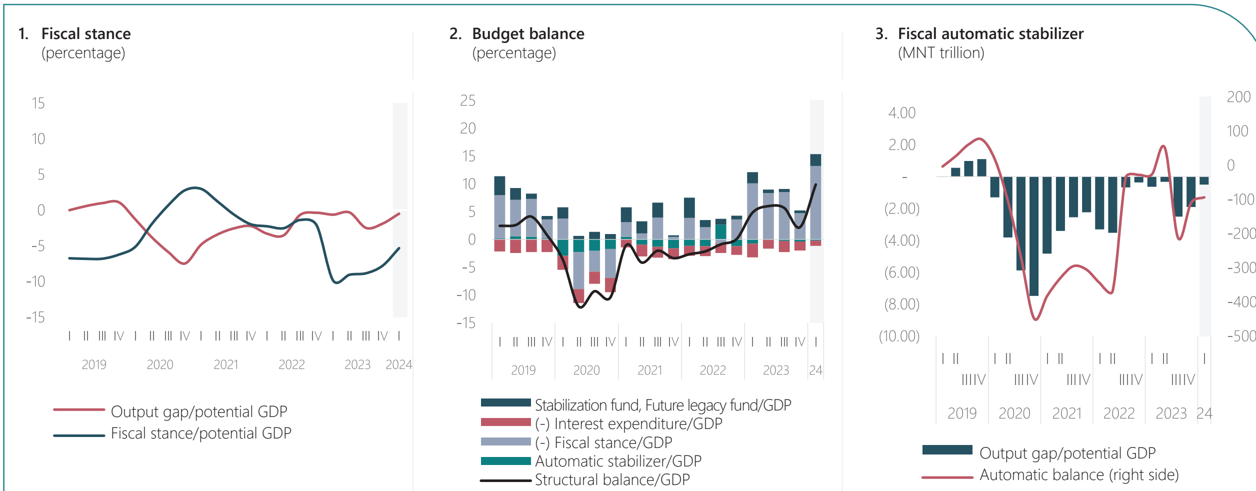
25. Budget expenditures aim at protecting household income and improving social security for citizens. As part of the government's policy to extend economic growth to every household and increase real income, child benefits are being provided to every child, and wages and pensions were increased on July 1, 2023, and government employee wages was adjusted for inflation on April 1, 2024. Consequently, as of the first quarter of 2024, salary expenses increased by MNT 624 billion or 2.4 times from the same period last year, and pension and benefit expenses increased by MNT 235 billion or 26.4 percent from the same period last year. The total current expenditure of the 2024 budget was approved at MNT 21.2 trillion,

Figure II.1 Budget revenue, expenditure and balance



and 35.9 percent is allocated to social insurance and welfare pensions and benefits, 25.3 percent to salaries and wages of government employees, 11.7 percent to ensuring the normal operation of public institutions, 7.3 percent to child allowances, 2.9 percent to discounts and exemptions granted by the government to citizens and enterprises, 5.5 percent to foreign and domestic loan interest payments, and 1.6 percent to current expenses in the health and education sectors financed by performance.

Figure II.2 Fiscal stance, budget balance, fiscal automatic stabilizer



Source: MED estimation

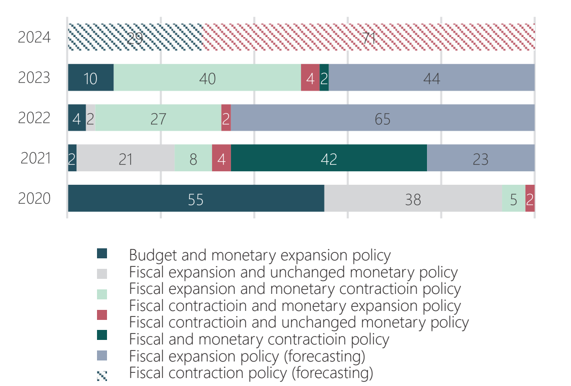
Source: MED estimation
Note: Positive values of interest expenditure and fiscal stance add to the budget deficit, so the values are multiplied by -1 for clarity.

Source: MED estimation

26. Fiscal stance indicates a contractionary fiscal policy. The cyclically adjusted primary balance was estimated at a surplus of MNT 2.2 trillion, indicating a contractionary fiscal policy. The automatic stabilizer reached MNT 38.6 billion (0.23 percent of GDP) while interest payments totaled MNT 154 billion (0.9 percent of GDP). The fiscal stance, representing discretionary fiscal policy, was at MNT -2,171 billion or -13.19 percent of GDP. The automatic stabilizer increased by MNT 65.4 billion from a year earlier, reflecting the positive impact of the economic cycle on budget balance.

27. According to the IMF's estimate, in 2024, the primary budget balance of most countries is expected to be in surplus. The fund estimates that 71 percent of all countries will implement tight fiscal policies.

Figure II.3 Monetary and fiscal policies
(percentage share)



Source; IMF, Fiscal Monitor
Note: 34 developed countries and 20 developing countries were included in the calculation. Positive (negative) cyclically-adjusted primary balance indicated contractionary (expansionary) fiscal policy. A hike (cut) in the policy interest rate indicates tighter (looser) monetary policy.

CHAPTER II

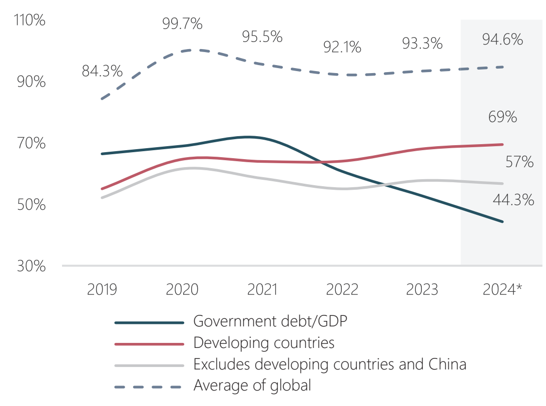
2.2 GOVERNMENT DEBT SUSTAINABILITY

28. The outstanding balance of government debt decreased by 10.9 percent from the same period of the previous year, reaching the lowest level in the last seven quarters. The government's total debt at the end of the first quarter of 2024 was MNT 29.8 trillion, down by MNT 3.6 trillion from the same period last year. The government debt-to-GDP ratio, expressed in current value, reached 33.7 percent, a decrease of 4.9 percentage points from the end of 2023. The reduction in government debt was positively influenced by decreases in external debt of 5.3 percent, domestic debt of 1.9 percent, and contingent liabilities of 2.2 percent. Compared to the end of 2023, foreign debt decreased by MNT 732 billion, or 2.4 percent, and domestic debt decreased by MNT 37.5 billion, or 16 percent. Also, the build-transfer type concession liabilities of MNT 236.5 billion, were fully settled as of the first quarter of 2024.

29. The successful repayment of foreign bonds was the primary factor in reducing the government's total debt. The government's foreign debt decreased by 3.3 percent compared to the end of the previous year, as foreign bond payments decreased by MNT 439 billion and foreign loans decreased by MNT 63 billion. As part of the debt management measures, the remaining USD 53 million of the Khuraldai bond, was fully repaid in March 2024, significantly reducing the outstanding balance of the foreign securities debt. The state budget allocated MNT 204 billion for interest payments of government securities and MNT 196 billion for interest payments of foreign loans. The latest international bonds including Nomad, Century-1, Century-2, and Century-3 are all issued for debt refinancing. As of the first quarter of 2024, the government's foreign debt constituted 22.8 percent of Mongolia's total foreign debt, down 1.8 percentage points than the same period last year.

30. The nominal government debt-to-GDP ratio is lower than the average of other countries. Specifically, the ratio of the government's nominal balance of foreign currency debt to GDP is below the average for developing countries. For example, in 2019, the ratio of Mongolia's nominal government debt balance to GDP was 68.1 percent, compared to 55 percent for developing countries. By 2023, the average for developing countries rose to 68 percent, while Mongolia's ratio decreased to 51.9 percent. This indicator tends to be higher for developed countries and lower for developing and low-middle-income countries. As of 2023, the share of the nominal balance of government debt to GDP in developed countries is 93.3 percent, while according to the IMF's criteria, it is 53.2 percent for low-income countries.

Figure II.4 Nominal balance of government debt (percentage of nominal GDP)



Source: Ministry of Economy estimation, IMF
Note: The above indicator is the amount calculated by weighting the nominal balance of the government's debt expressed in foreign currency to the nominal GDP expressed in US dollars.
*For 2024: For Mongolia, the balance of the government debt in the first quarter of 2024 is calculated by comparing it with the MED's GDP forecast for 2024, and for other countries, it is calculated based on the IMF forecasts.

BOX 4. LAW ON BUDGET FRAMEWORK FOR 2025, AND BUDGET PROJECTIONS FOR 2026-2027

The Law on Mongolia's budget framework for 2025, and budget projections for 2026-2027 was approved by the Parliament on June 5, 2024. The law was developed within the policy objectives that includes:

- To maintain stable economic growth of more than 6 percent.
- To reduce inflation to approximately 3 percent in the medium term to enhance economic competitiveness and boost households' real income.
- To boost export income and bring gross international reserves to USD 10 billion in 2026.
- To lower the budget balance-to-GDP ratio to -2.0 percent in 2025, -1.5 percent in 2026, and -1.0 percent in 2027, with a policy of maintaining budget balance in surplus thereafter.
- To gradually reduce the ratio of the present value of government debt-to-GDP to 50 percent in 2025, 45 percent in 2026, and 40 percent in 2027.

In addition, the medium-term budget framework statement fully complies with the special budget requirements specified in the Law on Fiscal Stability and other related laws.

Table II.1. Law on Mongolia's budget framework for 2025, and budget projections for 2026-2027

№	Main indicators of economic	Budget framework statement	Projections	
		2025 он	2026 он	2027 он
1	Real growth rate of GDP /percentage/	8.0	6.5	6.5
2	The rate of increase in consumer prices	6.0	4.0	3.0
3	Consolidated budget structural revenue/MNT billion/	29,400.1	31,951.2	34,460.3
	- Share of GDP	30.9	30.5	29.5
4	The maximum amount of the total expenditure of the consolidated budget /MNT billion/	31,300.4	33,521.8	35,628.1
	- Share of GDP	32.9	32.0	30.5
5	The increase in the total expenditure of the consolidated budget	3,939.9	2,221.4	2,106.3
	- Share of GDP	4.1	2.1	1.8
6	Structural balance of the consolidated budget	-1,900.3	-1,570.6	-1,167.8
	- Share of GDP	-2.0	-1.5	-1.0
7	Capital expenditure of the consolidated budget /MNT billion/	7,273.3	7,564.2	7,866.8
	- Share of GDP	7.7	7.2	6.7
8	The total amount of government debt, in present value /MNT billion/	47,507.1	47,117.6	46,708.6
	- Share of GDP	50.0	45.0	40.0
9	According to the Law on Social Welfare, the total amount of expenses to be financed from the budget /MNT billion/	2,850.4	2,931.8	3,269.6
	- Share of GDP	3.0	2.8	2.8

CHAPTER III

MONETARY SECTOR

III. MONETARY SECTOR

OVERVIEW

The inflation rate remained within the Bank of Mongolia's target band as both domestic and import price growth moderated. As of June 2024, the Central Bank cut the policy rate twice by a total of 2 percentage points, bringing the policy rate to 11 percent. Disinflation, along with higher real interest rates and a stable exchange rate, boosted households' real income and contributed to the increase in total savings. Due to the increased credit resources of commercial banks, the amount of newly issued loans to individuals and enterprises increased and capital adequacy and profitability indicators improved. In the future, to mitigate inflation, measures aimed at ensuring comprehensive reforms in the agricultural sector, enhancing food supply, streamlining export and import regulations, boosting foreign exchange reserves, and constraining the budget deficit, will be implemented.

