

Lessons from Mongolia's Transition to the Market

Paper prepared for the UNDP Transition Conference,
Hanoi, Viet Nam, May 31st to June 1st, 2004

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Executive Summary

- i. Mongolia, unlike other Asian Transitional economies, has since 1990 pursued a 'shock-therapy' or 'big bang' transition to a market economy. This has entailed rapid liberalisation, de-regulation, and mass privatisation, accompanied *inter alia* by stringent stabilisation policy.
- ii. The transition period has, for the most part, been characterised by weak levels of economic growth, and increased levels of poverty and income inequality, and deteriorating human development. Such outcomes, are however, far from uncommon for countries adopting a rapid transition strategy, and it has been argued that Mongolia's performance, relative to others pursuing similar policies, has been considerably better than the norm. And stabilisation measures succeeded in curbing an episode of hyperinflation, currency depreciation and a balance of payments crisis within four years of the initial transition.
- iii. As a landlocked nation located within the interior of a vast continent, Mongolia faces extraordinary developmental challenges given by its climate and topography. It has one of the lowest population densities in the world, and entered the transition period in a comparative state of backwardness, being without any significant infrastructure, and with its industrial base and agricultural sector poorly adapted to the global market place. Mongolia also suffered some very significant exogenous shocks during the transition, including the withdrawal of capital transfers from the former Soviet Union which were estimated to be equivalent to 30% of GDP.
- iv. Yet the nation possessed and retains distinct advantages. These are given by its huge and largely untapped mineral wealth, and in common with other ex-socialist nations, it has an educated and healthy population. In addition, Mongolia has also been the recipient of significant levels of aid, which by the late 1990s, had come represent approximately the same share of GDP once accounted for by the soviet subsidies referred to above.
- v. Policy making in Mongolia's early transition was fragmented and confused. Several reforms were hurried and poorly sequenced, and it is likely that the consequences of these failures were severe both for the economy and the livelihoods of ordinary Mongolians. Economic policy has remained avowedly laissez-faire in nature and has only latterly shown signs of adaptation. This lack of attention paid to the wider developmental agenda has given rise to a variety of economic and social weaknesses.

vi. Although it is difficult to make firm conclusions on the contribution of individual policies to outcomes, this report finds, for the overall period, in relation to:

- Economic outcomes; that the speed of reform deepened the initial recession, and that poor phasing of price liberalisation, undertaken prior to banking reform and a weak supply response, contributed greatly to the hyperinflation experienced in 1992 and 1993. Moreover, that strong adherence to laissez-faire economics in the early and mid transition, both weakened growth, and may have compromised longer term economic development objectives.
- Poverty and income inequality; that the extent, depth and severity of poverty are exceptionally high in Mongolia and a nation which began the transition with no discernable poverty is now estimated to have over a third of its population subsisting living below the official absolute poverty line. Moreover, that transition policies tended to be made in ignorance of their effects on the poor, and have on occasion directly contributed to worsening income inequality. This is most clear in relation to the methods of privatisation adopted, and this has compromised the prospects for pro-poor (i.e. poverty reducing) economic growth from emerging.
- Social outcomes; that the transition has seen declines in both educational and health outcomes; with the most severe effects being felt in terms of worsening maternal mortality and life expectancy. Furthermore, that there are clear connections between these outcomes and the conduct of the transition strategy. These range from the pressure on public budgets, to the nature of the coping strategies which ordinary citizens were forced to adopt.

vii. Yet in spite of the general adherence to shock-therapy, there is evidence of policy learning by Government during the period, and it is possible to discern four stages in the evolution of policy;

- The initial transition, characterised by a 'dash for change', predicated on the political imperative of cementing the new order.
- A consolidation phase, given not by a slowing of the pace of reform, but a period of consistent implementation.
- An acceleration and rejuvenation following the election of a new and even more pro-market Government.
- A mature stage, characterised by policy adaptation and innovation.

- viii. The capacity and competence of policy making has also improved with time. Whilst it is apparent that stewardship in the early years was characterised by administrative confusion and the poor phasing of reforms, recent economic management is more outcome focused, and the Poverty Reduction Strategy Paper (PRSP)¹ preparation process has played a part in this.
- ix. It also must be made clear, that of all of the nations undertaking the transition to the market, Mongolia's record in the political sphere is exemplary. Political and constitutional change has been secured without the 'stain' of political violence.
- x. This report finds that although the adopted strategy was carried out with the consent of the Mongolian people, the conduct of policy, particularly in the early and mid stages, contributed to economic and social dislocation. Whilst it is evident that the resulting retrenchment was shorter-lived and in some senses less severe² than others pursuing the same strategy, it is equally clear that thus far, the performance of Mongolia's Asian neighbours, who have pursued 'gradualist' transition policies, has been strikingly better.
- xi. Social and economic outcomes have only recently begun to strengthen and only time will tell if Mongolia's course of shock-therapy will prove a price worth paying for longer term prosperity.

¹Referred to in Mongolia as the Economic Growth and Poverty Reduction Strategy (EGSPRS)

² Comparisons of relative severity are inevitably problematic; whilst Mongolia's GDP compression is relatively low at 22%, the poverty impacts and the reduction in domestic absorption are sizeable.

Introduction

1. Mongolia's transition process, which was characterised by a 'shock-therapy' of rapid price and trade liberalisation, deregulation, and mass privatisation, is without parallel in East Asia and stands in direct contrast to the 'gradualist' approaches favoured by China and Vietnam.
2. Mongolia's policy choices and experience have much more in common with her northern neighbour, Russia, and the wider Commonwealth Independent States (CIS), and this apparent disjuncture makes Mongolia an excellent case study with which to examine the series of contested questions which dominate the debate over transition strategies. The most significant of these, is whether the negative effects of 'shock-therapy' type policies will prove transitory, and that early rapid reform will secure in time, an economic vitality capable of outstripping the performance of the 'gradualists'?
3. The objective of this paper is to assist that debate by reviewing Mongolia's transition experience; the policy choices made and the consequent social and economic outcomes. This paper has been based largely on secondary materials (referenced throughout the text and listed in the bibliography), but it has also drawn on a series of interviews carried out with local policy makers and commentators, a list of whom is provided as an Appendix.
4. The paper has five principal sections:
 - The first provides essential background on Mongolia and the context within which the transition has taken place.
 - The second documents the policies adopted, their chronology and adaptation through time.
 - The third part then analyses the impact of policies, and their interplay with domestic and external events, this is done with reference to both economic performance and the wider the socio-economic agenda.
 - The fourth section reviews the overall effectiveness of the transition strategy and offers conclusions.
 - The fifth and final section provides a very brief outline of the key developmental challenges faced for the future.

Part I: Context and the Pre-existing Conditions

5. Mongolia is a vast landlocked country with a sparse and unevenly distributed population, and an unforgiving climate. It ranks in terms of area as seventeenth largest in the World and fifth largest in Asia, yet has a total population of only 2.7 million and a population density of a mere 1.5 persons

per hectare. Statistics also show it to have one of the highest seasonal temperature ranges in the World, with day time temperatures in the summer averaging 30°C and falling during winter nights to a chilly 40°C below zero (Otgontuya, 2003). It also ranks amongst the 40 or so landlocked nations of the world, as one of the most remote from the sea.

6. These geographical realities make for a highly problematic economic and productive environment regardless of the challenges posed by the transition. The Mongolian economy suffers from what is frequently referred to as the 'tyranny of distance'; the costs of internal supply, moving export goods to market, and the building and maintenance of infrastructure, are often prohibitive. The harshness of the environment and its susceptibility to severe conditions intensifies the vulnerability of the population to a series of deprivations. This is made most clear during the *Dzud* (extreme winter) of 2000-2002, when exposure and then drought, resulted in the death of an estimated 11 million pastoral animals, decimating the livelihoods of rural people and the businesses which relied on them, with output from this sector recording a staggering 29% decline over the two affected years (UNDP,2004).

