UN ESCAP Training Workshop
«Infrastructure financing challenges, opportunities, and enabling regulations, governance, and policies in Mongolia »
Ulaanbaatar, Mongolia, 21-22 November 2019
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2. Current state of Infrastructure financing
   A. Lack of Infrastructure in Mongolia
   B. Public financing
   C. Private financing
   D. Public-Private Partnership (PPPs)
   E. Belt and Road Initiative

3. Infrastructure financing: Challenges
   A. Public financing
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4. Infrastructure financing: Opportunities and Modalities
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5. Conclusions and proposed way forward
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Mongolia is a resource-rich land-locked developing country located in the central eastern Asian region. Compared to countries with coastal borders, Mongolia has land borders with Russia and China only and faces significant infrastructure constraints in connecting and accessing regional and world markets.

After a balance-of-payment crisis between 2014 and 2016, Mongolia requested and received an IMF Extended Fund Facility (EFF) in May 2017 to revive its economy. The total funding associated with the program is USD5.5 billion, which includes support from Japan, Korea, China, the World Bank, and the Asian Development Bank (ADB). Mongolian economy has recovered since then and the real GDP growth was 6.9 percent in 2018. ADB expects the economy will grow by 6.7 percent in 2019 and 6.3 percent in 2020.
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5. Conclusions and proposed way forward
CURRENT STATE: LACK OF INFRASTRUCTURE IN MONGOLIA

As indicated by the Index of Quality of Overall Infrastructure by the World Bank, the quality of infrastructure in Mongolia is not sufficiently good.

Source: World Economic Forum Global Competitiveness Index
CURRENT STATE: LACK OF INFRASTRUCTURE IN MONGOLIA

Infrastructure, Index – Mongolia, China and Russia

Source: World Economic Forum Global Competitiveness Index
CURRENT STATE: LACK OF INFRASTRUCTURE IN MONGOLIA

Infrastructure, Index – Asia Pacific LLDCs

Source: World Economic Forum Global Competitiveness Index
CURRENT STATE: LACK OF INFRASTRUCTURE IN MONGOLIA

Transportation

• Mongolia has a road network of about 48,538 km, but only about 13.2% are paved.
  • This affects the country’s growth prospects, particularly on jobs, trade, and connectivity.

• Investing in road improvement and maintenance is crucial because it creates jobs, provides people with better connectivity and access to markets and public services such as schools and hospitals, and improves road safety.

• This is especially the case for Mongolia, one of the least densely populated countries in the world – approximately 2 persons in each square kilometers.

• International roads connecting Russia, Mongolia and China has vital economic importance.
Energy sector

- Electricity consumption in Mongolia has been growing steadily over the years.
- No new combined heat and power (CHP) plants were built in the past 36 years.
- During winter months, it is common for electricity consumption to exceed the built-in supply capacity of the local power plants during peak hours, so Mongolia often imports electricity from Russia.

Source: National Statistics Office
ICT sector

• Mongolia has a 43,018km of fiber optic lines.

• Most important ICT assets in Mongolia are owned by the government as well as some private players. (Information Communication Network Corporation)

• Mobile and IPTV sectors are dominated by the private sector. (Mobicom Networks, Skynetworks, Railcom Center, Gemnet and other private players.)

• ICNC – State budget

• Private players - Private financing

Till 2030, it is estimated that Mongolia needs to invest amounts equal to 5% of its GDP in infrastructure each year. Most vital areas are transportation and energy sectors while there is smaller need for financing in ICT sector. This is in line with the fact that:

- There are already multiple railway and paved road projects pending financing;
- Mongolia still relies on importation of electricity from Russia during peak usage hours in winter;
- Mobile and fibre optic line has already penetrated to most remote areas of Mongolia.
CURRENT STATE: LACK OF INFRASTRUCTURE IN MONGOLIA

Infrastructure Financing Needs in the Asian LLDCs

2018-2030

% of GDP

Transport  Energy  ICT  WSS

Source: Economies 2018, 6(3), 43; Estimating Infrastructure Financing Needs in the Asia-Pacific Least Developed Countries, Landlocked Developing Countries, and Small Island Developing States
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As can be seen from the below figure, most infrastructure projects in Mongolia are implemented by the public sector.