CHAPTER III

3.1

INFLATION AND MONETARY POLICY

31. As of the first quarter of 2024, in line with the previous projections, the inflation rate decreased and fell within the central bank's target range. The average annual inflation rate was at 7.2 percent, marking a decrease of 5.0 percentage points compared to the same period last year.

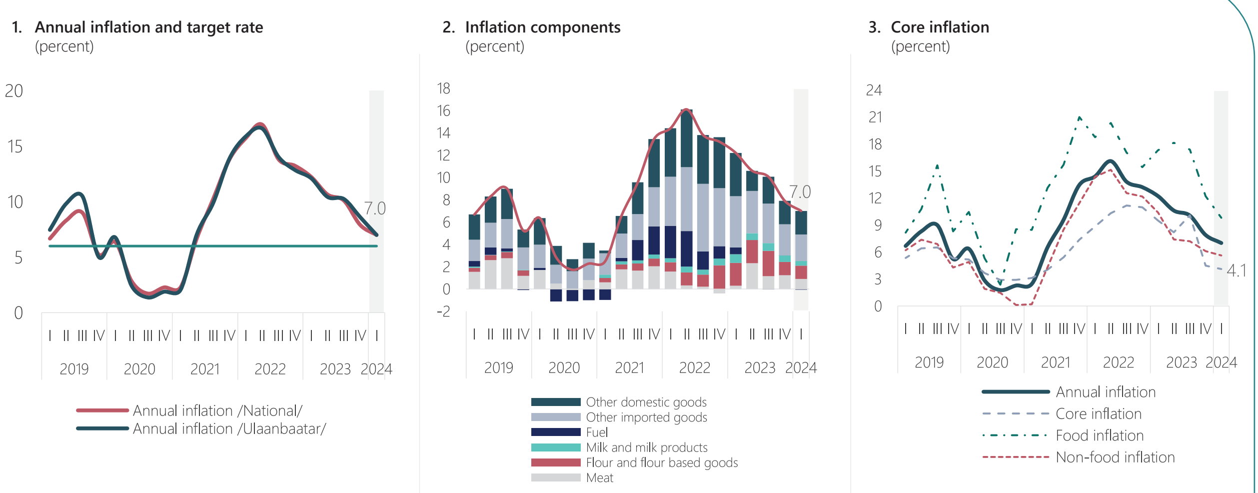
32. In the first quarter of 2024, the annual inflation rate was 7.0 percent, down 5.2 percentage points compared to the same period last year. The decline in inflation was attributed to the following group of goods and services: 1.9 percentage points to food and non-alcoholic beverages, 0.8 percentage point to clothing, footwear, and cloth, 0.9 percentage point to housing, water, electricity, and fuels, 0.4 percentage point to furnishings, household equipment, and tools, 1.0 percentage point to transport.

33. Reflecting economic recovery, demand-driven inflation accounted for 4.1 percent of annual inflation, and supply-driven inflation accounted for 2.9 percent. Demand-driven inflation accounted for about 60 percent of total inflation due to the increase in pensions, allowances, government employees' salaries, and strong household consumption, and resilient domestic demand.

34. The contribution of imported and domestic goods to annual inflation declined by 2.8 and 2.4 percentage points, respectively, compared to the same period last year. The basket for consumer price index at the national level covers the price of 410 items collected. Out of 410 selected items of goods and services, 220 items were imported goods, which account for 46 percent of the total weight and 190 items were domestic goods which account for 54 percent of the total weight. Inflation from imported goods accounted for 34.1 percent of the annual inflation. The stable exchange rate, disinflation in other countries, and reduced transportation costs mainly contributed to the decrease in inflation from imported goods. The decrease in inflation from domestic goods and services was mainly attributed to 1.9 points to food and non-alcoholic beverages, and 0.3 to restaurants and hotels.

35. Food inflation contributed 2.8 percentage points, and non-food inflation contributed 4.2 percentage points to total inflation. The food group's

Figure III.1 Inflation



Source: National Statistics Office
Note: Quarterly inflation rates are calculated from the last months of the quarter.

Source: National Statistics Office
Note: The components of annual inflation are shown by goods and groups with high contributions to inflation

Source: National Statistics Office
Note: Core inflation is calculated by subtracting food, fuel, and solid fuel from total inflation

price increased by 9.8 percent in the first quarter of 2024. The price increase of the main food products remains high as prices of flour and flour-based goods increased by 17.4 percent, meat by 10.9 percent, and dairy products and eggs by 10.6 percent. The increase in the prices of these products accounts for about 60 percent of food inflation.

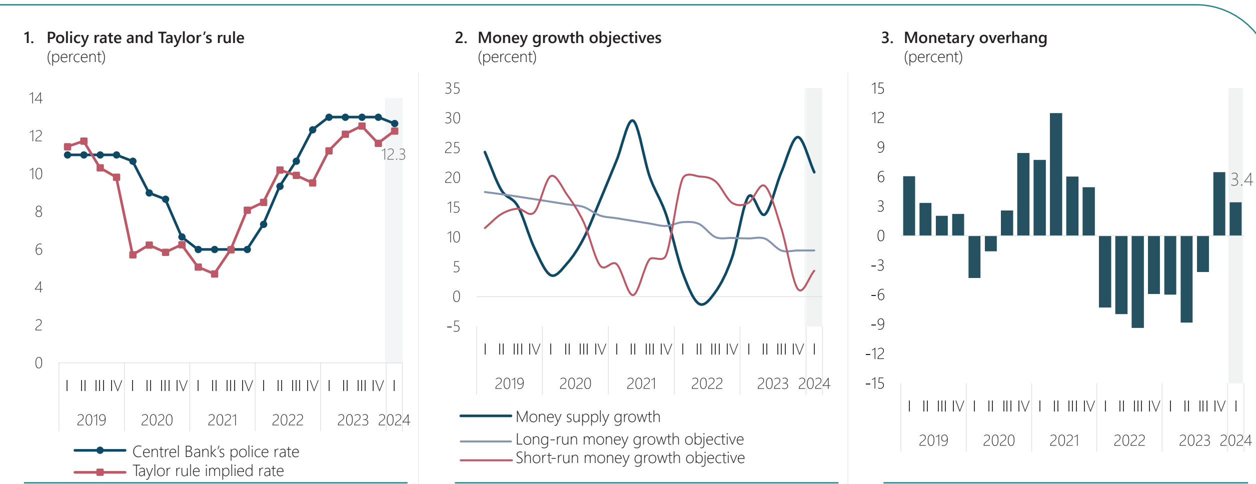
36. The annual inflation rate in Ulaanbaatar dropped by 5.1 percentage points, reaching 7.0 percent. The annual inflation rate in Ulaanbaatar declined as price growth of most item groups slowed. The food group inflation decreased by 6.3 percentage points to 9.3 percent, and the transport group had a deflation of 0.6 percent, which was the main driver of the disinflation in Ulaanbaatar. The price of AI-92 fuel remained stable, while AI-80 fuel price decreased by 0.5 percent, and diesel price decreased by 6.8 percent from the same period last year. On the other hand, the price of education services increased by 21.2 percent in autumn 2023, which contributed 0.5 percentage points to Ulaanbaatar city's inflation.

37. The latest surge in global container shipping and food prices increases inflationary pressures. The cost of international shipping soared as businesses prepared to ship goods for the festive season far earlier than usual and disruption from attacks in the Red Sea continued. The World Container Index (WCI) increased by 202 percent from a year earlier to $4801 per 40 ft container, which is 187 percent higher than the pre-pandemic average. As of May 2024, the FAO Food Price Index (FFPI) increased slightly from the previous month but remained down 3.4 percent compared to a year earlier, as increases in the price indices for cereals and dairy products offset decreases in those for sugar and vegetable oils, while the meat price index remained largely unchanged. Inflation decreased in most trading partner countries. Particularly, as of April 2024, inflation in the Eurozone, United States, Great Britain, Japan, South Korea, Sri Lanka, Kazakhstan, and Kyrgyzstan receded while inflation in Russia, China, Georgia, and Turkey's accelerated.

38. The policy rate is at an appropriate level in line with the current state of the economy. The Central Bank cut the policy rate by two percentage points to 11 percent in 2024. The policy interest rate calculated by the Taylor rule was at 12.3 percent in the first quarter of 2024, which is close to the Central Bank's policy rate of 12.7 percent. It is important not to ease monetary policy too early or too fast as rising credit growth and price spikes of imported goods due to the delays in transport pose risks to the disinflation process.

39. Money supply growth was above the short-run money growth objective for the past 3 quarters. In the first quarter of 2024, the monetary overhang was estimated at 3.4 percent, suggesting that the short-run money growth objective was higher than the long-run money growth objective. The monetary overhang decreased from the previous quarter but was greater than zero, indicating that the money supply was higher than the equilibrium level.

Figure III.2 Taylor's rule, money growth objectives, money overhang



Source: National Statistics Office, MED estimation
Note: The implied rate calculated by Taylor's rule represents the appropriate value of the central bank's policy rate and is an equation containing variables such as the policy rate set in the previous quarter, inflation, expected inflation, nominal interest rate, and a fixed coefficient.

Source: Bank of Mongolia, MED estimation
Note: The long-run money growth objective is calculated by the sum of the targeted inflation rate and the difference between the GDP growth trend and the money velocity. The difference between the long-run money growth objective and the monetary overhang determines the short-run money growth objective.

Source: MED estimation
Note: Monetary overhang determines whether the money supply in the market is at an appropriate level, and a value greater than 0, in this case 3.4 percent, indicates the need to reduce the money supply.

CHAPTER III

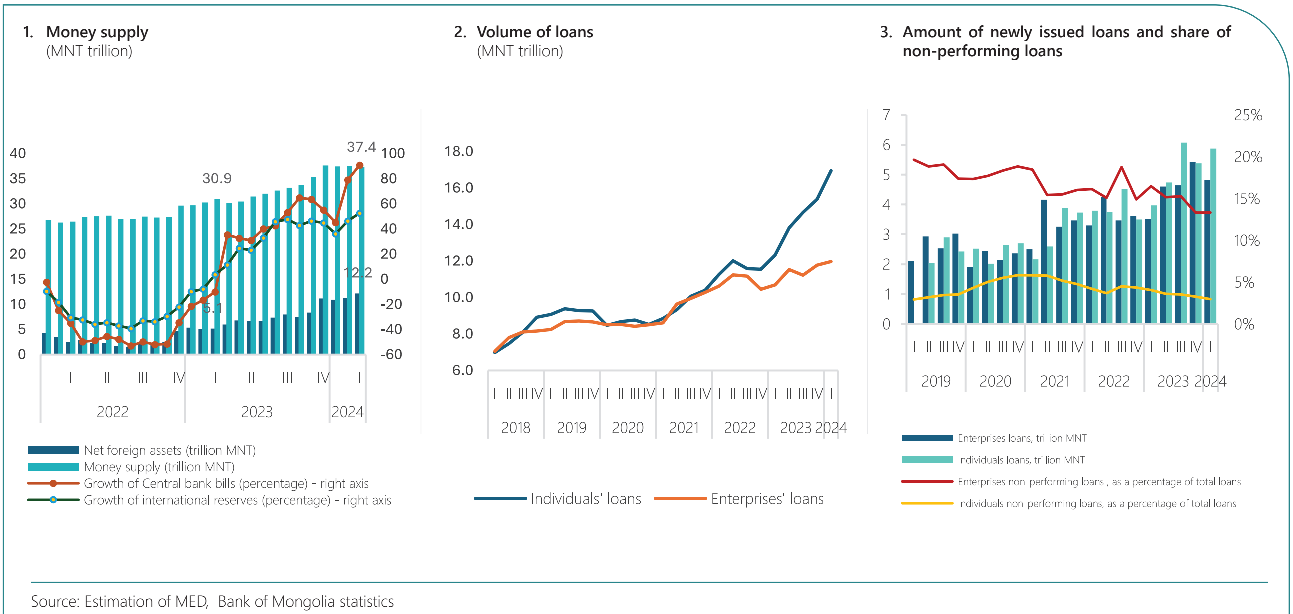
3.2 FINANCIAL SECTOR

40. Money supply increased due to increased net foreign assets, driven by improvements in the balance of payments. By the end of the first quarter of 2024, the money supply reached MNT 37.4 trillion, marking a 20.9 percent increase from the same period last year. Particularly, domestic currency deposits grew by 16.3 percentage points, and domestic current accounts by 9.5 percentage points. In contrast, foreign currency deposits decreased by 4.7 percent and foreign currency current accounts by 0.4 percent. The growth in net foreign assets and increased lending associated contributed to the expansion of the money supply.