Figure 1: Map of Mongolia



7. Mongolia's ancient tradition of nomadic pastoralism still survives to this day with upwards of 40% of the population being directly engaged in the herding of animals, chiefly goats and sheep. Rural life styles are frequently subsistence-based, with families of herders selling their products, especially cashmere and camel wool, as a cash crop to itinerant traders.

8. The Nation's vast area and geology have also endowed it with considerable and valuable mineral resources. These include; copper, gold, molybdenum, uranium, coal, oil shale and oil. Yet although these resources represent a windfall, their presence also has implications for the structure and orientation of the economy. Together, copper concentrate and gold, now dominate exports, occupying over half of the total by value (NSO, 2003). As a result Mongolia is heavily dependent on the primary sector, and extremely vulnerable to changes in world commodity prices.
9. Mongolia's geopolitical position casts a long shadow over her developmental history. Sandwiched between two of the world's great powers, Mongolia has long been a place of change and conflict. Indeed, modern Mongolia is very much smaller than the nation of the Khans, with Inner Mongolia being permanently annexed by China in the early part of the 20th century. The declaration of an independent state in 1921 also marked the beginning of its economic and strategic, though not full political, integration within the former Soviet Union. Although central planning was not formally entrenched until the middle of the century, Mongolia came to represent a near complete command economy by the 1970s. It is this historical legacy more than anything else, which has shaped post-socialist Mongolia's transition policy choices.
10. By any objective criteria central planning under Soviet tutelage did much good for ordinary Mongolians. The social and economic gains particularly in the latter part of this period are striking. By 1989, Mongolia had transformed itself from an ex-feudal state of near backwardness into a nascent industrial nation, with economic growth rates during the 1980s, the decade before the transition, averaging 4.5% (Nixson and Walters, 2000).
11. Alongside the symbols of a modern socialist state which included its own Cosmonauts, Mongolians had come to enjoy an enviable level of human development in the context of a nomadic and pastoral society. Life expectancy in 1989 averaged 63.8 years, whilst adult literacy covered a near complete 98% of the population. A network of health and educational facilities was developed serving both town dwellers and rural nomads. A particular feature was the use of dormitory schools to educate the children of herdsmen (UNDP, 2004).
12. In addition, the socialist economy had reached a pragmatic accommodation with nomadic pastoralism. Through a series of interventions, including the provision of agricultural infrastructure (wells, marketing and distribution channels), collective services (veterinary provision and disease control) and emergency management (fodder buffer stocks), the State supported and regulated herding and its interplay with the natural environment. (UNDP/ Nixson and Walters, 2004)

13. However, the performance of the real economy was not nearly so positive. Industrialisation and agricultural production were supported by large capital inputs and ongoing subsidies financed by transfers from the Soviet Union. Analysts have valued the level of this aid to be in the region of 30% of GDP (Nixson and Walters et al, 2001).
14. Thus, well before the transition policy makers and central planners both in Moscow and Ulaanbataar were beginning to question the effectiveness and consistency of Mongolia's development strategy. As Nixson and Walters (2000) note, the externally imposed model of industrialisation was 'running out of steam', heavy plant and collective arable farms were inefficient, even by Soviet standards, and had no obvious locational rationale or market for their products. As early as 1985, measures were beginning to be taken to reorient economic objectives in line with clearer competitive advantages.
15. As a result, the economic conditions which pertain at the beginning of Mongolia's transition more closely approximate those of the CIS nations; Mongolia had a soviet-style economy, characterised by over-capitalized and poorly adapted industries, and unsustainably high consumption levels sustained by transfers from its northern patron. Yet, it also possessed significant human capital and development advantages, along with systems and structures which maintained welfare and production in extremely inhospitable climatic and geographic conditions.

Part II: The Transition

The Political Economy of Change

16. The transition began in earnest in 1990, a year before the collapse of the former Soviet Union, following tumultuous political events which closed with the resignation of the entire central committee in July of that year. These resignations led to presidential elections which saw the election of a reformist regime, which then embarked on an ambitious process of wholesale economic reform including mass privatisation and rapid liberalisation (Pomfret, 1999).
17. The new political and economic order was consolidated by the adoption of a new constitution in 1992. The constitution established Mongolia as a parliamentary democracy with a presidential head of state, a single legislative chamber headed by a Prime Minister elected every four years and an independent judiciary, and through a series of devices, enshrined the primacy of a market-led economy (Ibid).

18. Of all the transitional reforms, it is these in the political domain that have proved the most successful. In marked contrast to many other transitional nations, Mongolia has experienced no significant violence or loss of life throughout the entire transition process, and this is in spite of some highly challenging social and economic conditions. Equally, in the wake of the events of 1990, political parties, and subsequently interest groups, have taken shape within a rapidly developing and distinctly Mongolian democracy.
19. Following the acceptance of the 1992 constitution, elections were held which confirmed the former communist Mongolian Peoples Revolutionary Party (MPRP) in power. Yet in spite of its title, the MPRP became and remains, far from socialistic. In power it has made policy choices which have brought about an unrelentingly rapid transition. These policies were accelerated still further when the MPRP was defeated in 1996 by the Democratic Union (DU), and maintained when the MPRP was re-elected in 2000. Regardless of the criticism of the transition policy stance, it cannot be sustained that the Mongolian people did not consent to the shock-therapy policies favoured by government after government.

The Economic Reform Agenda

20. Drawing on the above, the orientation of policy has been remarkably consistent throughout the period. Adaptation has amounted to a sophistication rather than a rejection of the strategy, and the most significant changes in emphasis have only taken place in recent years.
21. Broadly stated, the dominant stance has amounted to a wholesale rejection of central planning, and its replacement with a laissez-faire approach to economic policy making, and a belief in the market to deliver efficiency gains, economic growth and ultimately a broadly based prosperity. The rejection of central planning was so strong that in the initial years, the State almost came to forsake any form of control or coordination. The early transition has been described as a period of 'organisational chaos' with different ministries forming administrative baronies, and subsequently pursuing divergent and often contradictory, objectives (Nixson and Walters, 2000).
22. Successive elections since then have served to consolidate coordination within government, but the official downplaying of the State's role in the development process is a facet which survives today. Indeed, Government has purposefully eschewed the kind of economic and industrial policies pursued either by the gradualist transition nations of China and Vietnam, or those associated with the East-Asian Developmental State³.

³ As associated with the economic development model adopted by Taiwan and South Korea.

Chronology of Reforms

23. In common with shock-therapies pursued elsewhere, the speed of the process has been underpinned by the imperative of affecting simultaneous changes in the nature of the economy.

The measures that were taken can be summarised as follows:

- Liberalisation of prices and trade relations, including the abolition or severe reduction of import tariffs and quotas;
- Deregulation of financial markets, including financial (i.e. interest rate) liberalisation, capital account convertibility and floating the domestic currency, the *Togrog*;
- The mass privatisation of state property, ranging from residential apartments to major enterprises;
- And a general scaling back of state regulatory activity, accompanied by the establishment of new institutions and legal instruments essential to the working of a market economy.

24. The justification for the near simultaneous implementation of these measures is typically made within the supporting literature, in terms of the 'interrelated web' of economic relations which underpin a modern market based economy, and hence, the strong complementarities and interdependencies that exist between reforms⁴. Specifically, that the objectives of transition; corporate restructuring, structural realignment of the economy and growth; can only be secured through a 'cathartic break' from the past in which new economic realities and modes of conduct are enforced. Privatisation assumes a particular centrality, as it is argued the 'soft budget constraint' enjoyed by State Owned Enterprises (SOEs) can only be curbed through the transfer of ownership (Lipton and Sachs, 1991).

25. Yet in Mongolia as elsewhere, the political imperative for shock-therapy, and the need to make the new order irrevocable, was a good deal more significant than the economic rationale in shaping strategic choice, and politics dominated the agenda well into the middle years of the transition (Marshall, Nixon and Walters 2003).

26. Equally, changes of this scale and nature clearly cannot in any practical sense, be made to occur in the same or even a proximate, time period. To generalise, the Mongolian reforms began with liberalisation and deregulation measures, followed quickly by the privatisation of small and medium

⁴ See various standard texts e.g. Estrin (1994).

enterprises and later by divestiture from the larger SOEs. For the greater part of the transition, institutional reform took place on a sporadic basis, and a significant disjuncture existed and remains, between legislative enactment and implementation.

