Proceedings and Outcomes of the Neo-liberal Policy During the Mongolian Economic Transition

Enkhbayar Shagdar
Visiting Researcher, Research Division, ERINA

1. Introduction

After 70 years of power being concentrated in the hands of one political party, Mongolia held its first free election in 1990 and the first democratic constitution was approved in 1992. The Constitution declared the people's ultimate goal to be the building of civil democratic society in the country. These democratic changes in the political environment were crucial turning points in Mongolia's recent history. The country embarked upon an irreversible path towards a market economy in 1990 and today continues to implement political and economic reforms recommended by multilateral development banks and international financial institutions such as the International Monetary Fund (IMF), the World Bank[1] and the Asian Development Bank (ADB), with the aim of becoming a democratic society with a free market economy. Mongolia became a member of the IMF, World Bank and the ADB in 1991 and joined the WTO in 1997. The economic policy undertaken in Mongolia during this transformation can be described as a classic example of the 'neo-liberal' policy package, which is characterized by price and trade liberalization, financial liberalization, privatization, deregulation and small government.

At the beginning of the economic reforms, the country's immediate priority was to establish the basis of a market economy and the government adopted a policy of 'shock therapy' that quickly removed many regulations and controls while trying to hand as many activities over to the private sector as possible. The initial transformation included two sets of policies to be implemented simultaneously. The first set included measures for achieving a macroeconomic balance and the *liberalization of prices and trade*, introducing a unified *floating exchange rate*, strict wage and credit controls and the *abolition of subsidies*, and developing a social safety net. The second set of policies was oriented towards structural changes, including the *privatization of state sector assets*, a guarantee of property rights, *enterprise restructuring*, the *reform of fiscal and financial systems*, introducing a legal framework for reform, control over monopolies, encouraging foreign investment, and the reform of the education and healthcare sectors. Securing macroeconomic stabilization, increasing investment and savings, developing economic and social infrastructure, export promotion, boosting the competitiveness of Mongolia and ensuring economic growth have been defined as priority objectives of the transition phase. The main outcome to have emerged so far from the period of transition to the new social system is intensive political and economic reform within a short period of time, as well as Mongolia's opening up to the world, the liberalization of the economy and its irrevocable metamorphosis into a market economy, and its transformation into a democratic country respecting multiple opinions. However, the implementation of policy has often resulted in undesirable outcomes, with Mongolia experiencing economic contraction, slow growth, unemployment, poverty and inequality as a result. The country is still struggling to bring the majority of its citizens out of poverty and put the economy on a sustainable growth path. In describing the post-1990s economy of Mongolia, Dr. Namjim states that, although rapid social and economic changes occurred during transition, an efficient market economic mechanism has not been formed yet and the economy is in crisis. There are many troubling social problems and the majority of the population is trapped in poverty (Namjim, 2000). This paper investigates some features of this neo-liberal policy and its outcomes in Mongolia in the course of its transition towards a free-market economy.

2. Neo-liberalism in the Economic Policy

2.1. Price Liberalization and Inflation

The reform programs launched by the first democratic government in 1990-1992, including price and trade liberalization, the establishment of new banking and financial systems, and privatization, laid the foundation for the development of a private sector-based, market-oriented economy in Mongolia.

Prior to 1991, the prices of all products were set directly by the government through the decrees of the State Committee for Price and Standardization, with the difference between world prices and domestic production costs being subsidized from the state budget. Government Resolution No. 20 on January 15, 1991, concerning measures relating to the transition to a market economy, was the first, radical step in the price liberalization process in Mongolia, as a result of which the prices of 60% of all products were liberalized, with the prices of the remainder being doubled. The number of directly controlled retail prices was reduced from 220 categories to 35, along with 10 categories of imported goods. At the same time, pensions, scholarships and the wages and salaries of workers and employees of governmental organizations and

[1] E.g., policies prescribed by the World Bank's 'Stand-by', ESAF (Enhanced Structural Adjustment Facility), PRGF (Poverty Reduction and Growth Facility) and PRSP (Poverty Reduction Strategy Paper) programs.

state-owned enterprises increased twofold, along with twofold increases in taxes and tariffs. The authorities called these measures a change in the money scale, although in fact it was a twofold devaluation of the Mongolian national currency: the Mongolian Togrog (MNT). As a consequence of this resolution, the purchasing power of all cash deposits at banks and cash money held in private hands decreased twofold, except private savings deposited at banks. In order to protect private savings, the amount of private savings deposits in banks were doubled. Although the public were somewhat prepared for the reforms and a new economic system, such a sudden change without prior explanation was a 'shock' for most citizens.

Furthermore, the prices of petroleum products were raised fourfold in June 1991, and the list of controlled retail prices was cut from 35 to 17 in September 1991. This process commenced once more in March 1992, when the government officially liberalized almost all prices except a few rationed goods (e.g. petroleum products, housing, electricity and other public services); and by February 1994, price controls on more than 90% of all goods and services in Mongolia had been removed. Between October 1992 and 1996, there were several increases in the price of petroleum products and the national currency was devalued a number of times (Box 1).

As a result, the prices of all goods and services began to escalate and the Mongolian economy experienced high inflation during the early 1990s. Annual inflation rose to 325.5% in 1992, with the highest rise taking place in foodstuffs, at 476.6%. Such high inflation was mainly caused by the extensive liberalization of prices and periodic devaluations of the national currency, as the import dependence of the Mongolian economy was very high. Most of the basket of consumer goods that defines the Consumer Price Index, 70-90% of intermediate goods, and 100% of petroleum products were imported, and this is still the case even today. Nevertheless, owing to a tight monetary policy, annual inflation dropped to 6% in 1998 and further to 1.6% in 2002. In particular, the consumer price index for foodstuffs declined by 1.2% in 2002 from the previous year (Table 1). On the other hand, one may suspect that these lower inflation rates were achieved at the cost of a high rate of hidden unemployment.