41. The commercial banks' loans increased. As of the first quarter of 2024, the total outstanding balance of loans extended by commercial banks reached MNT 28.9 trillion, marking a growth rate of 25.7 percent year-on-year. Within this total, normal loans amounted to MNT 25.6 trillion, recording a significant 32.0 percent increase from the same period last year. During the first quarter of 2024, banks slightly eased the criteria for car and consumer loans while maintaining standards for other types of loans. Household consumer loan debt increased sharply to MNT 374.1 billion, more than doubling from the previous year. Additionally, pension loans amounted to MNT 1.4 trillion, increasing by 57.7 percent year-on-year, salary loans totaled MNT 4.6 trillion, up by 43.1 percent, and herder's loans reached MNT 1.4 trillion, rising by 15.6 percent.

42. Newly issued loans increased. In the first quarter of 2024, the amount of newly issued loans reached MNT 11.7 trillion, representing an increase of 36.9 percent or MNT 3.1 trillion. Breaking down the growth of newly

Figure III.3 Money supply and credit indicators



Source: Estimation of MED, Bank of Mongolia statistics issued loans by sector, the trade sector accounted for 3.1 percentage points, salary loans accounted for 5.5 percentage points, deposit-backed loans accounted for 4.3 percentage points, financial and insurance sector loans accounted for 3.8 percentage points, while mining sector loans accounted for 2.2 percentage points.

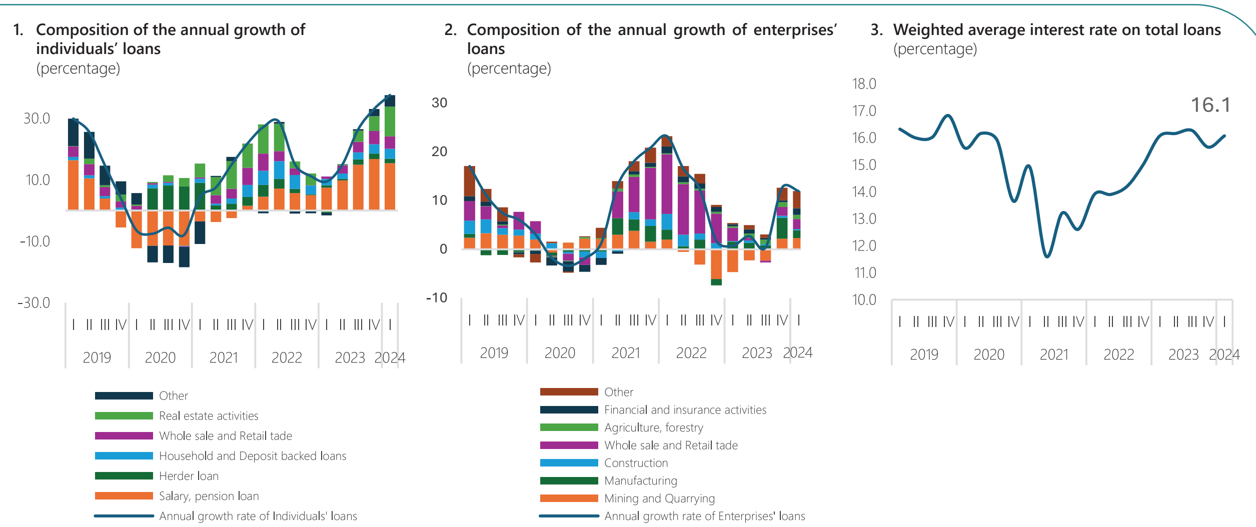
43. The share of non-performing loans in total loan decreased. As of the first quarter of 2024, the total amount of non-performing loans reached MNT 2.1 trillion, accounting for 7.1 percent of the total loan balance. The amount of non-performing loans decreased by MNT 167.0 billion from the same period last year, and the share of total loans decreased by 2.5 points from the same period last year. The reduction in non-performing loans is expected to positively affect economic growth and the stability of the financial sector.

44. Disinflation, higher real interest rates, and the stability of the exchange rate supported the real income of households and contributed to the growth of total savings. The bank deposits increased to MNT 22.4 trillion in the first quarter of 2024, increasing by 18.9 percent from the same period last year. Individuals' savings accounted for 83 percent of the total savings, while enterprises' savings accounted for 17 percent. Deposit growth and deposit interest rates are positively related on the supply side. The interest rate on deposits rose to 11.8 percent in the first quarter of 2024, marking a 1.2 percentage points increase from the same period last year. The combination of relatively stable price level and the increase in deposit interest rate had a significant impact on the overall growth of total deposits.

45. The spread between deposit and loan interest rates narrowed compared to the same period last year. Commercial banks interest rate increased by 0.3 percentage points from the same period last year to 17.0 percent, and the amount of loans increased, which improved the profitability of banks. In the short term, a reduction in the difference between deposit and loan interest rates has a positive effect on stimulating economic activity.

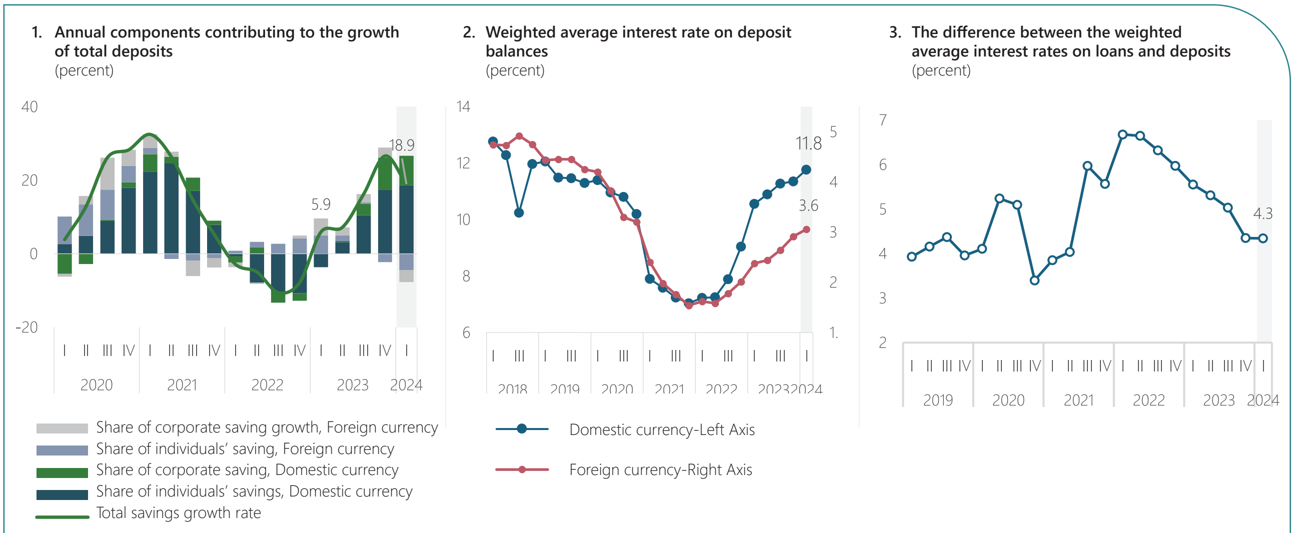
46. The improvement in asset quality due to the decrease in non-performing loans had a positive effect on the profitability of banks. As of the first quarter of 2024, banks' return on assets averaged 2.45 percent over the past six quarters, which is 3.6-fold higher than the average in 2020 and 1.8-fold higher than the average in 2021. For banks, profitability is inversely related to non-performing loans. The increase in interest income had a positive effect due to the decrease in non-performing loans and the increase in normal loans.

Figure III.4 Components of annual loan growth and indicators of interest rates



Source: Estimation of MED, Bank of Mongolia statistics.

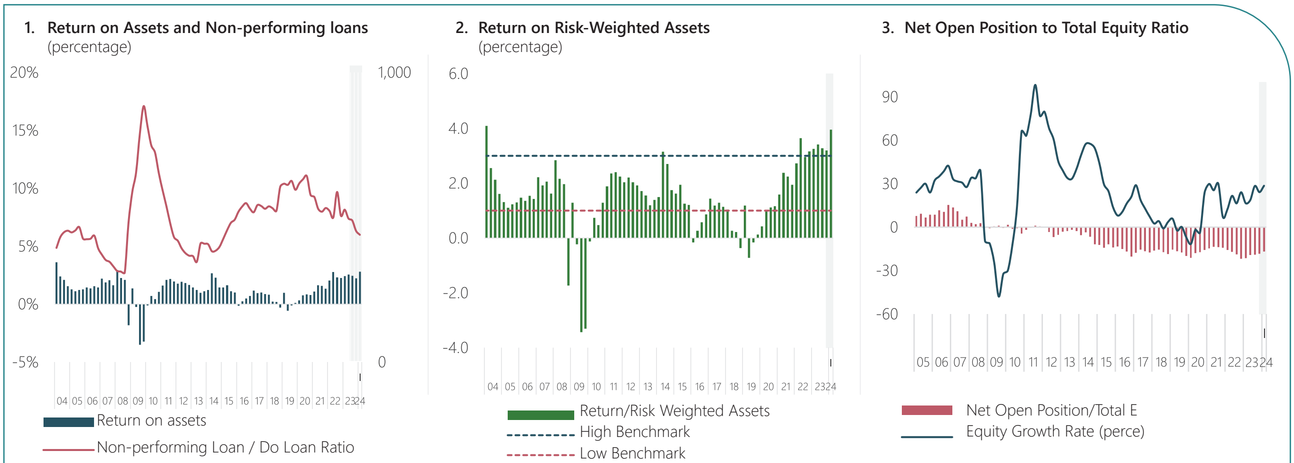
Figure III.5 Components of annual growth in total deposits and indicators of deposit interest rates



Source: Estimation of MED, Bank of Mongolia statistics.

47. The capital growth of commercial banks increased, and exchange rate related risk alleviated. On January 29, 2021, an amendment to the Banking Law required systematically important banks to operate as an open joint-stock company, and other banks to adopt the form of joint-stock companies. Following this legal change, major banks went public and in the first quarter of 2024, the capital growth of commercial banks reached 28.6 percent, up 12.1 percentage points compared to a year earlier. The ratio of net open positions to total equity decreased by 4.6 percentage points in absolute terms compared to the same period in the previous year, reducing banks' exposure to currency fluctuations.