Source: Closing The Financing Gap in Asian Infrastructure, Asian Development Bank
The government of Mongolia is the main sponsor of investment projects in Mongolia with government capital expenditures at 9.3% of GDP in 2017.

Source: GROWING WITHOUT UNDUE BORROWING, Enhancing efficiency of spending and revenue, World Bank
CURRENT STATE: PUBLIC FINANCING

Following are the main methods to finance public infrastructure projects in Mongolia.

- General budget.
- Foreign grants and loans.
- Development Bank of Mongolia (DBM).
### GENERAL BUDGET OF MONGOLIA - 2019

<table>
<thead>
<tr>
<th>Ministry</th>
<th>Budgeted cost (USD thousand)</th>
<th>%</th>
<th>Financing amount (USD thousand)</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Ministry of Education, Culture and Science</td>
<td>347,165</td>
<td>36.3%</td>
<td>476,799</td>
<td>39.2%</td>
</tr>
<tr>
<td>2 Ministry of Road and Transport</td>
<td>181,464</td>
<td>19.0%</td>
<td>170,325</td>
<td>14.0%</td>
</tr>
<tr>
<td>3 Ministry of Construction and urban development</td>
<td>101,674</td>
<td>10.6%</td>
<td>90,821</td>
<td>7.5%</td>
</tr>
<tr>
<td>4 Ministry of Health</td>
<td>72,355</td>
<td>7.6%</td>
<td>81,016</td>
<td>6.7%</td>
</tr>
<tr>
<td>5 Ministry of Energy</td>
<td>71,851</td>
<td>7.5%</td>
<td>95,819</td>
<td>7.9%</td>
</tr>
<tr>
<td>6 Ministry of Finance</td>
<td>65,532</td>
<td>6.9%</td>
<td>146,386</td>
<td>12.0%</td>
</tr>
<tr>
<td>7 Ministry of Mining And Heavy Industry</td>
<td>750</td>
<td>0.1%</td>
<td>2,000</td>
<td>0.2%</td>
</tr>
<tr>
<td>8 Ministry of Justice and Internal Affairs</td>
<td>30,083</td>
<td>3.1%</td>
<td>40,839</td>
<td>3.4%</td>
</tr>
<tr>
<td>9 Ministry of Population Development and Social Protection</td>
<td>18,148</td>
<td>1.9%</td>
<td>23,758</td>
<td>2.0%</td>
</tr>
<tr>
<td>10 Ministry of Defense</td>
<td>13,701</td>
<td>1.4%</td>
<td>15,500</td>
<td>1.3%</td>
</tr>
<tr>
<td>11 Ministry of Food, Agriculture, Light Industry</td>
<td>10,223</td>
<td>1.1%</td>
<td>16,337</td>
<td>1.3%</td>
</tr>
<tr>
<td>12 Minister of Environment and Tourism</td>
<td>8,395</td>
<td>0.9%</td>
<td>7,300</td>
<td>0.6%</td>
</tr>
<tr>
<td>13 Ministry of Foreign Affairs</td>
<td>1,079</td>
<td>0.1%</td>
<td>2,875</td>
<td>0.2%</td>
</tr>
<tr>
<td>14 Others</td>
<td>33,206</td>
<td>3.5%</td>
<td>47,776</td>
<td>3.9%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>955,626</strong></td>
<td><strong>100%</strong></td>
<td><strong>1,217,551</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

Source: The Government of Mongolia, Fiscal budget for 2019
CURRENT STATE: PUBLIC FINANCING

Foreign Grants and Loans

- Mongolia is still reliant on foreign loans.
- China and Japan are the biggest financiers of investment projects in Mongolia.