27. Fairly early on the Government was also forced to introduce harsh economic stabilisation measures to deal with a very considerable level of inflation which emerged almost immediately after the initial liberalisation of consumer prices. Tight monetary policy and the prioritisation of price stability, often to the detriment of higher levels of economic activity, have been evident since the hyperinflation of the early 1990s.
28. The degree of consistency and pace of reform throughout the entire process, regardless of political change, is strong. Yet it is possible to discern some changes in emphasis, and dissect the transition into the four chronological stages outlined below. It is worth noting that although this disaggregation has been developed judgmentally by the author, its general shape is supported by some of the government officials interviewed in support of this paper⁵.

- Stage I - The Immediate Transition: This period refers to the two to three years following the collapse of the socialist state in 1990 and the adoption of the new constitution. This period also runs for a year or so beyond the election of the MPRP government in 1992.

This period was characterised by a strong rejection of the command economy and a 'dash' for change, but also by poor coordination and administrative failure. Several rapid, and for many ill-considered and poorly phased, reforms were undertaken, notably the over-night liberalisation during 1991, of a large proportion of consumer prices (excluding 35 essential items categories) and most imported goods prices.

As early as January 1991, privatisation by direct assignment was initiated via the issuing of vouchers to citizens. These are divided into several lower value red (or pink) vouchers for the purchase of small and medium sized enterprises, and one higher value voucher for the purchase of larger SOEs. The former are tradable on the secondary market whilst the latter can only be assigned by the owner. Privatisation of herds and the collective farms known as *Negdels* is also initiated via a framework agreed by parliament, though individual allocation decisions were left to localities and cooperatives (Otgontuya 2003, UNDP/ Nixson and Walters 2004).

⁵ Notably officials within the Ministry of Finance and Economy and the Central Bank

Some essential institutional changes also took place with the Ulaanbaatar Stock Exchange being set up in 1991, and the State Bank of Mongolia was converted into six commercial joint stock banks, and its regulatory functions separated and vested with the newly constituted central 'Mongol Bank' (Pomfret 1999).

- Stage II - Consolidation: This period, which follows after the election of the MPRP under the new constitution in 1992, is not characterised by a slowing in the pace of reform, but rather the implementation and completion of past measures. The years 1992 to 1993 see the largest number of enterprises privatised. Further price liberalisation takes place, with only a very small number of goods and services still being subject to control (chiefly the major public utilities) by the end of 1993. This period also sees the floating of the national currency (in 1993), and measures to deregulate of the capital account. However, it must be recognised that the Togrog was already subject to a 'dirty float' and had already depreciated very considerably. Import tariffs are also slashed to an across the board 10%, giving Mongolia an extremely liberal trade regime.
- Stage III - Rejuvenation and Acceleration: This third stage covers the period from 1996, following the election of the Democratic Union (DU) on a platform of still more radical reform. The new administration begins by fully completing the liberalisation of prices and abolishing all tariffs. This latter act is a considerable leap of faith since at the time tariff income represented in excess of 15% of government revenues. This action also coincides with accession to the World Trade organisation which is completed in 1997.

Mongolia's new leaders also move to accelerate the by then moribund privatisation process, announcing further sales and that major enterprises can be bought outright by foreign entities. Accompanying this, virtually all remaining restrictions on capital transactions are lifted and a series of tax holidays are offered to foreign investors. The Government also moves rapidly to complete the transfer of residential property. This is done free of charge to resident occupiers, regardless of the fact that over 50% of the population live a nomadic way of life and are thus left out of the distribution process. By the end of the DU's term in office around 97% of all residential property is in private hands.

In contrast to previous periods, more serious attention is given to institutional reforms, notably in the banking sector and the national insurance system. Banking reform is however, somewhat forced by a liquidity crisis in several major commercial banks. Nevertheless, the reforms do secure the system for future improvement and consolidation.

- Stage IV - Adaptation and Innovation: This final, or rather the latest stage in the transition, follows a change of government and the return of the MPRP to power in 2000. The new government's platform, in rhetoric at least, was far more developmental and mindful of the interests of the poor and vulnerable. But it must also be noted that their programme remains far from a reappraisal of the forgoing policy decisions. It is best described as a continuation of the past policy stance, but with a greater consideration of the outcomes, and especially the medium term consequences for revenues, employment and output. Crucially, future sales of the remaining SOEs are to be made to strategic investors, with consideration given to the regulatory consequences of reform. Alongside this, a raft of aid-funded technical assistance projects to establish utility, and economy-wide anti-trust, regulatory agencies have been initiated. Some retrenchment in liberalisation also takes place, with tariffs being re-imposed, albeit at a flat 5%, and a cashmere export tax is introduced.

Institutional reforms are given a far shaper focus. Particular efforts are made in relation to public sector reform including civil service capacity building, accounting and budgeting. This parallels the more strategic direction of policy making, signalled by a variety of national documents published from 2000 onwards. The most significant of these are the Interim PRSP completed in 2001 and the final PRSP (entitled the Economic Growth Support and Poverty Reduction Strategy) in 2003.

Yet equally, far more radical ideas are developed and begin to be implemented, including the privatisation of land, which is currently being achieved by what amounts to an assignment process without vouchers. The Government has also made clear its intention to privatise parts of the social sector, including schools and hospitals using what it describes as the 'New Zealand model' (Government of Mongolia, 2003). But the status of this latter controversial proposal remains unclear at the time of writing.

Part III: Appraisal of Performance

29. It is worth making clear at the outset of this third section that attributing emergent economic and social conditions to particular policy choices is necessarily problematic. To identify cause and effect with any clarity requires the establishment of an adequate counterfactual. Yet no such benchmark exists, since events cannot be compared to a situation where no transition took place, or one where different transition polices were deployed in the same economic environment to that faced by Mongolia in the 1990s. Thus any appraisal is at best proximate, and the most that can be done is

to track the evolution of policies alongside outcomes, and the performance of others adopting both similar and radically different strategies.

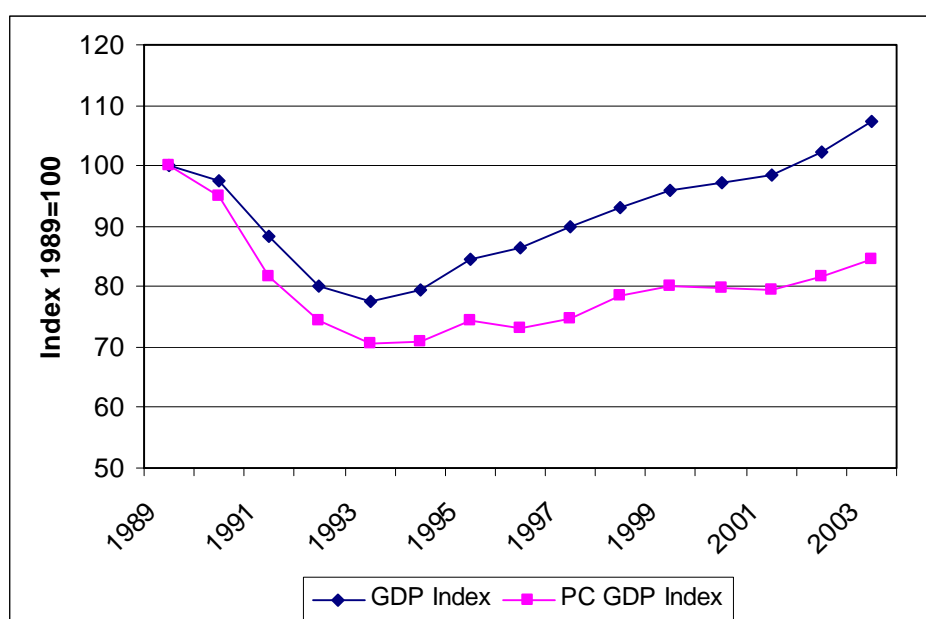
30. The fallout of the transition policy stance is reviewed below under three headings; first economic performance, second the consequences for poverty and inequality, and third, the wider social impacts, including health and education outcomes and personal responses to change.