Figure III.6 Profitability and prudential ratios



Source: Bank of Mongolia, MED estimate
Notes :Net Foreign Assets = Foreign Assets - Foreign Liabilities
Return on Assets = Profit (loss) for the reporting year / Total assets

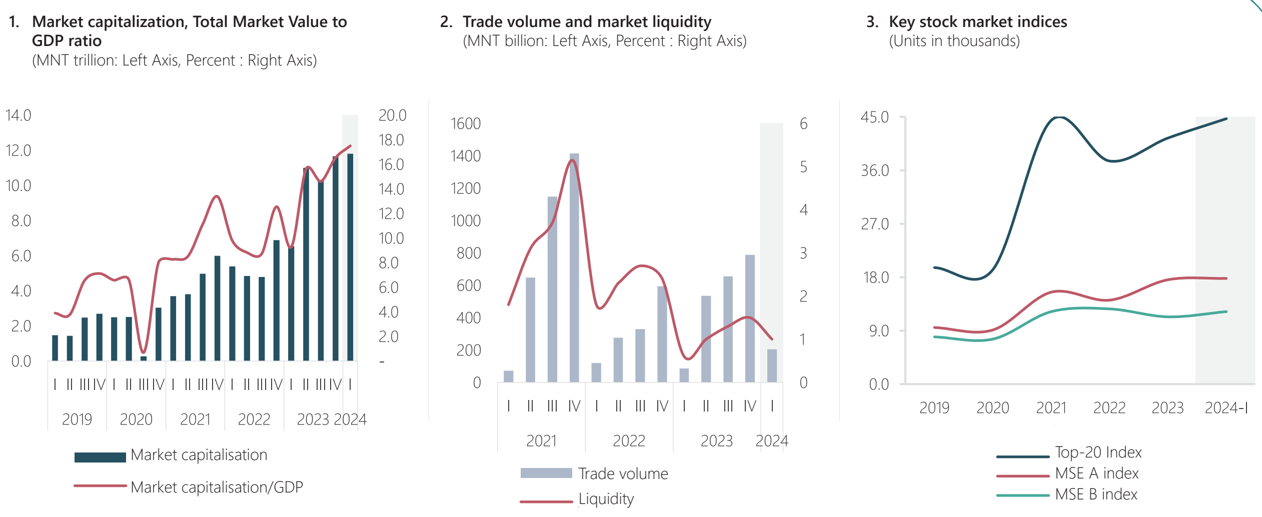
Source: Bank of Mongolia, MED estimates
Note: A lower Return on Risk-Weighted Assets (RORWA) benchmark below 1 percent suggests that the bank's profitability may not align with the expected risk, indicating potential inefficiencies in asset allocation or risk management. Conversely, an upper benchmark exceeding 3 percent indicates that the bank is achieving high profitability relative to the risk it has assumed.

Source: Bank of Mongolia, MED estimates
Notes: The net open position is calculated as foreign currency assets minus Foreign currency liabilities.
A high ratio of net open position to total equity indicates significant exposure of a bank or financial institution to foreign currency risk.

48. The stock market expanded. In the first quarter of 2024, the stock market capitalization reached MNT 11.8 trillion, marking a 1.8-fold increase from the previous year. The overall stock market valuation represents 17.5 percent of the GDP. Recent improvements in the capital market's value and trading activity are attributed to banks' initial public offerings. Securities trading in the first quarter of 2024 totaled MNT 204.9 billion, a 2.4-fold increase year-on-year. Stock trading accounted for 67.8 percent of total trading, followed by corporate bond trading at 22.6 percent, asset-backed securities at 8.9 percent, and investment fund units at 1.2 percent.

49. The liquidity of the securities market improved, with increases observed in the TOP-20 and MSE-A indices. In the first quarter of 2024, 124 joint-stock companies participated in 62 trading sessions, totaling MNT 127.6 billion in market value. Primary market trading accounted for 7.0 percent (MNT 8.9 billion), while secondary market trading constituted 93.0 percent (MNT 118.7 billion). Furthermore, trading of company debt instruments surged 3.6 times to MNT 42.6 billion, whereas no new corporate bond issues were registered. During this period, the TOP-20 index soared by 21.7 percent compared to the same quarter of the previous year. Additionally, the liquidity ratio of the securities market rose by 0.4 percentage points to 1.0 percent.

Figure III.7 Stock market



Source: Stock Exchange and Financial Regulatory Commission.
Note: Stock market capitalization is compared to gross domestic product (GDP)

CHAPTER IV

EXTERNAL SECTOR

IV. EXTERNAL SECTOR

OVERVIEW

Total foreign trade grew by 6.5 percent in the first quarter of 2024, compared to a year earlier. Despite higher export volumes of coal, copper concentrate, and iron ore, total exports recorded a slight decline due to falling coal prices and decreased agricultural exports following extreme weather conditions. On the other hand, robust domestic demand, a recovery in household income, and credit expansion boosted demand for imports, leading to the growth in trade turnover. Despite the deterioration of the current account balance due to the import growth, the balance of payments improved with the increased net inflow of FDI and government loans, contributing to further accumulation of gross international reserves and appreciation of the exchange rate.

The Government remains committed to implementing measures aimed at ensuring sustainable economic growth and the stability of the exchange rate, which include increasing exports, increasing the level of processing, supporting domestic production of import substitutes, boosting gross international reserves, reducing the pressure of import-induced inflation, and managing external debt effectively.

CHAPTER IV

4.1 FOREIGN TRADE

50. Trade turnover increased. Trade turnover reached USD 6.1 billion in the first quarter of 2024, up 6.5 percent from the previous year. Imports surged by 24.7 percent due to strong domestic economic activity, while exports decreased by 2 percent due to falling commodity prices. The foreign trade balance reached USD 1.2 billion, down by 32 percent from the previous year.

51. In the first quarter of 2024, total exports declined by 2 percent to USD 3.7 billion. The weaker-than-anticipated export performance can be attributed primarily to the decreased prices of export commodities and significant livestock losses in the agricultural sector.

52. Despite robust foreign demand and an increase in the physical volume of coal exports, Mongolia's coal export declined primarily because of reduced prices for coking coal at Ganzmod port. China experienced a 12 percent year-on-year decrease in domestic coking coal production in the first quarter of 2024 due to mine inspections, which led to increased imports and bolstered Mongolia's coking coal exports. Mongolia exported 17.7 million tons of coal in the first quarter of 2024, marking a 28 percent rise from the previous year. However, the average price of Mongolia's coking coal at Ganzmod Port decreased by 9.7 percent year-on-year to 1,490 yuan.

53. The average transaction price of coal on the Mining commodity exchange stood at USD 135 per ton, surpassing the average border price in non-exchange markets by 7 percent. In the first quarter of 2024, 5.2 million tons of coal were traded on the exchange. Furthermore, starting from 2024, the Mining commodity exchange started trades of copper concentrate and fluorspar concentrate.

54. Copper concentrate and iron ore exports increased. With the start of underground mining at Oyutolgoi and enhanced railway transportation, copper concentrate exports reached 367 thousand tons in the first quarter of 2024, a 1 percent increase from the same period last year. Iron ore exports totaled 1,804 thousand tons, up 28 percent from the same period last year.

55. The export of agricultural products declined reflecting harsh winter and spring seasons and livestock losses. By the first quarter of 2024, meat exports fell by 47 percent, wool exports by 49 percent, and leather exports by 26 percent, compared to a year earlier, primarily due to severe weather conditions affecting most parts of the country.

56. Imports surged due to sustained domestic economic growth. Approximately 60 percent of imported goods are used for intermediate input in domestic production. As the economy grew for eight consecutive quarters, imports reached USD 2.4 billion in the first quarter of 2024, marking a 24.7 percent increase from last year.

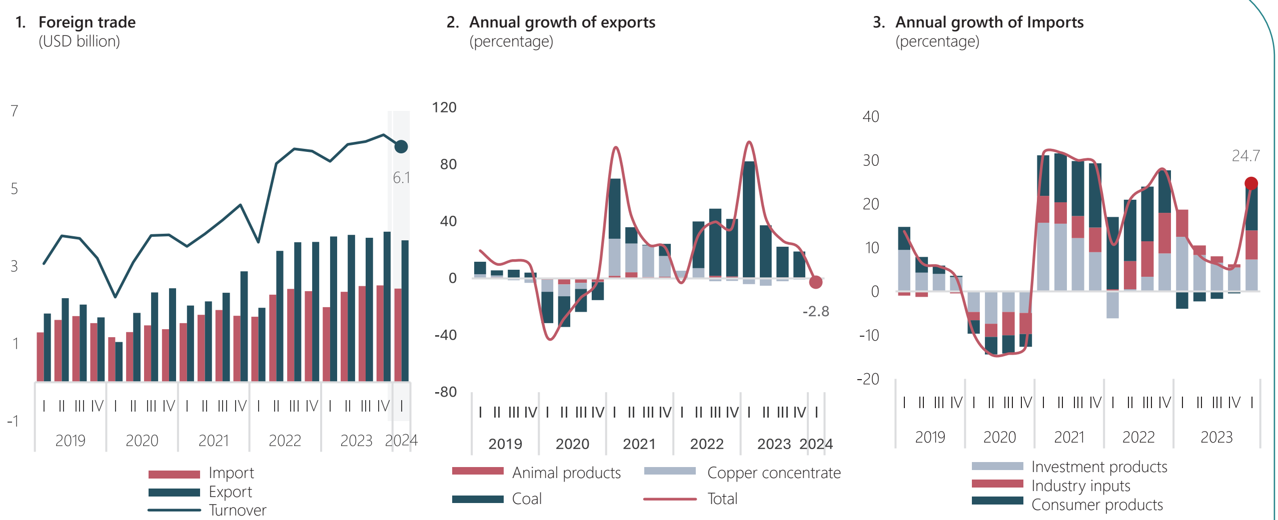
57. The increase in the prices of imported goods was at a low level due to disinflation in trading partner countries. In the first quarter of 2024, imports increased by USD 475 million from the same period of the previous year. 95 percent of this increase was due to the volume increase and 5 percent was due to price changes. The increase in import prices was low as inflation remained subdued in China, which accounts for 36 percent of imported goods and products.

58. Considering the growth of imports by group, 10.7 percent of the total increase was attributed to consumer products, 6.8 percent to machinery and equipment, and 6.7 percent to industrial inputs.

59. The increases in households' real income and consumer credit enhanced purchasing power, and boosted demand for consumer goods, stimulating the growth of imported goods. Mongolia purchases approximately 30 percent of its final consumption products from foreign countries. Households' real income grew for the last three consecutive quarters, leading to increased household consumption. As a result, the imports of consumer goods reached USD 890 million, marking a 30 percent increase from the same period last year. In addition, as of the first quarter of this year, individual loans increased by 37.6 percent, with consumer loans increasing by 2.2 times, thereby boosting the import of durable goods. Also, as the Japanese yen fell to its lowest level since 1990, the average import price of passenger cars decreased by approximately 20.0 percent. As a result, in the first quarter of 2024, the imports of passenger cars reached 34 thousand units, marking a 2.4-fold increase. Due to the increase in passenger cars imports and heightened activity in anticipation of anniversary events in provinces, the imports of automobile gasoline reached USD 167 million, marking a 46 percent increase. However, imports of alcoholic beverages declined as domestic production increased due to the excise tax hike introduced in 2023.