![Bar Chart showing Public external debt by country, March-31 2019 (USD Thousand)](chart.png)

Source: Central Bank of Mongolia, Mongolia’s Gross External Debt Position
Development Bank of Mongolia

- Established in 2011 to provide financing of large-scale projects and programs for Mongolia’s development.

- Some infrastructure projects financed by DBM in the past are:
  - Railway of 23.4km connecting an iron ore mine in northern Mongolia to the main railway system.
  - Paved road of 240km between Tavantolgoi coal mine in southern Mongolia and the border between China.
  - Capacity building of Combined Heating and Power plant #4, the main power generator in Mongolia.

- By the end of the 2018, total loans and advances were MNT2,800.8 billion.

Source: Development Bank of Mongolia, 2017 Annual Report
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5. Conclusions and proposed way forward
CURRENT STATE: PRIVATE FINANCING

Concentrated in ICT and energy sectors.

Almost no private sector investments towards the transportation sector including paved roads, railway, etc.

ICT

- Mongolian private sector owns approximately half of all fiber optic lines in Mongolia and all of mobile and IPTV networks.
- These are financed primarily by foreign equity, foreign loan, and vendor financing.
CURRENT STATE: PRIVATE FINANCING

Energy

• Private investors have also been active in the energy sector, mostly wind and solar power plants, in recent years.
  • Tariffs are fixed and the government is obliged to purchase all outputs generated by the independent power plants.
• Infrastructure project that was implemented by the private sector: “Salkhit Wind Farm”
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CURRENT STATE: PUBLIC-PRIVATE PARTNERSHIPS (PPPS)

• Until 2017, many Build-Transfer (BT) contracts were awarded to private companies by various line ministries, UB city, and municipal governments.

• The Government has executed 42 concessional agreements with total project cost of MNT 2,628 billion (US$986 million), 25 projects have completed construction. (the Law on Concession was passed in 2010)

• The PPP function of the government is under the responsibility of the PPP Division of National Development Agency.

• One of the conditions of IMF funding in May 2017 was to stop any new BT contracts and consolidate PPP into the general budget of the government.

• The balance of payables to the existing BT contracts are being paid gradually, which still keeps putting pressure on government budget.

• Now - 12 projects with total project cost of 464.8 billion MNT (US$174 million) on the Concession List approved by the government (BOT).
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CURRENT STATE: BELT AND ROAD INITIATIVE

• China proposed the BRI in 2013 to improve connectivity and cooperation on a transcontinental scale.

• Countries that lie along the Belt and Road corridors are ill-served by existing infrastructure and by a variety of policy gaps. As a result, they undertrade by 30 percent and fall short of their potential FDI by 70 percent. (Source: “Belt and Road Economics” (2019), World Bank.)

• BRI transport corridors will help in two critical ways - lowering travel times and increasing trade and investment.

• Travel times will decline by up to 12 percent once completed.

• Travel times with the rest of the world are estimated to decrease by an average of 3 percent, showing that non-BRI countries and regions will benefit as well.

• Reconstruction of the paved road between Ulaanbaatar and Darkhan is part of the Russia-Mongolia-China corridor identified in the BRI and has a high priority from the government of Mongolia.

• “Belt and Road Economics” (2019) report by the World Bank indicates:

  “Azerbaijan, Mongolia, and Tajikistan could experience negative welfare effects because infrastructure costs would exceed gains from integration.”
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Fiscal balance

- Fiscal surplus only twice in the past 10 years (2010 and 2018).
- Implementation of big mining projects and high commodity price in 2010 and 2011 supported budget revenue significantly. But the budget expenditures started increasing significantly from 2012.

Source: Mongolian Statistical Information Service and Reserve Bank of Australia
CHALLENGES: PUBLIC FINANCING

Current account balance

The volatile nature of current account balance due to heavy reliance on mineral exports.