Economic Performance⁶

Data and Trends

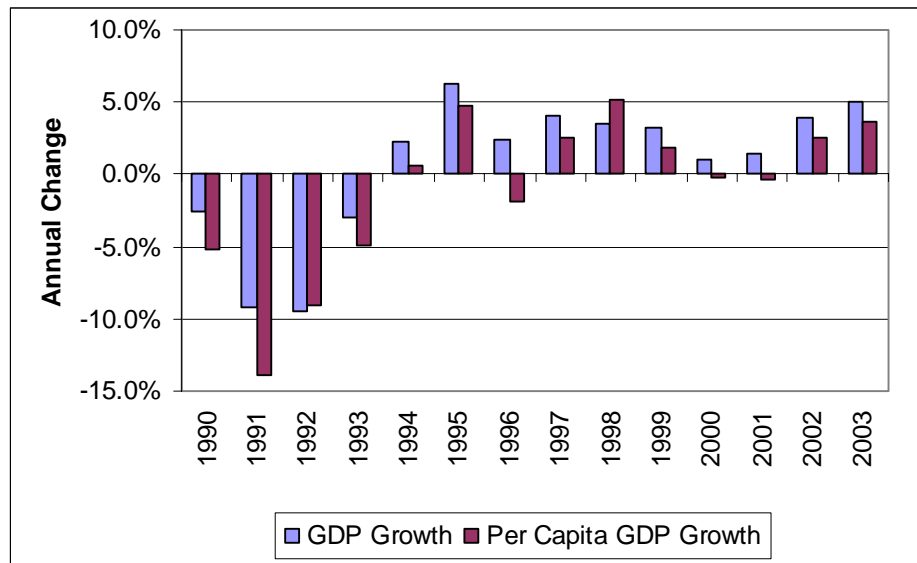
31. The initial transition is followed almost immediately by a sizeable fall in output in 1991 and this accelerates in 1992 and 1993. This is reflected in the real economy by growing unemployment and the bankruptcy of the major SOEs. Growth returns strongly in 1994 and the overall GDP compression is of the order of 22%. GDP surpasses its 1989 value some twelve years later in 2002
32. Yet the prognosis of per capita GDP is significantly worse, with a total reduction of 30% on the 1989 value in the 'trough' of the recession, and there is still no immediate prospect of it returning to its pre-transition level. Underpinning this is of course, Mongolia's positive population growth rate, which currently averages 1.4% per annum. The overall trends are depicted in Figure 2, and the difference between overall and per capita GDP growth rates are drawn out in Figure 3 below.

Figure 2: GDP and GDP per Capita 1989 to 2003



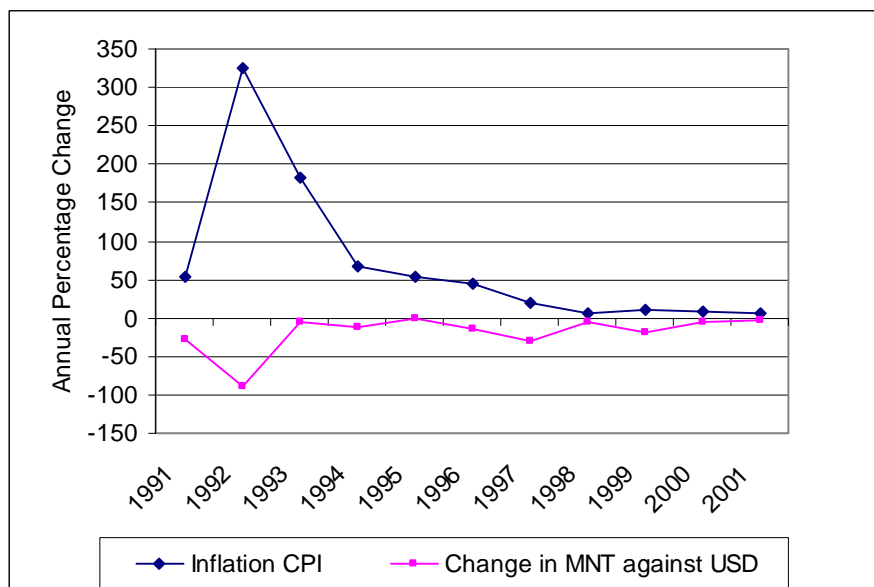
⁶ To assist with this section a summary of the key data sets for the full transition is given at Appendix B.

Figure 3: GDP and Per Capita GDP Annual Rates of Change



33. This pattern of initial crisis and recovery is familiar to economies pursuing rapid transition policies, as is the emergence of hyper-inflation as prices are liberalised. Mongolia experiences similar price instability in 1991 and 1992 and its progressive containment through harsh stabilisation policy. Concurrent to inflation has been the progressive and still ongoing depreciation of the Togrog against the US dollar as is illustrated in Figure 4 below.

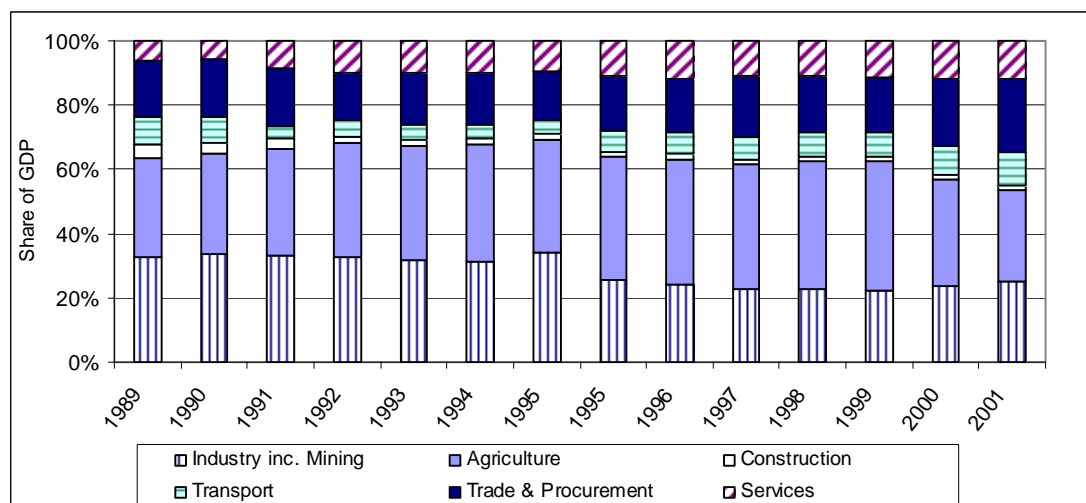
Figure 4: Annualised Inflation Rate & Depreciation of the Togrog against the US Dollar 1991 to 2001



34. The transition has also resulted in a radical re-orientation of the real economy, with the contraction of the former industrial base, a rise initially in the share occupied by agriculture and its output (though not its productivity), the emergence of a vibrant service sector, and latterly, the rejuvenation of the crucial mineral extraction industries. This is illustrated in Figure 5 below, but

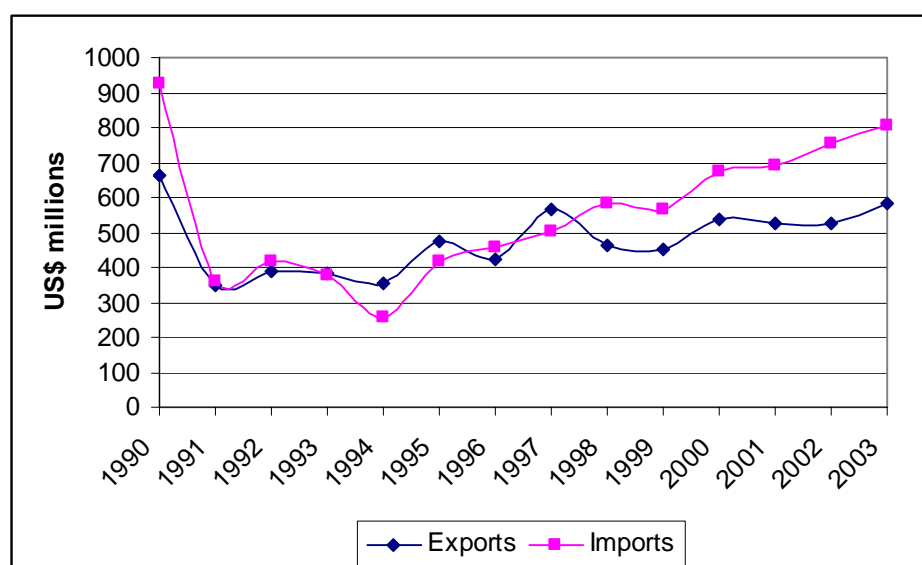
rather imperfectly as Mongolian statistics did not in the early transition distinguish between mining and the wider industrial sector, and the picture is further clouded by fluctuations in the world price of copper concentrate throughout the period.