60. The import of equipment increased as loans and foreign direct investment improved the financial resources of enterprises, and some equipment was exempted from customs duties. As part of efforts to increase domestic production and diversify the economy, the Government exempted equipment used in food, agriculture, energy, and mineral processing plants from customs duties, and some equipment was exempted from value-added tax. Additionally, commercial banks' newly issued loans increased by 37 percent and foreign direct investment grew by 2.2 times, which led to increased financial resources for firms. The imports of equipment reached USD 624 million, marking a 31 percent increase compared to the same period last year. Notably, there was significant growth in the imports of equipment used in the mining, processing, and energy sectors.

Figure IV.1. Foreign trade



Source: MCGA

Source: MCGA

Source: MCGA
Note: Imported goods are classified for consumption purposes.

61. The imports of construction materials is expected to rise due to an increase in mortgage loans and the reduction of customs duties on cement. The construction sector grew by 27 percent in the first quarter of this year, leading to an increase in the import of construction materials to USD 194 million, marking a 5.7 percent increase compared to the same period last year. A total of MNT 500 billion was allocated to mortgage loans from the Savings Fund, resulting in a total mortgage loan source of MNT 1.2 trillion. With this increase in mortgage loan availability, the demand for housing is expected to rise, leading to an increase in the import of building materials in the future. To prevent further inflation, the Government decided not to restrict the timing and quantity of cement imports and reduced its customs duty to 5 percent.

62. The imports of agricultural goods and products are expected to continue to grow. To protect the agricultural sector from risks and ensure a stable supply and adequate reserves, it has been decided not to impose a quota or deadline for the imports of animal feed and wheat flour. Furthermore, these products were exempted from customs duties starting May 2024.

BOX 5. IMPORT TARIFF EXEMPTION ON FLOUR

About regulation of flour import quality

Meat, flour, and milk have varying production and supply levels based on the season and are essential for household consumption. According to 3.1.6 of the Food Law, strategic food products are indicated as flour, grain seeds, milk, animal meat, and drinking water. Also, in 6.7 of the law, based on the demand and supply, the Cabinet member in charge of food matters is responsible for defining the export and import amount of strategic food in the particular year after presenting the calculated export and import amounts to the National Committee on Food Safety who shall discuss. Flour and its main ingredient, wheat seeds, are considered strategic foods, both quantity-controlled.

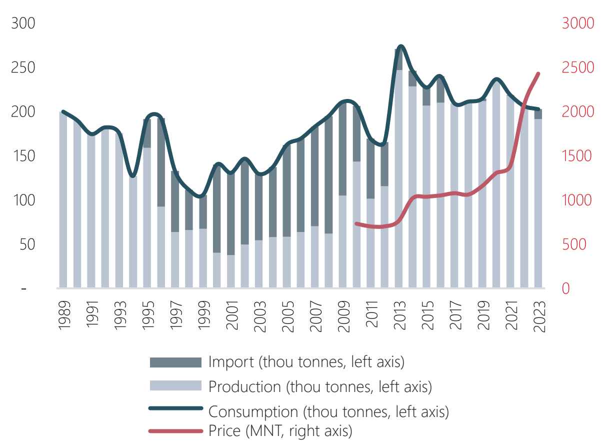
Before 2018, our country used to control the import quantity of flour. However, as a member of the World Trade Organization, the parliament approved the Law on Enriched Foods in 2018, aligning with Article 11 of the General Agreement on Tariffs and Trade and Article 4.2 of the Agreement on Agriculture. Accordingly, from 2020, there will be no quantity control on enriched flour imports, which must be enriched with seven types of vitamins and minerals, according to the Law on Enriched Foods.

Current situation

In Mongolia, as of 2023, 31% of total households are in rural areas, and 62 percent of them are pastoral households. This year, Mongolia is experiencing an unprecedented challenge due to nationwide snowfall that is reported to be double the long-term average. This substantial snow accumulation, reaching up to 90% coverage of the country in January, has intensified the dual challenge of a 'White1' and 'Iron2' dzud acting together. As of March 2024, about 60% of the 330 soums (rural communities) in Mongolia are currently affected. This includes 47 soums in 14 provinces that are under ice or icy conditions, while 135 soums in 17 provinces are under the white dzud conditions. Due to this hard condition, populations in rural areas are facing particularly severe challenges. For instance, due to the blocked road and pass closures, food transportation from the capital city Ulaanbaatar was interrupted, leading to supply-side prices rising risk, especially flour. Compared with pre-pandemic and 2022 where the peak of inflation, flour prices increased by 2.1 times and 67% respectively as of March 2024. In addition to this price increase, dzud open up price hike condition, especially in western regions where there are no flour mills. Therefore, within the framework of measures to maintain a stable supply of flour and bakery products in rural areas, the manner of determining the quantity of imports made it possible to import non-enriched flour and prevented a short-term supply interruption. Also, flour has been exempted from customs duty from May 1st of 2024, to stabilize the rise in flour prices.

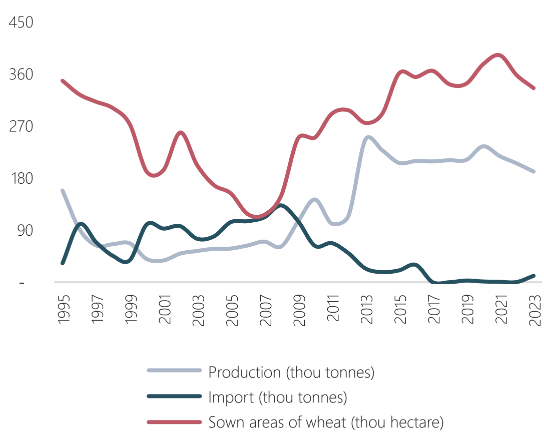
Figure IV.2 Flour consumption and production

1. **Flour production, import, consumption and price**
(thousand tonnes: left axis, MNT: right axis)



Source: National Statistics Office

2. **Sown area of wheat, flour production and import**
(thousand tonnes and hectare)



Source: National Statistics Office

BOX 6. IMPORT TARIFF EXEMPTION ON CEMENT

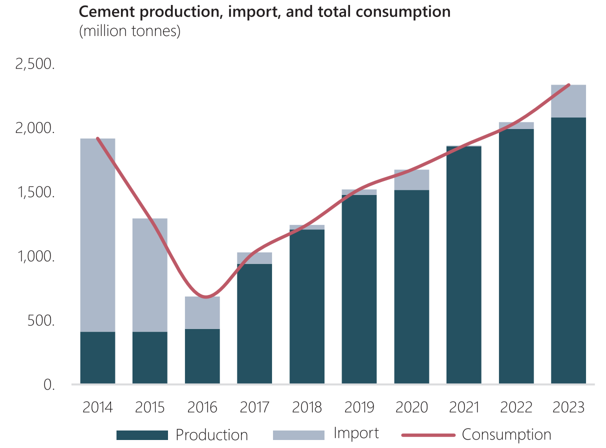
As of 2024, Mongolia operates 7 cement factories with a total installed capacity of 4.5 million tons of cement per year. By 2023, domestic factories are expected to supply 89% of the country's total cement consumption. A 20% customs duty on cement imports is in place to prevent the importation of substandard cement and to protect domestic producers.

In 2022, two out of the five domestic cement factories ceased production due to the commencement of renovation work. As a result, the remaining three manufacturers primarily supplied cement for large national projects, leading to a shortage in the retail market and a subsequent increase in cement prices.

From the demand perspective, the need for housing construction is anticipated to increase. For instance, following the approval of the National Wealth Fund Law on April 19, 2024, it was mandated that savings fund resources be allocated to housing, education, and healthcare. In 2024, MNT 500 billion from the savings fund was allocated to mortgage loans.

Because of the risk of price inflation in the construction sector due to the improvement of lending due to the increase in mortgage financing and the increase in demand for housing, there will be no limit on the amount of cement imports used in most construction inputs. And according to Government Resolution No. 188 of 2024, the customs duty on cement will be adjusted starting from May 1, 2024. It has been decided to reduce the duty rate from 20 percent to 5 percent for the period from 2024 until October 1, 2024.

Figure IV.3. Production and consumption of cement



Source: MED calculation, Ministry of Construction and Urban Develop ment, MCGA

CHAPTER IV

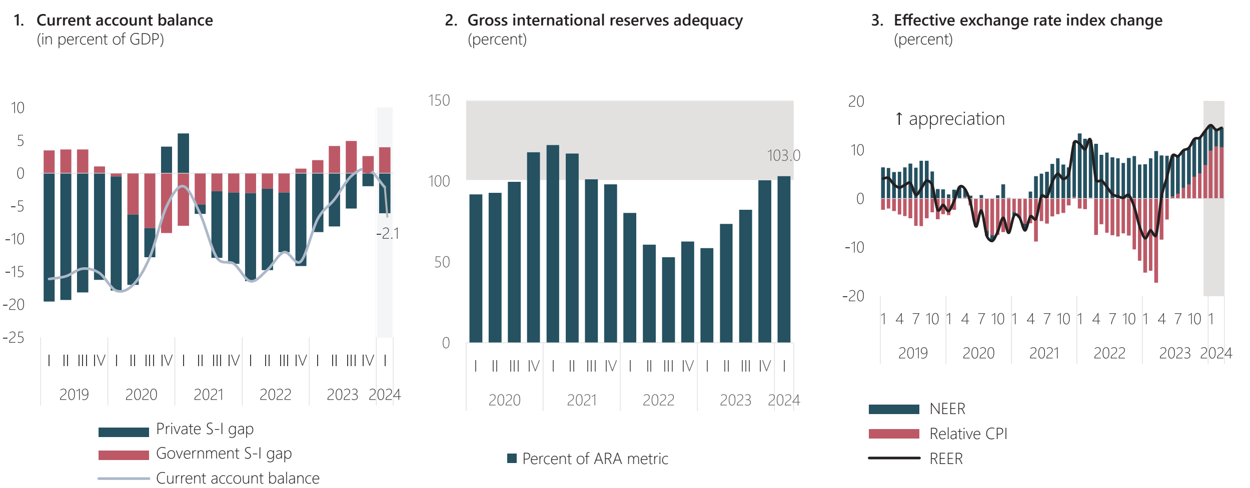
4.2 BALANCE OF PAYMENTS

63. Despite the deterioration of the current account balance, the balance of payments improved in the first quarter of 2024, supported by the financial account surplus. The current account recorded a deficit as import growth outpaced export growth. Compared to a year earlier, the imports of goods and services rose by USD 0.6 billion, reflecting the surge in imports of machinery and equipment and vehicles, while the exports increased by only USD 82 million due to falling export prices. On the other hand, the financial account recovered to a surplus of USD 0.9 billion in the first quarter of 2024, from a deficit of USD 0.5 billion in the first quarter of 2023, with increased net inflow of FDI and government loans and decreased outflows related to trade advances. As a result, the balance of payments improved to a surplus of USD 0.4 billion in the first quarter of 2024, up 4.7 times from a year earlier.

64. International bonds were repaid successfully, and new corporate bonds were issued. In March 2024, the Government of Mongolia successfully repaid the remaining amount of the USD 600 million Khuraldai bond issued in 2017. Also, in January 2024, the "Mongolian Mortgage Corporation HFC" LLC issued a USD 225 million bond, while the Development Bank of Mongolia issued a USD 200 million bond in March 2024.

65. The gross international reserves continued to increase, and the exchange rate was stable. The gross international reserves rose by 52.7 percent from a year earlier to USD 5,250 million at the end of the first quarter of 2024, equivalent to 4.4 months of imports and 103 percent of the ARA metric. Consequently, the real effective exchange rate appreciated in the first quarter of 2024 compared to the same period last year.

