

# Stability and growth

## INTERVIEW WITH NAMID BAYARTSAIKHAN

MINISTER OF FINANCE, MONGOLIA



**NAMID BAYARTSAIKHAN** is Minister of Finance of Mongolia and has considerable experience in finance and economics.

### What are the current guiding principles of financial policy in Mongolia?

The guiding principles of financial sector reform in Mongolia are financial stabilisation, liberalisation and privatisation.

As of the end of 2006, 16 commercial banks, 18 insurance companies, more than 200 non banking financial institutions and 22 brokerage companies were operating in the Mongolian financial sector, and they provide a variety of financial services. In November 2006, we successfully privatised our last state owned commercial bank 'Savings Bank'. It means that the Mongolian financial sector has been fully privatised and depends on the initiatives and operations of the private sector.

The Government of Mongolia pays great attention to financial stabilisation, liberalisation and the structural adjustment of the economy. It accepts the need for reforms, and the creation of new stable norms in the financial sector.

Recently, the Mongolian Parliament adopted the "Law against money laundering and terrorism", "Anti-corruption law" and "Law on the status of Financial Regulatory Agency". We hope that by adopting these laws, Mongolia has made a step forward in the establishment of sound financial sector development.

Mongolia's sovereign credit rating in the international market is improving from year to year. By the evaluation of international financial institutions, Mongolia's overall status became positive, with short term and long-term credit rating at B and B+ accordingly. The upgrades were attributed to Mongolia's strong growth prospects and the ongoing reductions in government debt underpinned by improved fiscal indicators which will result in investor confidence in the country's economic and financial prospects. This ranking reflects the country's political and economic stability, sound macro-economic fundamentals and the positive business environment.

### What are the key challenges in establishing high and sustained economic growth rates in Mongolia?

Funding requirements are enormous in the production and service sectors in Mongolia. We believe that our economic growth will result from the effective

utilisation of mining deposits and raw materials such as wool, cashmere and leather processing production through advanced technology. In this sector Mongolia has significant mineral deposit resources and raw materials. In the area of macro-economic management and taxation, Mongolia has created reasonably favourable conditions. Transport costs to export markets are still high and we are addressing this issue. We are working on further improvements to our railways and roads with the assistance of our external partners and are cooperating with investors in the mining sector. I personally believe that Mongolia will find the best way to resolve this issue before too long.

A wide ranging debate amongst the relevant stakeholders in the mining sector and their expression of interest may be viewed by some foreign investors as a difficulty in the sector. However, I assume, this is an inevitable process that will bring us the optimal utilisation of our mining deposits.

### How do you address the relative importance of foreign direct investment versus domestic investment with regard to Mongolia's economic stability?

Obviously, foreign direct investment is essential to any economic development, firstly because it does not involve debt or debt responsibility to the receiving country and secondly it is a transfer mechanism for both technical and management skills and knowledge.

Skills transfer from developed countries is equally essential to funding flows as plays an important role in the future development and progress of our country.

In recent years, foreign direct investment increased significantly. According to statistics the majority of the investments are aimed at the mining sector. The Foreign investment relations are regulated by the Constitution of Mongolia, Law on Foreign Investment and other related laws and legislation and the international treaties and agreements of which Mongolia is part.

We pursue an equal treatments policy such as granting concessions and exemptions to both foreign and domestic investors. Here I would like to mention an example. The amount of investment budget planned in 2007 is equal to the amount made in the last 4-5 years which reveals the country's enormous financial and funding needs for achieving its development goals.

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The country's financial capacity is increasing and internal funding and investment flow is strengthening not only as a consequence of foreign investment but also as a result of economic growth. The government of Mongolia places a major emphasis on furthering these positive trends.

#### **What is the policy on corporate and individual taxation – do you foresee further changes to the tax system?**

Tax policy became one of the most important issues facing the Government of Mongolia, taking into account its impact on investment, business development, and economic growth. In July 2006, Mongolia's parliament enacted a far-reaching tax reform. The new tax reform package includes the following:

- Corporate Income Tax (CIT), which consisted of two brackets, 15 per cent and 30 per cent were both lowered by 5 per cent each. The threshold increased to 3 billion MNT.
- Personal Income Tax (PIT) decreased to a 10 per cent flat rate and increases the credit threshold to 84,000 MNT/month from 48,000 MNT/month.
- Value added tax (VAT) decreased to a flat 10 per cent from the current 15 per cent.

Even though the tax revenue will be decreased substantially and expenditures are rising, the overall policy is to maintain a sustainable fiscal position. The main objectives of the reforms of the package of tax laws are to decrease the tax burden, encourage enterprises and reduce the unequal burden of taxes. We also believe that these tax regime policies will have other beneficial effects such as the steady reduction in the shadow economy, the expansion of the tax base, increasing tax collection efficiency, the elimination of various tax exemptions and holidays, and the creation of a fair environment for tax payers which will improve compliance and reduce complexity by clarifying and simplifying the tax laws. There is also greater focus on working to tighten the tax administration and improve tax collection efficiency and revenue productivity from different sectors such as the efficient use of tax revenues from the mining sector.

#### **You have pursued a tough monetary policy in Mongolia-what impact is this having on the interest rate environment?**

Thanks to a tough monetary policy pursued by the Bank of Mongolia, the weighted average interest rates of the commercial banks is decreasing gradually. However, this decline is rather slow. This also indicates that a tough monetary policy has no significant affect in reducing the interest rate on loans. For instance: the weighted average loan borrowing interest in Mongolian tugrugs was 28.3 per cent and

in US dollars 14.8 per cent in 2005 while it decreased slightly to 24.5 per cent for Mongolian tugrug and to 15 per cent for the US dollar loans respectively by the end of 2006.

#### **What are your forecasts for the key economic indicators in Mongolia over the medium term?**

Real economic growth for the years 2007-2010 are projected to be on average 12 percent. We are planning to exploit two of the largest mines Oyu tolgoi and Tavantolgoi. Due to the exploitation of these large fields in the years 2009 and 2010, economic growth during this time is projected to accelerate to 15-16 percent. On the other hand, the consumer price index is estimated to be stable and fluctuating below 5 percent. We are projecting that external trade and current account balance of payment's surplus will amount to approximately 10 percent of GDP. In parallel to trade and BOP surpluses foreign reserves will certainly increase significantly. Macro-economic indicators tend to be stable in the mid-term. As these large mining fields are exploited and utilised for the economic cycle this in turn will have a positive effect on public finances and the budget as the overall budget balance will result in a sustainable macro-economic situation.

#### **What is your vision for Mongolia's economic development over the coming years?**

Researchers and academics within the framework of a working group representing the government, have prepared "*Mongolian National Development Strategy*" and it is planned for submission to the parliamentary session. Within the framework of this long term policy, by the year 2021 Mongolian GDP per capita is projected to reach US\$12,000. And surely, this will result in increasing competitiveness and production diversification in Mongolia. Every Mongolian's health, future, life expectancy and capacity will be significantly improved. We will follow a strategy, over the next 15 years, to process leather, cashmere, natural resources and many other raw materials to improve and increase the economic benefits. Since 1990, we have enjoyed seventeen years of improving macro-economic management. Throughout these years we believe we have gained enough experience to employ a market based economy. In the future, we believe we can further perfect this market based economy. We are aiming to reach a high level of development by exploiting our natural resources together with the world's best technology. We are striving hard to achieve this without losing time. I have expressed my wishes and desires in this interview with FIRST. The Mongolian government will work hard to make it a reality. **F**