Source: World Bank Data, Current Account Balance (% of GDP)
Government revenue

- The mining sector - 33% of total government revenue and 11% of GDP in 2011 (when FDI inflows peaked at US$4.7 billion)

- In 2016, mining-related government revenue dropped to 15% of total government revenue and 3.1% of GDP

- In 2017, mining revenues went up to MNT1.6 trillion and 21% of total budget revenue and over 6% of expected GDP.

Source: GROWING WITHOUT UNDUE BORROWING, Enhancing efficiency of spending and revenue, World Bank
Government revenue

The amount of grants Mongolian government receives from development partners and foreign countries is not significant and is volatile.

Source: International Monetary Fund, World Revenue Longitudinal Data
Government expenditures

- The capital expenditures by the government is especially volatile.
- The main driver of the increase in capital expenditure was off-budget expenditures in 2012-2015.
- The DBM’s off-budget expenditures averaged 5.9% of GDP in 2012-2014.

Source: GROWING WITHOUT UNDUE BORROWING, Enhancing efficiency of spending and revenue, World Bank
**CHALLENGES: PUBLIC FINANCING**

**Public debt**

- Significant increases:
  - In 2011 - “Chinggis Bond” to finance important infrastructure projects.
  - In 2017 - IMF EFF (a total of USD5.5 billion loans from IMF and other parties).
  - The debt level of 84.7% in 2017 (Ceiling of 85% by the Fiscal Stability Law)
  - The current debt-to-GDP ratio - One of the highest (far exceeding the 45.5% average of middle-income countries and the 35.6% average of low-income countries in 2015)

![Public external debt (USD million)](image)

Source: Central Bank of Mongolia, Mongolia’s Gross External Debt Position
CHALLENGES: PUBLIC FINANCING

Public debt

The components of government borrowing as percentage of GDP.


Source: GROWING WITHOUT UNDUE BORROWING, Enhancing efficiency of spending and revenue, World Bank
Public debt

- Bilateral loans are the largest part of government borrowings at 54%.
- China (including a USD2 billion swap line between the Bank of Mongolia and the People’s Bank of China) has the highest share of 59.7% (Excluding loans from donor agencies)
- Japanese government is the second largest lender at 26.3%.

Source: Central Bank of Mongolia, Mongolia’s Gross External Debt Position
Concessional debt

- Decreased significantly in the past few years as Mongolia became a low-middle income country.

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Foreign Direct Investment

- Very high correlation between FDI and GDP growth rate.
- Historical high - USD4.57 billion in 2011 (when the GDP growth also hit a record high of 17.3%)
- The main reason for the volatile nature of FDIs is that it is concentrated in mining sector.

Source: World Bank, Consultant
CHALLENGES: PRIVATE FINANCING

Foreign Direct Investment

• Concentration on mining sector – Not enough diversification in economy.

• Usually include investments in related vital infrastructures (power plant for processing; roads and railways for transportation)

Source: Mongolian Statistical Information Service
Banking sector

- Has grown significantly (measured in total assets, loans, and deposits as a share of GDP)
- NPL ratio has increased to 10% in 2018 due to legacy loans to construction and mining sectors from the economic slowdown of 2014-2016.

Source: Consultant estimation based on balance sheet of banks from Central Bank of Mongolia
**Banking sector**