Figure 5: Approximate GDP Shares 1989 to 2001



35. Changes the pattern of employment reflect these trends. In the initial transition unemployment rises dramatically, labour is then absorbed by herding, and subsequently by the informal sector. But in spite of declining official unemployment rates there remains a considerable level of under-employment. At the same time, there is a fairly rapid, though somewhat stepped, increase in the share of GDP occupied by the private sector. By 1995, the figure was above 50% and in recent years, has accounted for around 75% of output (NSO, 2003 and Mongolian Donors Consultative Group, 2003)
36. Mongolia's balance of payments position undergoes still more radical change, with an initial balance of payments crisis being replaced by current account surpluses as the recession deepens and domestic absorption is reduced sharply. This is followed in time by the emergence of a chronic trading deficit. A time series for imports and exports is provided in Figure 6 below.
37. The current deficit has increasingly been financed by aid flows which by the late 1990s were approaching the GDP share once occupied by the former Soviet transfers. This has somewhat abated in time, but recent estimates still show Mongolia to be highly reliant on aid. Overseas Development Assistance (ODA) currently represents around 20% of GDP ranking Mongolia in 2002 as the eleventh most aid dependant country in the World⁷.

Figure 6: Mongolian Imports and Exports 1990 to 2003



38. The pattern of trade has also changed very substantially, with China and Asia, and less so the United States and Western Europe, emerging as major export markets. Underlying this is the collapse of the former Soviet-led trading regime, the Council for Mutual Economic Assistance (CMEA) and the liberal trade policies were adopted.

39. The Government's fiscal position showed a familiar pattern of deterioration during the transition, but deficits are now contained. Furthermore, the recent agreement of the Russian Federation to accept cancellation of what effectively amounts to 97% of the so-called 'convertible rouble' debt incurred during the pre-transition period, previously claimed to amount to US\$ 10 billion, will mean the outstanding debt position will also be settled⁸. It is worth noting though, that the accumulation of concessional finance in recent years (mainly from multilateral donors) will present problems if growth is not forthcoming. A major challenge therefore, is channelling these resources to productive activities. Figures presented to the Donors Consultative Group Meeting held in Tokyo in 2003, show debt (excluding the rescheduled rouble debt) represented approximately 85% of GDP.

Evaluation of Outcomes

40. The literature on Mongolia's post transition economic performance is far from vast, yet even within the small number of authoritative studies that have been undertaken, a lively debate has emerged between two distinct and somewhat ideologically-coloured schools of thought.

⁷ Based on data for 2001 given in the Global Human Development Report for 2003

⁸ Sourced from The Russia Journal, January 13, 2004, www.russijournal.com

41. The positive view of the impact of the policy stance is advanced by neoclassical contributors and this includes work undertaken by the International Monetary Fund (IMF). For authors like Pomfret (1999), the transition recession was short lived compared to those visited on other comparable ex-Soviet nations in Central Asia. Cheng (IMF/ Cheng, 2003) goes some way further by describing the Mongolian transition experience as experience as 'smooth' and its output performance 'strong'⁹. He does this on the basis of a comparison over time against the performance of other CIS and Eastern European nations on a number of dimensions ranging from the size of the GDP compression, to the time between the implementation of reforms and the emergence of positive growth.
42. Cheng explains Mongolia's 'good' performance in terms of; the lack of structural distortions at the beginning of the transition, such as the lower level of over-industrialisation; and the early application of reforms which have resulted in strong efficiency gains. Using econometric techniques he shows that most of the recovery has resulted from improvements in total factor productivity and not capital accumulation (Ibid).
43. Yet in essence, these positions only posit Mongolia's transition as a success, in terms of the relative performance of other ex-Soviet and Eastern European nations and typically those pursuing the same sorts of transition policies. No attempt is made to compare outcomes against those achieved by the gradualists of South and East Asia. Moreover, evidence from the more successful, and generally 'better phased' (if not strictly gradualist), reformers of Europe is also down played.
44. It is very clear these accounts focus very directly on aggregate GDP change and the narrow success of stabilisation policies. Little or no attention is given to the per capita level of GDP which has still not recovered to pre-transition levels or the wider socio-economic and poverty fallouts. This second point is taken up by the critics, and one which we return to in some detail in the next section. Yet the voices critical of the Mongolian transition also directly challenge the economic adequacy of the strategy.
45. Nixon and Walters (2000) offer two very significant criticisms. First, they question the adequacy of measuring the demand-shock of the initial retrenchment via the use of GDP aggregates alone, and argue that the economic crisis which gripped the country in 1992 and 1993 was far more severe for the real economy. They assert that the reduction in domestic absorption was as high as 60%, and underpinning this was the poor coordination of liberalisation policies and the near-overnight withdrawal of the consumption subsidises from former Soviet Union during 1991.

⁹ See Cheng page 15 (IMF 2003)

46. Second, they put a persuasive case that although the inflationary episode of the early 1990s is a phenomenon common to transition economies, its cause in the Mongolian case, is far from common. Instead of being the result of a profligate government borrowing excessively from the banking system, they cite the poor phasing of price liberalisation with the decontrol of imports, a weak domestic supply response and an unregulated banking sector as the crucial factors. They go on to argue that the subsequent and long lasting monetary squeeze, seals the fate of what few competitive value-adding industries remain. Other commentators have since argued that the severity of the monetary policy response begins a process of effective de-industrialisation.
47. Griffin in a major study prepared for UNDP in 2000 on economic policy making and poverty reduction re-iterates this line, but expands the critique asserting that that shock-therapy and adherence to laissez faire economics generally, have served to 'lock' Mongolia in a position of capacity under-utilisation and mass poverty. Specifically, he argues that ongoing punitively high interest rates, the erosion of domestic savings and the running down of industrial capacity, have caused chronic under-employment and fundamentally constrained Mongolia's medium-term growth potential. Griffin's study which provoked controversy when published, also highlights the strategy's failure to promote new value-added and employment generating activities, and prevent the rise of insecurity and income inequality.
48. Moreover, both Griffin and Nixson and Walters are critical of the level of aid dependency. The former arguing this will ultimately result in a debt crisis and the latter, that aid flows distort the capital account and artificially raise the value of the Togrog. This in turn fundamentally compromises competitiveness and distorts the balance of payments. Data from the central bank is supportive of a strengthening in the Togrog against its main trading partners, if not the US dollar, during the later part of the transition¹⁰.

National Views

49. The majority of government officials interviewed for this paper generally hold to a middle or 'mildly positive' position, acknowledging the early weaknesses, but stressing a dramatic improvement in policy and outcomes during the mid and latter years of the 1990s. Others have expressed doubts over whether Mongolia had any other option other than to adopt rapid reforms, citing both fiscal and political pressures as being overwhelming.
50. National authors, for example Altantsetseg (2002), highlight the difficulties imposed by exogenous shocks on economic performance. These have included the loss of the Soviet transfers in 1991, the

¹⁰ Data provided by the Mongol Bank show the real value of the Togrog has appreciated by some 31% since 1995.

East Asian Financial crisis of 1997 and the Dzungar of 1999. In a paper prepared for the Japanese Development Agency (JICA), she uses econometrics to show that growth during the latter transition period would have been in the region of 6% had these shocks not compromised the economy.