Figure IV.4. Current account balance, GIR, exchange rate

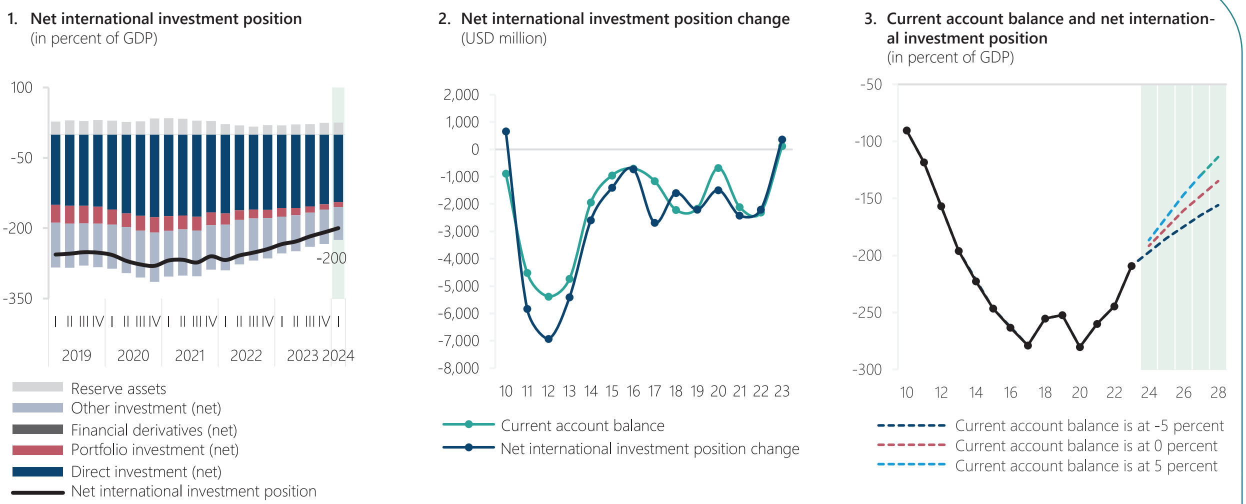


Source: MED calculation, Bank of Mongolia
Note: Current account balance-to-GDP ratio is calculated as rolling sum of four quarters.
The IMF's ARA (Assessing Reserve Adequacy) metric comprises of four components (i)export income (ii)broad money (iii)short-term debt (iv)other liabilities with relative risk weights of 5 percent, 5 percent, 30 percent, and 15 percent, respectively.
In general, reserves in the range of 100-150 percent of the ARA metric are considered broadly adequate.

66. Total national investment exceeded total national savings. A current account deficit indicates that a country is investing more than its national savings can support. The government savings-investment gap remained positive for the last six quarters, as government savings increased due to the growth in the mining sector. However, private investment remains higher than private savings.

67. Mongolia's net international investment position remains weak, indicating a heightened vulnerability to external shocks. The net international investment position measures the difference between Mongolia's financial assets held abroad and its liabilities to other countries. At the end of the first quarter of 2024, the net international investment position stands at USD -41.5 billion, equivalent to -200 percent of GDP. The large net negative position shows that the financial liabilities far exceed the assets held abroad, suggesting increased exposure to external shocks. Avoiding large and persistent current account deficits and further accumulation of net external liabilities is important for improving the net international investment position and reducing vulnerability to adverse external shocks (Figure IV.5).

Figure IV.5. International investment position



Source: MED calculation, Bank of Mongolia
Note: GDP is calculated as rolling sum of four quarters.
In the last figure, real GDP growth and inflation rates are assumed to be constant to calculate changes in net international investment position

CHAPTER IV

4.3

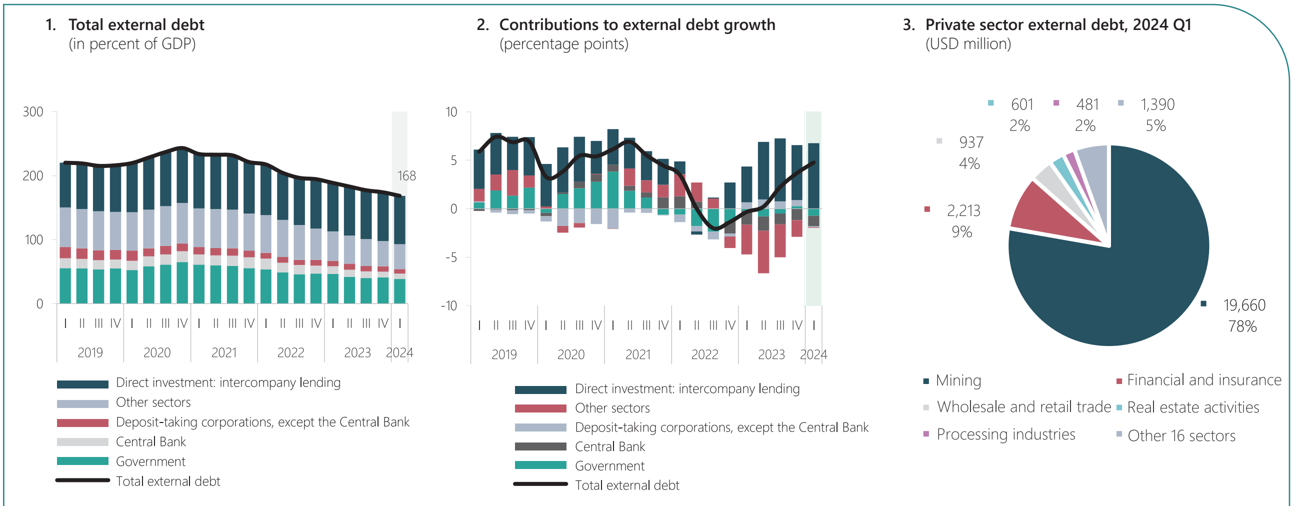
EXTERNAL DEBT

68. The gross external debt increased, largely due to the increases in debt securities and direct investment liabilities of the private sector. Mongolia's gross external debt totaled USD 35 billion as of the end of the first quarter of 2024, up by USD 0.4 billion from the end of 2023. However, the external debt-to-GDP ratio fell to 168 percent, down by 5.5 percentage points from the previous quarter, driven by the nominal GDP growth. The government's external debt decreased by USD 0.1 billion from the end of 2023, reflecting repayments of the Khuraldai bond, while the private sector's external debt excluding banking grew by USD 0.6 billion.

69. Most of the external debt is contracted by the private sector. Specifically, the private sector accounts for 72 percent of the total external debt, while government and central bank debt constitutes 23 percent and 5 percent, respectively. Within the private sector, the mining sector holds the largest share, representing 78 percent, followed by the financial and trade sectors which account for 9 percent and 4 percent, respectively. The remaining 10 percent belongs to 18 other sectors.

70. 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, facilitated by export and GDP growth. However, the ratio remains particularly sensitive to exchange rate depreciation and current account shocks. Compared to the baseline, the external debt-to-GDP ratio could be 14.2 percentage points higher when current account balance deteriorates by ½ standard deviation and 23.8 percentage points higher if exchange rate depreciates by 10 percent (Figure IV.7).

Figure IV.6. External debt



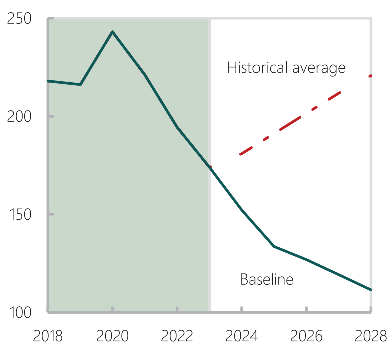
Source: MED calculation, Bank of Mongolia
Note: GDP is calculated as rolling sum of four quarters.

Figure IV.7. External debt sustainability

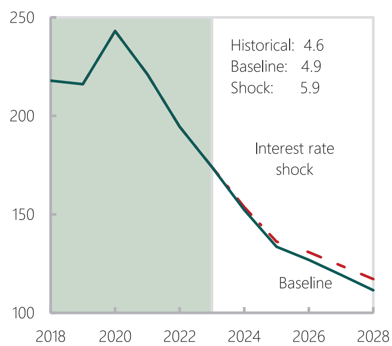
External debt (in percent of GDP, unless otherwise indicated)	Actual								Projections					Debt-stabilizing
	2018	2019	2020	2021	2022	2023			2024	2025	2026	2027	2028	non-interest current accoun
External debt: Baseline	**217.9**	**216.1**	**243.1**	**221.1**	**194.4**	**174.0**			**152.2**	**133.5**	**126.9**	**119.3**	**111.5**	**-7.9**
Change in external debt	-21.5	-1.7	26.9	-21.9	-26.7	-20.5			-21.8	-18.6	-6.6	-7.6	-7.8	
Identified net debt-creating flows	-20.9	-8.6	14.9	-25.3	-11.5	-28.7			-30.2	-28.7	-16.3	-17.6	-16.1	
Non-interest current account deficit	7.7	5.5	-4.9	5.6	4.9	-11.1			-10.8	-11.8	-11.6	-11.4	-7.7	
Net non-debt creating capital inflows	-6.8	-8.1	-4.6	-7.7	-0.9	-1.4			-1.1	-1.1	-1.0	-0.9	-1.0	
Automatic debt dynamics 1/	-21.8	-6.0	24.4	-23.2	-15.6	-16.2			-18.4	-15.9	-3.6	-5.3	-7.3	
Contribution from nominal interest rate	9.0	9.7	10.0	8.2	8.5	10.5			7.8	6.9	6.3	5.6	4.4	
Contribution from real GDP growth	-16.2	-11.3	10.5	-3.5	-9.9	-11.8			-8.9	-10.3	-8.0	-7.5	-7.0	
Contribution from price and exchange rate changes	-14.7	-4.5	3.9	-27.9	-14.2	-14.9			-17.3	-12.4	-2.0	-3.3	-4.8	
Residual	-0.6	6.9	12.1	3.4	-15.2	8.2			8.4	10.1	9.7	10.0	8.3	
External debt-to-exports ratio (in percent)	374.5	364.8	423.3	377.7	303.4	223.0			197.9	181.8	170.3	160.8	160.7	
External debt: Scenario with key variables at their historical averages 2/									**180.9**	**191.0**	**200.9**	**211.7**	**220.8**	**-4.1**
							historical average	standard deviation						
Real GDP growth (in percent)	7.7	5.6	-4.6	1.6	5.0	7.0	4.0	3.8						
GDP deflator in USD (change in percent)	6.5	2.1	-1.8	13.0	6.8	8.3	1.0	7.5						
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	11.1	-1.4	6.3						
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.

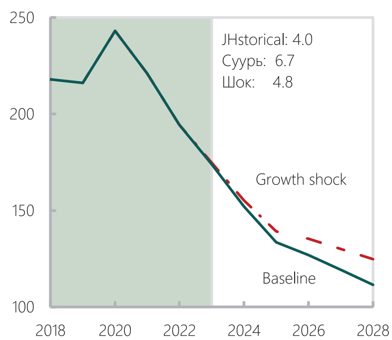
1. Baseline and historical scenarios



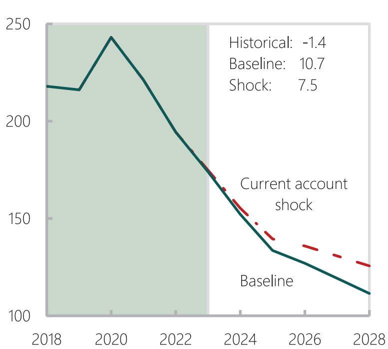
2. Interest rate shock



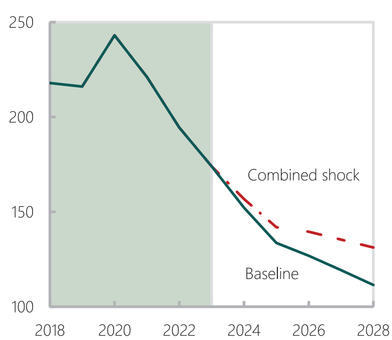
3. Growth shock



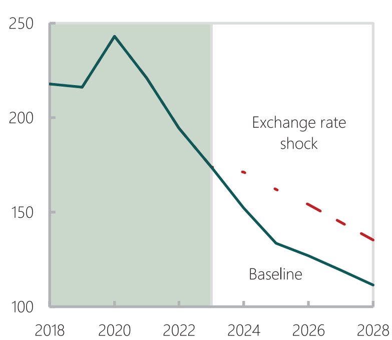
4. Non-interest current account shock



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.