**Sectoral breakdown of commercial bank loans**

<table>
<thead>
<tr>
<th>Sector</th>
<th>Amount (millions of MNT)</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Agriculture, forestry, fishing and hunting</td>
<td>282,080</td>
<td>1.3%</td>
</tr>
<tr>
<td>2. Mining and quarrying</td>
<td>1,489,921</td>
<td>6.7%</td>
</tr>
<tr>
<td>3. Manufacturing</td>
<td>1,303,774</td>
<td>5.9%</td>
</tr>
<tr>
<td>4. Electricity, gas, steam and air conditioning supply</td>
<td>100,357</td>
<td>0.5%</td>
</tr>
<tr>
<td>5. Water supply, sewerage, waste management and remediation activities</td>
<td>10,850</td>
<td>0.0%</td>
</tr>
<tr>
<td>6. Construction</td>
<td>1,079,051</td>
<td>4.9%</td>
</tr>
<tr>
<td>7. Wholesale and retail trade, repair of motor vehicles and motorcycles</td>
<td>5,342,879</td>
<td>24.1%</td>
</tr>
<tr>
<td>8. Transportation and storage</td>
<td>409,641</td>
<td>1.9%</td>
</tr>
<tr>
<td>9. Accommodations and food services activities</td>
<td>259,683</td>
<td>1.2%</td>
</tr>
<tr>
<td>10. Information and communication</td>
<td>99,251</td>
<td>0.4%</td>
</tr>
<tr>
<td>11. Financial and insurance activities</td>
<td>417,798</td>
<td>1.9%</td>
</tr>
<tr>
<td>12. Real estate activities</td>
<td>882,434</td>
<td>4.0%</td>
</tr>
<tr>
<td>13. Professional, scientific and technical activities</td>
<td>41,769</td>
<td>0.2%</td>
</tr>
<tr>
<td>14. Administrative and support service activities</td>
<td>45,714</td>
<td>0.2%</td>
</tr>
<tr>
<td>15. Public administration and defense, compulsory social security</td>
<td>1,597</td>
<td>0.0%</td>
</tr>
<tr>
<td>16. Education</td>
<td>116,927</td>
<td>0.5%</td>
</tr>
<tr>
<td>17. Human health and social work activities</td>
<td>90,453</td>
<td>0.4%</td>
</tr>
<tr>
<td>18. Other</td>
<td>10,164,008</td>
<td>45.9%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>22,138,186</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

Source: Central Bank of Mongolia, Loan statistic
CHALLENGES: PRIVATE FINANCING

Banking sector

• Loan maturity - up to 3 to 5 years with monthly repayments.

• Lacking long-term MNT funding, the banks are not able to fund long-term infrastructure projects.

![Standard loan](chart1.png)

| Source: Central Bank of Mongolia, Loan statistic |

![Loan weighted average maturity](chart2.png)

| Source: Central Bank of Mongolia, Loan weighted average maturity historical data |
CHALLENGES: PRIVATE FINANCING

Banking sector

- Lending rate for investment loans in MNT – 18% to 24%.
- Usually have monthly repayments schedule, adding pressure on project cash flow.
- Although interest rate in Mongolia is declining slowly in the past few years, it is still formidably high for financing infrastructure.

Source: World Bank, Data, Lending Rate (%)
CHALLENGES: PRIVATE FINANCING

Capital Market

- So far, there have been no cases of using the capital market to finance infrastructure projects.

- The largest IPO so far has raised only MNT17.6 billion (approximately USD6.7 million), not enough to finance any large infrastructure projects.