Poverty and the Transition

51. The impact of the transition on poverty levels is a facet of Mongolia's transition which is majored on by critical voices and one that tends to be overlooked by those with more positive perspectives. This is unsurprising, since by any evaluation, poverty has worsened considerably in the last thirteen years. Yet here again we face some problems in ascribing the causes of poverty directly to transition policy choices.
52. Prior to the transition there was little incidence of absolute income poverty in Mongolia, the welfare system of the state ensured the equalisation of incomes and entitlements at well above basic subsistence levels (Griffin et al, 2001). Inequality under such a system was also unheard of, yet by the time the first Living Standards Measurement Survey (LSMS) had been conducted in 1995, approximately 36% of the population were judged as being below the poverty line. A second survey in 1998, showed no significant change in the poverty headcount measure (P0). In addition a sizeable worsening in the depth and severity measures (P1 and P2) was apparent, demonstrating a worsening in the degree of immiseration and the distribution of consumption amongst the poor. Figures pertaining to these surveys are presented in Table 1 below (NSO/ World Bank 1996, NSO/ UNDP 1998).

Table 1: LSMS Results 1995 and 1998

| Poverty Measure | LSMS 1995 | LSMS 1998 | Change (%) +ve implies a worsening of the index |
|-----------------|-----------|-----------|--|
| Headcount (P0) | 36.3 | 35.6 | - 1.9% |
| Depth (P1) | 10.9 | 11.7 | + 7.3% |
| Severity (P2) | 4.8 | 5.6 | + 16.7 |

53. In addition, estimates for income inequality as given by the Gini coefficient also showed deterioration between these two years with the coefficient rising some 13% between 1995 and 1998; the respective values being 0.31 and 0.35 (UNDP, 2004). Unofficial estimates for 2002 show a further deterioration¹¹.

54. The Participatory Living Standards Assessment, carried out in 2000, which sought to provide a wider and more subjectively defined poverty assessment also showed significantly worsening levels of poverty in terms of perceptions, evidenced growing social exclusion and a widening gap between rich and poor (NSO/ World Bank, 2001).
55. Troublingly, as Bremmer a contributor to Griffin et al (2001), makes clear the LSMS estimates for both 1995 and 1998 potentially understate the degree of poverty present in Mongolian society. He argues that the methodology used to establish the poverty line in both studies makes two significant departures from standard statistical practice. Furthermore, that the distribution of income within Mongolia is such that the poverty levels are extremely responsive to changes in the line. After re-estimation, Bremmer suggests that a staggering 51.6% in 1995 and 51.7% in 1998 would be judged poor if standard analytical approaches had been adopted (UNDP/ Griffin et al, 2001).
56. The LSMS data set also reveals some interesting facts about the nature of poverty in Mongolia and the demographic composition of the poor. Most clear is the preponderance of poverty in urban areas outside the capital city, relative to the rural hinterlands. But it is also worth noting that the classification of rural and urban areas has become something of a debate between commentators, with the 2003 National Human Development Report re-describing all areas outside the central 'aimags' (provinces), dominated by the cities of Ulaanbaatar, Erdnet and Darkhan as rural¹².
57. The other key demographic markers of poverty given by the LSMS results less surprising; the poor are more likely to be unemployed, and more likely to be less well educated. A further feature is a strong differential in incidence and depth of poverty between male and female headed households, and by implication between single and two parent families¹³. Interestingly, critical commentators link this directly to the privatisation methods adopted, and particularly those deployed in rural areas for the division of herds, which systematically favoured male heads of household (UNDP/ Nixon and Walters 2004).

The Policy Debate

58. Unsurprisingly the debate around poverty is less polarised, with virtually all contributors recognising its severity and its reduction as a policy priority. Though this has only in recent years been acted on by Government; first through the National Poverty Alleviation Programme (NPAP) and more latterly by policies articulated in the national PRSP.

¹¹ Initial estimates provided to UNDP suggested a very sizeable increase in the Gini to 0.44, this was later revised by NSO to 0.37; thus far no official figure has been published (UNDP, 2004).

¹² See UNDP (2003), the methods adopted re-classify urban and rural areas using a Core-Periphery Model.

59. There is however, little consensus on what the actions the Government could have taken to address this problem in earlier years, and even less so in terms of whether the selected transition reform policies might have exacerbated poverty. Again the lines in this debate are drawn along familiar points of disagreement; with the Bretton Woods institutions and the Government holding to the efficacy of orthodox economic policies to support growth, alongside the sectoral re-allocation of the budget; versus critical voices who directly cite the transition strategy as being a cause of the level of poverty now experienced, and arguing for a substantial reshaping of the policy stance.
60. This agenda is perhaps best articulated by Griffin (UNDP/ Griffin et al 2001), in which he and other contributors argue for a pro-poor growth strategy based on employment generating activities, an activist industrial strategy and other interventions by the State. The specific actions identified by Griffin are the creation of a more favourable trading environment through tariff and export promotion policies (within WTO rules), a reduction in interest rates offered by the commercial banking sector to businesses, tackling the backwardness of Mongolia's infrastructure and improvements in family and personal economic security via a basic welfare system. In essence Griffin's case is that the laissez-faire transition needs to be slowed and reformulated, to something akin to the Chinese and Vietnamese models.
61. Although the Griffin report remains controversial, and his recommendations have for the most part been ignored by government, there are signs of official recognition of some of the proposals made. These include a stronger commitment to the poor, the mainstreaming of poverty reduction and an acceptance that ad hoc alleviation measures, such as those pursued under the NPAP are not a lasting solution to the problem. Additionally the Government has also signalled its intention to pursue more distinctly pro-poor policies, including the re-prioritisation of the budget, boosting investment in infrastructure, and the managed devaluation of the Togrog¹⁴.
62. Before moving on, it is useful to quickly touch on the issue of income inequality, as this clearly conditions the extent to which mainstream growth will be poverty reducing. And although low by international standards, Mongolia's Gini's coefficient deteriorated quite substantially between 1995 and 1998, suggesting that the transition was continuing to promote higher levels of inequality even as average incomes had begun to rise.
63. Not only does this augur badly for the prospects of the current levels of growth making any headway in reducing poverty, but also suggests that policy making has done little to address the fundamental problem. A separate study for UNDP on the relationship between privatisation policies,

¹³ Social convention in Mongolia dictates that single headed households are almost exclusively female-headed.

and poverty and inequality (UNDP/ Nixon and Walters 2004), concludes that the allocation methods used in respect of residential apartments and herds, has been a major underlying cause of rising inequality.

Social Consequences and Personal Survival Strategies

64. In addition to the severe economic retrenchment and the emergence of poverty, the transition period was witness to considerable social dislocations. These phenomena can be viewed at two different levels; firstly, in terms of outcomes in the health and education sectors, and second in terms of the coping and survival strategies adopted by ordinary Mongolians, which have given rise to some substantial demographic movements.
65. At the aggregate level, the dislocation was most severe in the health sector. As the population suffered the impoverishment of the early transition and the State struggled to meet its commitments, health indicators suffered greatly. Of particular significance was a striking increase in the levels of maternal mortality which doubled from an incidence of 1.2 to 2.4 deaths per 1,000 live births between 1990, and the depth of the economic crisis in 1993. Some deterioration in infant mortality and life expectancy was also observed, and it is disquieting that life expectancy in 2001 was little different from that recorded for 1990 (UNDP, 2004).
66. The impact in the education sphere at the national level of extraction is less striking with adult literacy standing up well. However, there was some reduction in overall enrolment rates during the early and middle years of the 1990s and a distinct gender imbalance emerging that has become very pronounced at the upper levels.
67. This imbalance is atypical in that it affects men, who are increasingly under-represented in tertiary and higher education. Paralleling this is a less pronounced reduction in boys' primary school enrolment rates. A number of factors underpin these trends, but the most significant are pressures on rural families, who in the light of harsh economic conditions tasked boys with assisting with the herding of animals, and the collapse of the vocational education system which was previously male dominated. This latter impact also has a transition dimension, as both budget pressures and bankruptcies of SOEs, contributed to the closure of vocational training institutions (UNDP, 2004).
68. The decline in social outcomes is best analytically illustrated by changes in the Human Development Index (HDI) and its sub-indices in the period since 1990. The HDI calculation is

¹⁴ See relevant sections in the F-PRSP (Government of Mongolia, 2003)

decomposed in Table 2 below for six sample years between 1990 and 2003. It is very clearly evident that the most significant factor in the HDI's decline is the fall off in the health indicator, the Life Expectancy Index. This is compounded by falls in GDP per capita and falling educational enrolment in the early transition, and offset by the improvement of these indicators in later years.