CHAPTER V

WORLD ECONOMY

V. WORLD ECONOMY

OVERVIEW

Global economic activity gained momentum in the first months of 2024 and forecasts for global GDP growth were revised upward. Gold, copper, coking coal, and oil prices increased due to the geopolitical instability and supply conditions, while iron concentrate prices fell.

CHAPTER V

5.1 WORLD ECONOMIC SITUATION

71. The global economy is gaining momentum. After slowing down in the last half of 2023, global economic activity recovered in the first months of 2024. The S&P Global PMI hit a 12-month high in May 2024 and world merchandise trade grew by 1.2 percent in February 2024, after shrinking by 3.5 percent in September of last year.

72. International institutions upgraded global economic growth forecasts. Following the stronger than expected economic activity, the IMF revised its 2024 global economic growth forecast by 0.1 percentage point to 3.2 percent, while the OECD lifted its outlook by 0.2 percentage point to 3.1 percent. The global growth is expected to be steady in 2024 and 2025 amid the ongoing geopolitical tensions and price hikes

73. Major central banks kept interest rates unchanged. The US economy grew by 1.6 percent in the first quarter of 2024, driven by growth in private consumption and fixed investment, while core inflation reached 3.6 percent in April 2024, the lowest level since April 2021. However, the Federal Reserve maintained its benchmark policy rates at 5.25-5.00 percent. As for the European Central Bank, the policy rate has also been kept unchanged as of May 2024, despite Eurozone inflation reaching 2.4 percent in April 2024 and remaining below 3 percent for the seventh consecutive month.

74. China's economic growth accelerated. China's economy expanded by 5.3 percent in the first quarter of 2024, after growing by 5.2 percent in 2023. The economic activity was mainly supported by the growth in the industrial and service sectors. The real estate sector, however, remained sluggish with investment and sales falling by 9.5 percent and 27.6 percent, respectively. To further stabilize the real estate sector, the policymakers announced a new CNY 300 billion program to buy unsold homes, removed mortgage rate floor, and further lowered minimum down payment ratios. Following the strong first-quarter performance, the IMF revised up China's growth projections for both 2024 and 2025 by 0.4 percentage points to 5 percent and 4.5 percent, respectively, in May 2024.

75. The Russian economy continues to expand. Russia's GDP grew by 5.4 percent in the first quarter of 2024. Economic growth was mainly driven by the expansion of the budget due to the increase in military spending related to the conflict in Ukraine. Exports in the first quarter of 2024 decreased by 6.9 percent from the same period of the previous year, 36.7 percent from the same period of 2022, and imports decreased by 10.3 percent from the same period of the previous year. The decrease in exports was mainly due to the decline in the prices of oil and natural gas. During the reporting period, inflation steadily increased from December 2023 to reach 7.7 percent, surpassing the Central bank's target of 4 percent. The Purchasing Managers' Index, an indicator of industrial sector expansion, reached 55.7 in March 2024, marking its highest level in the last seven years. Real industrial production grew by 8.5 percent in March 2024 compared to the same period the previous year, representing the strongest growth in the past two years. The sharp rise in new orders driven by domestic demand supported employment and stimulated inventory purchases, significantly impacting the expansion of the industrial sector. Russia's GDP expanded by 3.6 percent in 2023, surpassing the Ministry of Economic Development's expectation of 2.8 percent growth, bolstered by substantial defense spending and support for domestic industries. Looking ahead, the country's policymakers expect annual economic growth to reach 2.9 percent in 2024 and slow to less than 2.0 percent in 2025 and 2026.

CHAPTER V

5.2 COMMODITY MARKET DEVELOPMENTS

76. Gold price reached USD 2,074 per troy ounce in the first quarter of 2024, up 6 percent from the previous year. Central banks' increased purchases of gold amid the worsening geopolitical situation, which mainly contributed to the rise in gold prices.

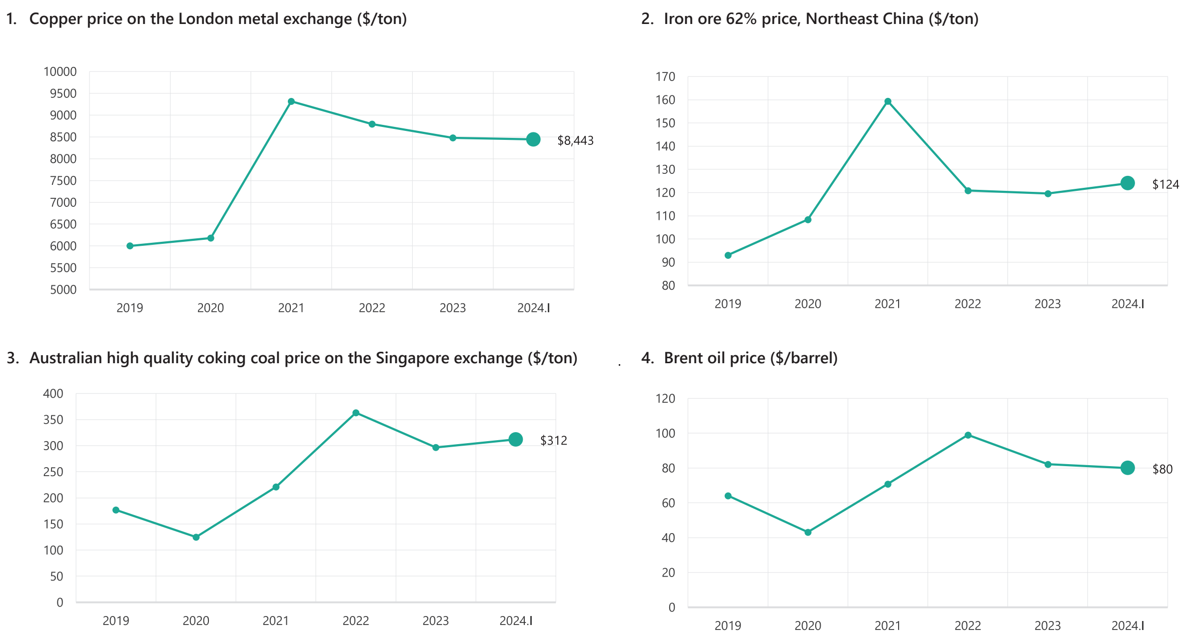
77. Copper price on the London Metal Exchange stood at an average of USD 8,443 in the first quarter of 2024, up 0.4 percent from the previous year. Infrastructure funding for chip production increasing in major countries such as US and China is mainly influenced the rise in copper price.

78. The average price of iron ore with 62 percent iron content was at USD 124 tons in the first quarter of 2024, down 11 percent from the previous year. Increased supply in Brazil and Australia, and the failure of China's property sector to recover was a major factor in the decline in iron ore concentrate prices.

79. The average price of Australian high-quality coking coal reached USD 313 million in the first quarter of 2024, up 5.2 percent in previous year. Coking coal price has mainly contributed to increase due to China lifting to ban on Australian's coking coal import and increased coal demand in India.

80. The average price of Brent oil reached USD 80 per barrel in the first quarter of 2024, up 2.9 percent in previous year. The OPEC member countries began to reduce oil supply intensively was mainly influenced the increase in oil price.

Figure V.1. Commodity prices



Source: Bloomberg

CHAPTER VI

RISKS

CHAPTER VI

6 RISKS

ONE. DZUD The extreme winter conditions observed in 80 percent of the total land area caused total loss of 6.3 million adult livestock and the number of young surviving animals declined by 28 percent at the end of 2023 and 38 percent in the beginning of 2024. As a result, reduced meat supply could trigger food inflation, while decline in agricultural production and capital accumulation may negatively affect household income and consumption in rural areas and adversely impact growth.

TWO. COMMODITY PRICE VOLATILITY The commodity price volatility risk stemming from uncertainty in global economy could weigh on the export revenues of Mongolia. Weaker economic activity in China due to the real estate crisis could also weigh on the demand and prices of commodities.

THREE. GEOPOLITICAL TENSIONS Further escalation of Russia's invasion of Ukraine, conflict in the Middle East, and continued attacks in the Red Sea could add to inflationary pressures with upward pressure on global prices of fuel, grain, food, and energy.

FOUR. ENERGY RELIABILITY Energy security is one of the fundamental factors for ensuring economic and social stability. However, approximately 20 percent of our country's electricity consumption is imported from the neighboring countries. Energy in Mongolia is also supplied by centralized sources, with aging plants and obsolete distribution systems. Disruption of energy supplies could limit real overall economic activity and productivity.

FIVE. SUPPLY DISRUPTION About 80 percent of Mongolia's total imports pass through Tianjin Port. During the COVID-19 pandemic, over 9,000 containers accumulated at Tianjin Port, disrupting the supply of imported goods and causing inflation to surge to 16.9 percent as import inflation accounted for 8.9 percentage points. As of June 2024, the number of containers at the port exceeded 5,000, which normally is around 3,000, due to reduced daily departures from Tianjin Port. The congestion could result in disruption in supply of goods and raise risk to further inflation.

APPENDIX

TABLE 0.1. SELECTED ECONOMIC INDICATORS

SELECTED ECONOMIC INDICATORS	2020	2021	2022	2023	2024Q1
REAL SECTOR					
Nominal GDP (in MNT billion)	37,453	43,555	53,852	68,872	16,454
Real GDP growth - production approach (percent change)	-4.6	1.6	5.0	7.0	7.8
Real GDP growth - expenditure approach (percent change)	-4.4	1.6	5.0	7.1	7.8
Domestic demand (percentage points)	-12.6	17.6	11.4	1.9	27.2
Exports of goods and services (percentage points)	-2.7	-7.5	13.9	23.3	-7.5
Imports of goods and services (percentage points)	11.0	-8.5	-20.3	-18.0	-11.9
Contribution to real GDP growth (percentage points)					
Final consumption	3.6	-2.3	6.5	6.1	23.4
Private	1.3	-4.0	5.1	4.8	14.6
Public	2.2	1.7	1.4	1.3	8.8
Gross capital formation	-16.2	19.9	4.9	-4.3	3.8
Net exports of goods and services	8.2	-16.0	-6.4	5.2	-19.4
			(in percent of GDP)		
Savings and investment					
Gross national savings	17.3	22.3	28.7	31.2	20.1
Gross capital formation	22.1	35.8	41.5	31.7	24.8
Private	14.1	29.1	34.6	24.3	19.8
Public	8.0	6.7	6.9	7.3	5.0
PRICES					
Consumer prices (eop, percent change)	2.3	13.8	13.2	7.9	7.0
Copper prices* ($/ton)	6,178	9,315	8,815	8,479	8,443
Gold prices* ($/troy ounce)	1,772	1,799	1,802	1,943	2,074
Oil prices* ($/barrel, Brent)	50	61	82	79	80
GDP deflator (percent change)	3.7	14.4	17.7	19.5	10.7
			(in MNT billion)		
GENERAL GOVERNMENT ACCOUNTS					
Total revenue and grants	10,444	14,306	18,522	24,310	7,673
Structural revenue and grants	9,464	12,711	17,127	23,218	7,322
Total expenditure and net lending	13,904	15,630	18,160	22,454	5,695
Overall balance	-3,460	-1,324	362	1,856	1,978
Overall primary balance	-2,521	-488	1,160	2,987	2,380
Structural balance	-4,440	-2,919	-1,033	763	1,627
Structural primary balance	-3,501	-2,083	-235	1,895	2,028
General government debt (NPV, in percent of GDP)	62.3	50.8	52.4	38.6	33.7
General government debt (nominal)	27,899	26,918	31,965	30,774	29,767
MONETARY SECTOR					
Broad money growth (percent change)	16.2	13.8	6.5	26.8	20.9
Reserve money growth (percent change)	-12.7	6.5	39.9	7.4	11.7
Velocity of money	1.5	1.6	1.8	1.8	1.9
Money multiplier	5.4	5.8	4.4	5.2	6.1
Credit growth** (percent change)	-4.0	18.5	7.5	22.7	22.3
			(in USD million)		
BALANCE OF PAYMENTS					
Balance of payments	787	-222	-727	1,457	373
Current account balance	-675	-2,108	-2,304	121	-251
Gross official reserves (in USD million)	4,534	4,366	3,400	4,921	5,250
in months of imports of G&S	7.4	5.7	3.4	4.4	17.3
Exchange rate					
MNT/USD (average)	2,813	2,849	3,140	3,466	3,392
MNT/USD (eop)	2,850	2,849	3,445	3,411	3,376
Nominal effective exchange rate (average)	43.0	41.3	38.8	37.6	39.4
Real effective exchange rate (average)	102.9	103.6	106.9	112.4	119.2