**Stocks**

<table>
<thead>
<tr>
<th>#</th>
<th>Symbol</th>
<th>JSC name</th>
<th>Industry Sector</th>
<th>Listed date</th>
<th>Total raised capital (MNT)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>INV</td>
<td>Invescore</td>
<td>NBFI</td>
<td>5/22/2019</td>
<td>17,600,000,000</td>
</tr>
<tr>
<td>2</td>
<td>MFS</td>
<td>Monos Foods</td>
<td>Food supplement</td>
<td>12/17/2018</td>
<td>8,585,858,960</td>
</tr>
<tr>
<td>3</td>
<td>ADB</td>
<td>Ard Credit</td>
<td>NBFI</td>
<td>11/30/2018</td>
<td>4,900,000,000</td>
</tr>
<tr>
<td>4</td>
<td>TUM</td>
<td>Tumen Shuvuut</td>
<td>Food</td>
<td>8/16/2018</td>
<td>10,000,000,000</td>
</tr>
<tr>
<td>5</td>
<td>AIC</td>
<td>Ard Insurance</td>
<td>Insurance</td>
<td>6/13/2018</td>
<td>5,250,000,000</td>
</tr>
<tr>
<td>6</td>
<td>MNDL</td>
<td>Mandal Insurance</td>
<td>Insurance</td>
<td>5/7/2018</td>
<td>7,491,619,200</td>
</tr>
<tr>
<td>7</td>
<td>ERDN</td>
<td>Erdene Resources</td>
<td>Mining</td>
<td>4/4/2018</td>
<td>2,494,720,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Development Corporation</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>8</td>
<td>MBW</td>
<td>Mongol Basalt</td>
<td>Manufacturing</td>
<td>4/5/2018</td>
<td>6,431,538,000</td>
</tr>
<tr>
<td>9</td>
<td>LEND</td>
<td>LendMN</td>
<td>Fintech</td>
<td>1/26/2018</td>
<td>5,000,000,000</td>
</tr>
<tr>
<td>10</td>
<td>ITLS</td>
<td>Itools</td>
<td>IT</td>
<td>9/27/2017</td>
<td>1,338,798,000</td>
</tr>
</tbody>
</table>

**Corporate bonds**

<table>
<thead>
<tr>
<th>#</th>
<th>Symbol</th>
<th>JSC name</th>
<th>Industry Sector</th>
<th>Listed date</th>
<th>Total raised capital (MNT)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>SUU Bond</td>
<td>Suu</td>
<td>Dairy</td>
<td>6/29/2017</td>
<td>6,000,000,000</td>
</tr>
</tbody>
</table>

Source: Mongolian Stock Exchange, Consultant
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4. Infrastructure financing: Opportunities and Modalities
   A. Public financing
   B. Private financing
   C. Public-Private Partnership (PPPs)
   D. Multilateral Development Banks and International Development Agencies
5. Conclusions and proposed way forward
### CHALLENGES: PRIVATE FINANCING

#### Public-Private Partnerships

The UN ESCAP PPP-Readiness Self-Assessment tool

Source: UN ESCAP, Public-Private Partnerships Readiness Assessment
### I. General Background Environment

1. GDP growing at an acceptable rate
2. Business confidence high
3. Stable exchange rate
4. Ease of establishing business
5. Few restrictions on repatriation of profits
6. Convertibility of foreign exchange
7. Financial sector experienced in assessing long-term lending decisions
8. Property rights effectively enforced, and compensation for expropriation is fair

### II. PPP Policy Framework and, Social and Political Environment

9. Broad political support for PPPs
10. Clear allocation of Authority / Responsibility
11. Distinct process for unsolicited PPP proposals in policy framework
12. Viable projects generated
13. Clear criteria for government financial support
14. Positive track record or political “Champion”
15. Civil society views PPPs as viable means of providing infrastructure and basic services
16. Funds available for projects with added social welfare purpose
17. Resettlement and rehabilitation provided for communities disrupted by PPP projects

### III. PPP Legal and Regulatory Framework

18. Legal basis for private sector participation
19. Limited restriction on foreign investors
20. Clear authority and procedure for acquiring rights of way
21. Regulatory rules and authority are clear for all PPP types expected
22. Price and quality of PPP monopolies regulated to protect consumers and others
23. Environmental laws are clear and transparent and are all available from a single source

### IV. PPP Institutional Capacity

24. Staff aware of legal, financial and basic technical issues in PPP projects
25. Defined government mechanisms in place to coordinate PPP needs
26. Technical capacity sufficient to ensure construction and service standards
27. Staff can assess outside work, including feasibility studies and risk mitigation strategies
28. Provision for assisting line agencies and local government in undertaking PPP projects
29. Arrangements for risk sharing are sensible and manageable
30. PPP documentation/best practices available in the public domain