Table 2: HDI for Mongolia 190 to 2001¹⁵

| Year | Life Expectancy Index | Education Index | GDP Index | HDI |
|------|-----------------------|-----------------|-----------|-------|
| 1990 | 0.645 | 0.845 | 0.467 | 0.652 |
| 1992 | 0.638 | 0.824 | 0.424 | 0.626 |
| 1995 | 0.647 | 0.849 | 0.424 | 0.635 |
| 1998 | 0.669 | 0.850 | 0.435 | 0.651 |
| 2001 | 0.639 | 0.884 | 0.497 | 0.674 |
| 2003 | 0.640 | 0.870 | 0.480 | 0.661 |

69. Many of these trends and outcomes are connected with the coping strategies adopted by ordinary families during the transition. These responses have been reflected in substantial demographic movements over the period, and three of the most significant are listed below:

- **Declining Fertility:** A substantial decline in the birth rate has been observed across all regions, but particularly in the capital city and urban centres. On average the crude birth rate fell by 52% during the 1990s compared to previous decade. This was a rational response on the part of women and families to rising levels of vulnerability, and had this not taken place, it is likely per capita GDP levels would have been even worse.
- **Changing Patterns of Migration:** Large population migrations emerged as early as 1992 with strong urban to rural flows, the turning point came in 1999, when flows reversed and large movements took place to the central cities. Initially, workers displaced by the collapse of industry migrated to rural areas to seek out opportunities in the newly liberalised pastoral sector. Yet this de-urbanisation or 'return to herding', essentially amounted to a subsistence strategy to escape the poverty developing in urban centres, rather than a re-balancing of incentives between agriculture and industry. Indeed, over the full transition period agricultural productivity has declined. A contributory factor to this has been the collapse of collective services previously provided by the collectivised farms the *Negdels* and the degeneration of agricultural capital and infrastructure, such as the common wells and

¹⁵ Source: UNDP National Human Development Report 2003, final year (2003) has not yet been cited in the Global HDR and has not yet been validated therefore.

storage facilities they once managed. Lurking at the heart of this, as many commentators and to some extent government sources acknowledge, is the rushed and poorly thought-out privatisation of the agricultural sector in the early 1990s.

The Dzud in 1999 provides the impetus for the reversal of flows to the central *aimags* containing Mongolia's principal cities. These flows are complemented by the pull of the emergent informal sector and the prospect of better educational, cultural and health facilities. The reality in some urban centres, particularly the capital, is somewhat different, and Mongolia is beginning to develop a serious urban poverty problem.

- The Growth of the Informal Sector: Unlike the other coping strategies listed above, entering the informal sector an employee, or more typically as an entrepreneur, has proved more than a temporary refuge for those disadvantaged by the transition. The sector is remarkably diverse, ranging from basic subsistence activities to new manufacturing concerns and numerous trading outlets. Government transitional policy on matters such as taxation and regulation, has proved remarkably hospitable to informal sector growth, making efforts not to stifle activity, and it has offered an inexpensive and basic means of securing official registration. Questions remain however, as to how existing policies can promote the expansion of this dynamism into the mainstream economy.

Part IV: Conclusions and Overall Appraisal of the Transition Strategy

70. It is useful to again preface the following conclusions with a caveat noting the inherent difficulties of making objective judgments on the success of specific policy instruments and the precise phasing of reforms since there is no cast iron counterfactual with which outcomes can be compared. However, it is possible to make observations about the overall conduct of the strategy and there is also sufficient evidence with which to judge the major policy instruments.
71. Mongolia is rightly described as pursuing a rapid, 'shock-therapy' or 'big-bang' approach to reform. This included within the space of three years from the initial transition, the near complete decontrol of consumer prices, capital and current account convertibility, significant trade liberalisation and privatisation of virtually all small and medium sized enterprises.
72. In the years following the adoption of such policies, Mongolia suffered a deep recession, hyperinflation, bankruptcies, industrial collapse, and most troublingly, the emergence of mass poverty and severe social dislocation. Yet the period of absolute retrenchment was contained and

the main economic aggregates have since recovered. It must also be noted that during the period, the economy suffered some very severe external shocks.

73. In terms of a narrow macroeconomic calculus is it apparent that Mongolia performed above average within the group of East European and CIS Nations, who also pursued rapid transition policies. This is in terms of both the impact of the transition strategy on aggregate output and the speed at which stabilisation policies produce their desired outputs.
74. Yet deeper level analysis casts doubt on the effectiveness of these policies in securing higher per capita incomes and in fostering new value-added activities. Moreover, there is prima facie evidence that the initial dash for change at the beginning of the process fostered administrative and governance failures which led to weak policy making. Several reforms were poorly sequenced and poorly executed, and this is likely to have exacerbated the economic crisis and led to the wholesale destruction of the former industrial base, making its adaptation impossible.
75. More damning evidence is provided by the very clearly better macroeconomic performance of those nations which selected gradualist transition strategies, who have enjoyed higher levels of growth and no serious economic retrenchment. But it is also not clear whether this option genuinely existed to Mongolia, which found itself rapidly engulfed by the collapse of the former Soviet Union, the withdrawal of substantial transfers and the disappearance of its previously guaranteed markets. And clearly, the near overnight loss of purchasing power equivalent to 30% of GDP, implied by the withdrawal of what are effectively consumption subsidies, had a very sizeable recessionary effect. It is also unlikely that the necessary political consensus required to support such a course of action could have been assembled at the close of the 1990s.
76. It is apparent that policy formulation was hampered by the strength of the reaction against any form of state planning apparatus. Effective coordination and national development planning processes are still being established, and this has been supported by the preparation of the EGSPRS (Mongolia's PRSP). The Government has also made efforts to synchronise achievement of the MDGs with PRSP implementation, with common indicators being used within the monitoring and evaluation frameworks¹⁶.
77. The conclusion above is also pertinent to institutional reform which was often sporadic in nature and conducted in response to particular crisis events. The recognition that effective market

¹⁶ In spite of this coordination between MDGs and the PRSP, initial reports suggest that without a sizeable shift in trends, the poverty reduction targets will not be met. Education and Health indicators are however estimated to be on track.

economies require good institutions and the capacity to develop them is something which has emerged as time has progressed. The more effective institutional reforms have included the recapitalisation and re-regulation of the banks in the mid 1990s and more recent efforts at public service management improvement.

78. In relation to poverty and poverty reduction, it is clear that the transition period has seen a very substantial increase in the level of poverty. Though the incidence of poverty appears to have stabilised from the middle part of the decade, it is disturbing to note that more considered poverty alleviation interventions and positive economic growth have failed to make any serious inroads into the problem. Additionally, the depth and severity of poverty appears still to be worsening. It is to be hoped that the renewed attention given to these challenges within the EGSPRS will be more successful.
79. Further to this, there is evidence to suggest that privatisation methods, notably the allocation of residential property without charge on an unequal basis and the discretionary local allocation of pastoral animals may have disproportionately contributed to the growth in inequality. Inevitably, this will blunt the poverty-reducing potential of economic growth. It is likely that more equitable means of asset distribution could have been found, including where appropriate, some form recompense on the basis of mortgage finance or deferred payment. Even were this not possible, a sound capital gains tax regime, would at least serve to limit any windfall surpluses accumulated.
80. In closing, two important points need also to be made. First, in spite of the ongoing weaknesses and failures, there is considerable evidence of policy learning and adaptation within official circles. It is vital that certain successes are not neglected and these include banking reform and the development of a stable macro-economic environment.
81. Second, it must be re-iterated that in the political sphere, Mongolia has outperformed, most of those transition nations that have embraced democracy, and this change was secured without the 'stain' of political violence. As a result it cannot be argued that the Mongolian people have not sanctioned the economic and social policy choices made.