*Bloomberg Terminal **Includes mortgage-backed securities

TABLE 0.2. REAL SECTOR

REAL SECTOR	2020	2021	2022	2023	2024Q1
Nominal GDP (production approach)	37,453	43,555	53,852	68,872	16,454
Real GDP (production approach)	26,655	27,092	28,455	30,454	6,065
			(percent change)		
Real GDP growth	-4.6	1.6	5.0	7.0	7.8
Mining	-9.9	0.8	-15.3	23.4	13.1
Non-mining	-3.7	1.8	8.2	5.0	6.9
Agriculture	5.8	-5.5	12.0	-8.9	-31.4
Mining and quarrying	-9.9	0.8	-15.3	23.4	13.1
Manufacturing	3.4	-0.9	6.1	5.1	6.3
Electricity, gas, stream, air conditioning supply	1.8	9.4	3.3	5.0	7.7
Construction	-3.2	-22.8	8.2	0.6	27.7
Wholesale and retail trade	-12.5	5.8	10.1	5.7	6.5
Transportation and storage	-18.2	-7.3	9.2	39.3	27.2
Information and communication	5.2	20.7	6.6	16.4	26.3
Other service activities	-2.6	3.8	5.4	5.2	3.7
Taxes less subsidies on products	-9.4	12.2	11.5	6.8	13.1
Deflator	3.7	14.4	17.7	19.5	10.7
			(percentage points)		
Contributions to real GDP growth					
Agriculture	0.8	-0.8	1.7	-1.3	-1.3
Mining and quarrying	-1.4	0.1	-2.1	2.6	1.9
Manufacturing	0.3	-0.1	0.5	0.4	0.4
Electricity, gas, stream, air conditioning supply	0.0	0.2	0.1	0.1	0.3
Construction	-0.1	-0.9	0.2	0.0	0.2
Wholesale and retail trade	-1.4	0.6	1.1	0.7	0.7
Transportation and storage	-1.0	-0.3	0.4	1.8	1.3
Information and communication	0.1	0.5	0.2	0.5	0.9
Other service activities	-0.7	1.1	1.6	1.5	1.3
Taxes less subsidies on products	-1.1	1.3	1.4	0.9	2.1
			(in MNT billion)		
Nominal GDP (expenditure approach)	37,883	44,703	54,878	70,444	16,853
Primary income	-3,526	-6,359	-5,072	-7,738	-1,693
Gross national income	34,357	38,344	49,806	62,706	15,160
Secondary income	769	1,223	1,363	1,378	592
Gross national disposable income	35,126	39,566	51,169	64,084	15,752
Domestic demand	36,953	45,574	58,219	64,392	16,545
National savings	6,556	9,985	15,747	21,997	3,385
Gross capital formation	8,383	15,993	22,796	22,305	4,178
Saving - Investment balance	-1,827	-6,008	-7,050	-308	-793
			(in percent of GDP)		
Domestic demand	97.5	101.9	106.1	91.4	98.2
Final consumption	75.4	66.2	64.5	59.7	73.4
Private	59.8	51.6	50.9	46.8	53.6
Public	15.6	14.5	13.7	13.0	19.8
Gross capital formation	22.1	35.8	41.5	31.7	24.8
Gross fixed capital formation	23.3	26.1	29.3	26.8	17.9
Changes in inventories	-1.2	9.6	12.3	4.9	6.9
Net exports of goods and services	2.5	-1.9	-6.1	8.6	1.8
Exports of goods and services	57.0	57.0	63.8	76.3	75.2
Imports of goods and services	54.6	59.0	69.9	67.7	73.4
Statistical discrepancy (in MNT billion)	-430	-1,147	-1,026	-1,573	-399

TABLE 0.3. GENERAL GOVERNMENT ACCOUNTS

GENERAL GOVERNMENT ACCOUNTS	2020	2021	2022	2023	2024Q1
			(тэрбум төгрөгөөр)		
TOTAL REVENUE AND GRANTS	10,444	14,306	18,522	24,310	7,673
Future heritage fund	914	967	0	416	284
Stabilization fund	66	628	1,395	676	67
STRUCTURAL REVENUE AND GRANTS	9,464	12,711	17,127	23,218	7,322
Tax revenue	864	11,300	15,459	21,451	6,909
Income tax	2,227	3,326	3,827	5,800	2,557
Social secutiry contributions	1,586	2,286	3,038	3,943	920
Property tax	155	201	238	397	109
Value added tax	2,209	2,838	3,946	4,773	1,286
Excise tax	777	827	848	790	280
Special tax revenue	17	17	19	22	6
Customs duties and export taxes	741	939	1,256	1,464	352
Other taxes, fees and charges	800	866	2,288	4,262	1,398
Non-tax revenue	952	1,412	1,668	1,767	413
General non-tax revenue	785	1,250	1,364	1,430	339
Capital revenue	1	2	4	8	1
Grant revenue	166	160	300	330	73
TOTAL EXPENDITURE AND NET LENDING	13,904	15,630	18,160	22,454	5,695
Current expenditure	10,829	12,804	14,229	17,047	4,698
Wages and salaries	2,649	2,532	1,666	2,322	1,081
Purchase of goods and services	2,202	2,170	2,140	2,740	687
Subsidies	375	454	537	580	134
Current transfers	4,663	6,813	9,088	10,273	2,394
Interest payments	939	836	798	1,132	402
Foreign	776	681	694	1,042	395
Domestic	163	155	104	90	6
Capital expenditure and net lending	3,075	2,826	3,930	5,408	997
Capital expenditure	3,034	2,982	3,803	5,175	843
Net lending	41	-156	127	233	154
OVERALL BALANCE	-3,460	-1,324	362	1,856	1,978
OVERALL PRIMARY BALANCE	-2,521	-488	1,160	2,987	2,380
STRUCTURAL BALANCE	-4,440	-2,919	-1,033	763	1,627
STRUCTURAL PRIMARY BALANCE	-3,501	-2,083	-235	1,895	2,028

TABLE 0.4. BALANCE OF PAYMENTS

BALANCE OF PAYMENTS	2020	2021	2022	2023	2024Q1
			(in USD million)		
I. CURRENT ACCOUNT	-675	-2,108	-2,304	121	-251
Goods	1,756	1,370	1,233	4,549	920
Exports F.O.B (credit)	6,991	8,136	9,854	13,914	3,431
Imports F.O.B (debit)	5,235	6,766	8,622	9,366	2,511
Services	-1,450	-1,675	-2,355	-2,592	-846
Credit	655	814	1,135	1,587	275
Debit	2,105	2,490	3,490	4,179	1,121
Primary income	-1,253	-2,232	-1,615	-2,233	-499
Credit	341	292	344	455	132
Debit	1,595	2,524	1,959	2,687	631
Secondary income	273	429	434	398	175
II. CAPITAL ACCOUNT	103	114	154	135	32
Credit	105	116	166	149	36
Debit	2	2	12	14	4
III. FINANCIAL ACCOUNT: net lending (+) / net borrow	-1,504	-1,982	-1,644	-1,477	-857
Direct investment (net)	-1,693	-2,060	-2,428	-2,172	-580
Portfolio investment (net)	563	25	445	818	-16
Financial derivatives (net)	-6	-8	-11	-2	8
Other investments (net)	-369	60	351	-121	-269
Of which: Currency and deposits	278	245	298	354	-245
Loans	-803	-501	67	-529	-86
Trade credit and advances	156	413	-15	54	61
IV. Net errors and omissions	-146	-209	-222	-276	-265
Overall balance	787	-222	-727	1,457	373
V. Reserve assets	787	-222	-727	1,457	373
Reserve	787	-225	-751	1,398	359
IMF loan	0	-3	-24	-59	-14
Exceptional financing	0	0	0	0	0
Memorandum items:					
Nominal GDP (in USD million)	13,314	15,286	17,150	19,872	4,850
Gross official reserves (in USD million)	4,534	4,366	3,400	4,921	5,250
in months of imports of G&S	7.4	5.7	3.4	4.4	17.3
MNT/USD exchange rate (average)	2,813	2,849	3,140	3,466	3,392
MNT/USD exchange rate (eop)	2,850	2,849	3,445	3,411	3,376

TABLE 0.5. MONETARY SECTOR

MONETARY SECTOR	2020	2021	2022	2023	2024Q1
			(in MNT billion)		
Net foreign assets	5,816	3,806	2,492	8,959	9,775
Net domestic assets	18,664	24,057	27,173	28,665	27,625
Domestic claims (net)	19,136	24,298	25,648	29,106	28,477
Other items (net)	-472	-241	1,525	-441	-852
Broad money	24,481	27,863	29,665	37,624	37,400
Currency outside depository corporations	753	847	831	906	827
Currency and deposits	23,728	27,016	28,834	36,719	36,573
			(percent change)		
Broad money	16.2	13.8	6.5	26.8	20.9
Net foreign assets	80.9	-34.6	-34.5	259.6	148.4
Net domestic assets	4.6	28.9	13.0	5.5	2.3
Domestic claims (net)	2.3	27.0	5.6	13.5	12.4
Net claims on government	-29.6	-49.8	107.6	91.3	57.9
Net claims on other sectors	-2.2	19.2	9.9	19.8	18.5
Claims on public sector	1,492.6	25.0	-5.0	-16.7	-8.6
Claims on private sector	-7.2	18.8	10.8	21.7	19.8
			(percentage points)		
Contributions to broad money growth					
Broad money	16.2	13.8	6.5	26.8	20.9
Net foreign assets	12.4	-8.2	-4.7	21.8	18.9
Net domestic assets	3.9	22.0	11.2	5.0	2.0
Memorandum items:					
Velocity of money	1.5	1.6	1.8	1.8	1.9
Nominal GDP growth (percent change)	-1.0	16.3	23.6	27.9	19.4
Consumer prices (eop, percent change)	2.3	13.8	13.2	7.9	7.0

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