### V. PPP Process: Project selection, contracting and post selection

31. Transparent procedures specified for all stages of the PPP process
32. Bidders given proper information, including requirements for submitting proposals
33. Competitive tendering process is transparent in practice
34. Objective criteria for project sponsor selection are known and applied
35. Defined performance requirements available prior to bidding
36. Contracts for PPP are irrevocable except through due process
37. Conflict resolution process is clear, including alternative to judicial resolution
38. International arbitration recognized and effective for dispute resolution
39. Ruling by technical and economic regulators can be appealed
Public-Private Partnerships

Mongolia is expected to score low in following indicators:

1. **General Background Environment**
   - “Business confidence high”
   - “Stable exchange rate”
   - “Financial sector experienced in assessing long-term lending decisions”

2. **PPP Policy Framework and, Social and Political Environment**
   - “Distinct process for unsolicited proposals”
   - “Clear criteria for government financial support”

3. **PPP Legal and Regulatory Framework**
   - “Clear criteria for government financial support”
   - “Funds available for projects with added social welfare purpose”

4. **PPP Institutional Capacity**

5. **PPP Process: Project selection, contracting and post selection**
   - “Transparent procedures specified for all stages of the PPP process”
1. Introduction

2. Current state of Infrastructure financing
   A. Lack of Infrastructure in Mongolia
   B. Public financing
   C. Private financing
   D. Public-Private Partnership (PPPs)
   E. Belt and Road Initiative

3. Infrastructure financing: Challenges
   A. Public financing
   B. Private financing
   C. Public-Private Partnership (PPPs)

4. Infrastructure financing: Opportunities and Modalities
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5. Conclusions and proposed way forward
Fiscal Discipline

The IMF concluded that strong policy implementation and a supportive external environment have helped Mongolian government over-perform the fiscal target under the program. (the Fifth Review of the EFF program in July 2019)

Some important steps were made on fiscal structural reforms:

• Any net increase to the subsidized mortgage loans are now included in the general budget.

• Spending by DBM is now included in the budget, i.e. on-budget.

• Effective ban on new PPP contracts on a BT basis.

Policy recommendation 1:

• Ensure the fiscal and monetary policy reforms made since 2017 under the IMF EFF program are not reversed, and continue with structural reforms to improve fiscal discipline, e.g. stopping subsidy on fuel prices, inclusion of the government mortgage program in the budget, and targeting social spending programs based on need.
Tax reform

• Corporate income tax rate will be decreased from 10 percent to 1 percent for business entities with annual turnover under MNT300 million (USD115,000).

• The threshold for 25 percent tax rate for pre-tax income was moved up from MNT3 billion to MNT6 billion.

• Success story: VAT – “E-Barimt” system was introduced in 2016.

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<thead>
<tr>
<th></th>
<th>2016</th>
<th>2017</th>
<th>2018</th>
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</thead>
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<td>VAT Revenue</td>
<td>1,140.7</td>
<td>1,619.2</td>
<td>2,196.4</td>
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</tbody>
</table>

Source: Mongolian Statistical Information Service

• Increasing User Charges

Policy recommendation 2:

• Continue implementing policies, such as tax reform, that are expected to increase government revenue in the long term.

• These policies should be based on extensive research and learn from past experiences by other countries.
Future Heritage Fund (sovereign wealth fund)

- Will be injected with 65% of all mining royalties and the dividends from state-owned mining companies collected by the government.
- The Government of Mongolia - inject MNT553 billion (USD217.3 million) in 2019.
- After that, MNT1 trillion (USD392.9 million) each year.
- Currently, the fund has total asset of MNT213 billion (USD80 million).
- The fund will be allowed to directly invest only in foreign exchanges. However, the fund must contribute 10% of its net income each year from 2030 to the general budget of the government.

Policy recommendation 3:

- Ensure there is no political influence on the operations of the Future Heritage Fund and use the proceeds from the future dividends for financing projects that have the highest priority.
Privatization

• Sale of state owned enterprises (SOEs) - Extra revenue for the government and potentially generates higher tax revenue under private management.