Part V: Key Challenges for the Future

82. The following provides a very brief synopsis of five key policy challenges faced by the Mongolian people in the coming years. At the outset, it is worth recognising that many of the issues discussed

are not contingent on the conduct of transition policies, and indeed, after thirteen years of structural reforms, there is a need to move rapidly to address a wider developmental agenda.

Poverty and Pro-Poor Growth

83. The highest priority facing Mongolia is the scourge of poverty, and its attendant social agenda. This includes health and educational under performance, rising crime and personal safety. The only long term and sustainable solution to these problems is the emergence of pro-poor economic growth.
84. In order for growth to be pro-poor active steps must also be taken to halt the worsening level of income inequality. This requires a raft of measures, some of them targeted directly at the poor and others on activities which would benefit the poor. These include; improving the supply of (micro) credit to small businesses, facilitating employment generating activities through selective tax and trade measures, and securing improvements in overall competitiveness.
85. Poverty is also likely to assume a new character in the coming years to one which is given by more severe and more localised problems, and government policy needs to consider budgetary measures to support basic living standards, through the provision of basic welfare. The use of comprehensive safety-nets, will also contribute to an overall reduction in risk aversion complementing entrepreneurship and the general level of economic activity.

Establishment of Value Added Activities

86. Central to securing economic growth is the need for the structural adjustment of the economy to more productive activities which generate higher value added. A number of structural features including weak infrastructure, poor financial intermediation and aid dependency distort incentives to entrepreneurs forcing investment into the non tradable-sector.
87. This requires the reorientation of policy on a number of fronts, ranging from improving the banking sector to incorporating the informal sector within the mainstream economy, to realigning national and local budgets to human development priorities and to reviewing trade policy to ensure the national currency is correctly valued.

Investment, Domestic Resources and Aid Dependency

88. In order for value added activities to emerge and for Mongolia to grow, more investment is needed, and in order for this to be sustainable, this needs to be met where possible by domestic resources.

Measures need to be taken to boost savings, and the demand for savings. This means providing incentives for savers and encouraging entrepreneurship.

89. In spite of several positive reforms the banking sector is still not effective or competitive. Interest rates are too high, credit lines are not of sufficient duration and spreads between deposit and lending rates are large. Banking practices need improvement, and the sector would also benefit from consolidation. Property rights and contracts also require better enforcement in order to reduce the risk aversion of banks.

Budget Priorities; Human Capital and Infrastructure

90. Public provisioning provides an essential tool with which to influence the pattern of production within the economy to signal the intentions of the government, yet realignment of the budget around priority areas has proved sluggish. This does not necessarily imply an increase in expenditure, but rather a realignment of priorities. The shares of the budget devoted to education and health, key areas for sustaining Mongolia's human capital, are too low.
91. Equally too little is devoted to investing in capital schemes that would boost Mongolia's growth potential. The Millennium Road project which is to run between the far east and west is an excellent start, yet better links need to be built to the market place and especially Mongolia's major trading partner, China. Again affording an expansion in this sector need not mean raising the overall budget, but re-allocation, more effective use of concessional finance and public service reform.

Institutional Development and Good Governance

92. Too often the transition strategy neglected the need for sound market supporting institutions and the development of an environment conducive to business. Institutional development encompasses the physical agencies, the formal laws and regulations and most importantly the informal conventions of society. Each needs attention and particularly the latter, since without cooperative behaviours, markets function poorly.
93. Good governance lies at the heart of this, and Mongolia must be commended for its sound and increasingly vigorous democracy. This needs to be built on and expanded into the sphere of economic governance. This applies both at the strategic level where the processes which successfully completed the PRSP need consolidating, and at the operational level, where public service management and the conduct of public servants, including anti-corruption measures, need to be strengthened.

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Appendix A: Government Officials and Commentators Interviewed

| | | |
|--|--------------------|--|
| 1. Ministry of Finance and Economy | Mr Jargalsaikhan | Director, Dept of Economic Policy and Planning |
| 2. State Property Committee | Mr Balikhuu | Advisor |
| 3. Ministry of Industry and Trade | Mr D. Badarch | Director, Policy Department |
| 4. Mongolbank (Central Bank) | Mr Boldbaatar | Director, Monetary Policy Division |
| 5. World Bank | Mr Saha Meyanathan | Resident Representative |
| 6. Asian Development Bank | Mr Darius Teter | Deputy Resident Representative |
| 7. Centre for Social Development (NGO) | Mr Gantumur | Chief Executive |
| 8. Prime Minister's Office | Mr Gerelt-Od | Economic Policy Advisor |
| 9. Science Academy | Ms Enkhtuvshin | Professor |
| 10. MNU, School of Economic Studies | Mrs B.Suvd | Director |

Appendix B: Key Data Trends 1990 to 2002 (2-3 year intervals)

| <u>Year / Indicator</u> | <u>1990</u> | <u>1992</u> | <u>1995</u> | <u>1998</u> | <u>2000</u> | <u>2002</u> |
|--|-------------|-------------|-------------|-------------|-------------|-------------|
| <u>Economic Performance</u> | | | | | | |
| GDP Growth (%) | -2.5% | -9.5% | 6.3% | 3.5% | 1.1% | 3.9% |
| Per Capita GDP Growth (%) | -5.2% | -9.1% | 4.7% | 5.1% | -0.3% | 2.5% |
| Consumer Price Index (%) | 0.0% | 325.5% | 53.1% | 6.0% | 8.1% | 1.6% |
| Exports (currently US\$ m) | 660.7 | 388.5 | 473.3 | 462.3 | 535.8 | 524.0 |
| Imports (current US\$ m) | 924.0 | 418.3 | 415.3 | 582.4 | 675.9 | 752.8 |
| <u>Industrial Structure</u> | | | | | | |
| Private Sector % of GDP | 0% | - | 51.3% | 68.8% | 72.2% | 75.0% |
| Sector Shares: | | | | | | |
| - Industry inc. Mining | 33.2% | 32.0% | 33.1% | 22.7% | 23.7% | 18.1% |
| - Agriculture | 30.7% | 35.0% | 34.5% | 39.9% | 33.2% | 20.7% |
| - Construction | 3.4% | 1.9% | 1.8% | 1.5% | 1.5% | 2.1% |
| - Transport | 7.7% | 4.7% | 4.1% | 7.3% | 8.7% | 14.0% |
| - Trade & Procurement | 17.8% | 14.7% | 14.7% | 17.6% | 21.1% | 27.6% |
| - Services | 5.8% | 9.6% | 9.2% | 10.9% | 11.8% | 14.2% |
| - Other | 1.3% | 2.1% | 2.5% | - | - | - |
| <u>Human Development</u> | | | | | | |
| HDI (1=maximum) | 0.652 | 0.626 | 0.635 | 0.651 | 0.669 | 0.679 |
| Life Expectancy (years) | 63.7 | 62.8 | 63.8 | 65.1 | 63.2 | 63.5 |
| Adult Literacy Rate (%) | 96.5% | 97.7% | 98.9% | 96.5% | 97.8% | 97.8% |
| Combined Enrolment Rate (%) | 60.4% | 54.3% | 57.0% | 62.0% | 69.6% | 69.7% |
| <u>Poverty & Inequality</u> | | | | | | |
| Headcount (%) | - | - | 36.3% | 35.6% | - | - |
| Gini Coefficient (1= maximum inequality) | - | - | 0.31 | 0.35 | - | 0.44 |

Notes:

Data in italics indicates estimated figures, or where a dispute, or contradiction exists between sources

A dash (-) is given where no reliable estimate could be derived.

Sources:

National Statistical Office of Mongolia – see NSO (2003)

Economic Policy Support Project Bulletins, published quarterly to 2003, USAID, Ulaanbataar (2003)

National Human Development Report – see UNDP (2004)