• In 2015, the parliament issued a list of SOEs to be privatized in 2015-2016.

• Although this list included major SOEs such as CHP3, CHP4, Mongolian Stock Exchange, and state-owned shares of some large mining companies, none of these companies have been actually privatized so far.

Policy recommendation 4:

• If necessary, update the privatization list of 2016 and start privatization using international best practices.

• If necessary, request technical assistance from experienced development agencies on the most efficient and effective ways of privatizing government assets.
OPPORTUNITIES AND MODALITIES: PUBLIC FINANCING

Development Bank of Mongolia

• In October 2018 - DBM successfully raised a five-year, USD500 million bond from international capital market (7.25% coupon).

• The first such bond to be issued by a quasi-government institution without a government guarantee.

• The fact that a quasi-government institution could borrow on the international market without a government guaranty is significant and opens new potentials for financing large scale projects.

Policy recommendation 5:

• Ensure the independence of DBM and allow the environment for it work for its mandate to invest in large-scale projects important for Mongolia’s development.
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OPPORTUNITIES AND MODALITIES: PRIVATE FINANCING

Foreign Direct Investments

• 70% FDI in Mongolia is in mining sector - Focus on the mining sector and the factors that might incentivize investment in this sector.

• Large scale mining projects usually have components of infrastructure in terms of power generation, paved road, and railway.

• But non-mining FDI also has great potentials: agribusiness, energy sector, etc.

Policy recommendation 6:

• Strengthen the capacity of the division inside the NDA that is responsible for investment promotion.

• In the long term, consider the creation of an independent investment promotion agency.

• Ensure the investment policies towards foreign investment are consistent and honored by the government.
**OPPORTUNITIES AND MODALITIES: PRIVATE FINANCING**

**Capital Market**

- There is an increased interest from individual investors towards the stock exchange (not enough for developing a broad capital market that can support large scale infrastructure projects.)

- A close cooperation among the various government ministries and agencies, the MSE, and the professional service providers on the stock exchange is needed to resolve the issues

**Policy recommendation 7:**

- Develop a long term strategy to improve corporate governance, create institutional investor base, and improve investment knowledge level about capital markets.

- Privatization or long-term lease of MSE to experienced international stock exchanges should be considered by the government. Since it was included in the privatization list of 2016, it will not be a totally new undertaking by the government.
OPPORTUNITIES AND MODALITIES: PRIVATE FINANCING

Public-Private Partnerships

• Compared with public procurement, PPPs place significant demand on the government at all stages, from pre-project preparation to contract negotiation and management, and complexities multiply alongside project scale.

• A successful implementation of PPP can be an alternative way for financing necessary infrastructure project without much pressure on public finances.

Policy recommendation 8:

• Legal and regulatory framework should be updated to adapt to the current legal structure in Mongolia. The Law on Concession should be updated.

• Connection between PPP and public investment programs should be clarified.

• Institutional stability should be obtained to ensure the agency in charge of PPP and its staff accumulate know-how and experience in the long run.

• Implement a successful pilot PPP project with support from donor agencies.
OPPORTUNITIES AND MODALITIES: PRIVATE FINANCING

Multilateral Development Banks and International Development Agencies

Financing by multilateral development banks (e.g. World Bank, ADB, EBRD, IFC) and foreign development agencies (e.g. JICA) remain to be one of the largest sources of foreign investment into Mongolia. Through partnership with government and private sector, they have directly financed most large-scale infrastructure projects in Mongolia.

- IFC – InfraVenture Fund
- ADB - Asia Pacific Carbon Fund
- Canadian Climate Fund for the Private Sector in Asia

**Policy recommendation 9:**

- Work closely with climate oriented finance institutions such as Green Climate Fund to explore opportunities for financing infrastructure projects.
- Explore the many ways, not just debt or equity financing, donor agencies can support developing countries in developing infrastructure.
THANKS FOR YOUR ATTENTION