2.2. Trade Liberalization and Net Exports

Mongolian trade prior to 1990 was characterized by a state monopoly on trade, a centrally planned pricing system, and limited export markets in the former CMEA[2] countries, in which the Soviet Union occupied the dominant share. During that time, only 7 state-run foreign

Box 1

A Chronology of Devaluation (Rates in MNT per US＄1)

1988	Non-commercial exchange rate introduced at MNT20
Till June 1990	Fixed exchange rate at MNT3
July 1990	Devalued to MNT5.63 and pegged to US＄
May 1991	Devalued to MNT7.10
June 10, 1991	Devaluation of commercial rate to MNT40 For barter trade–MNT7.10 Free market rate–MNT100-150
August 1991	All commercial banks and the Central Bank (Bank of Mongolia) allowed to buy and sell hard currencies.
October 1991	Devalued to MNT100
Ontober 18,01991	Currency exchange center opened in Ulaanbaatar, with rates of MNT125-135
May 1992	Unification of commercial and barter rates at MNT40 Free market rate ranged around MNT250
January 8, 1993	Devalued to MNT150
May 28, 1993	Floating exchange rate introduced, ranging around MNT400

Source: Amarjargal, 2002.

Table 1. **Mongolia: Annual Consumer Price Index Changes for Selected Groups of Commodities 1992-2002 (%)**

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
Overall index	325.5	183.0	66.3	53.1	58.7	9.7	6.0	9.9	8.1	8.1	1.6
Foodstuffs	476.6	197.5	58.7	56.0	52.4	-2.4	0.9	9.1	5.2	9.6	-1.2
Clothing, footwear and cloth	253.0	92.1	81.2	46.2	53.1	26.3	10.5	5.0	-0.3	4.3	5.8
Household goods	279.7	162.3	55.6	82.7	41.8	20.3	-6.8	4.7	2.7	1.2	2.4
Cultural goods and recreation	109.5	270.9	105.5	89.4	65.2	35.7	19.8	15.4	3.9	-1.6	4.4

Source: Mongolian Statistical Yearbook, various issues.

[2] Council for Mutual Economic Assistance

trade corporations were allowed to engage in foreign trade transactions under the state order system. Each of these corporations specialized in a particular form of foreign trade transaction and type of products[3]. However, the country lost its traditional trading partners with the collapse of the CMEA along with the discontinuation of the flow of finance from the Soviet Union due to its internal difficulties and its subsequent collapse in 1990. The financial flow from the Soviet Union was equal to 35% of the country's GDP (Amarjargal, 2002). Moreover, trade transactions began to be made in hard currency, thus ending the transactions in transferable rubles that had been used between CMEA countries.

At that time many enterprises had to halt production due to such difficulties as power cuts and shortages of spare parts, raw materials and fuel. Under these conditions, it was necessary to undertake trade reforms aimed at integration with international trade. Consequently, along with removing the state monopoly, the government abolished all quantitative restrictions on exports and imports, along with the export/import state order system. According to the Law of Mongolia on Economic Entities passed in May 1991, all forms of economic entity, including sole proprietorships, and individuals were allowed to engage freely in independent foreign trade activities. As a result, Mongolia's trade has diversified in terms of export destinations and the sources of its imports.

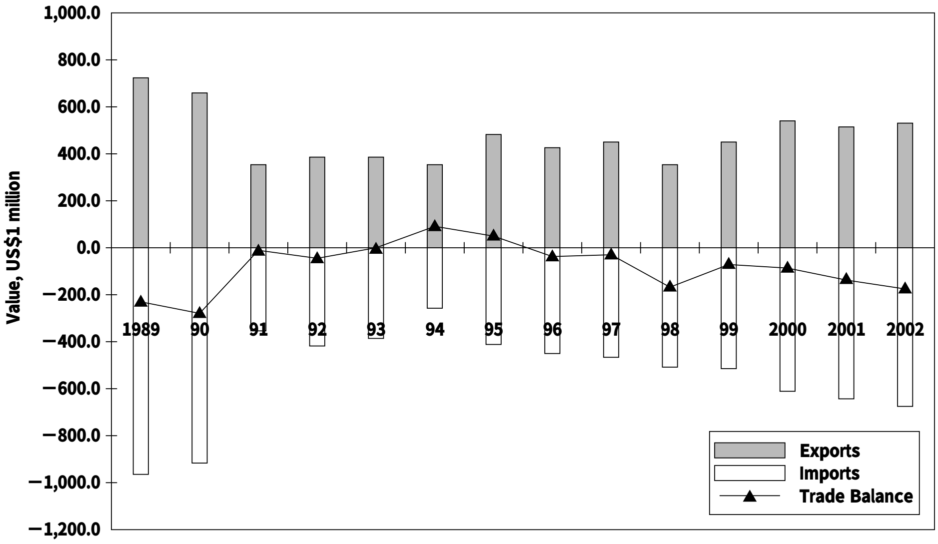
Another step towards its goal of integrating with international trade was Mongolia's accession to the World Trade Organization (WTO) in January 1997. Then, on May 1, 1997, the government began unilaterally to abolish the uniform customs duty of 15% and excise taxes on all imported goods, apart from those levied on a few items, such as alcohol, tobacco, petroleum products and motor vehicles. However, due to a growing need to increase budget revenues, the government increased value-added tax (VAT) from 10% to 13% in September 1998. The following year, in 1999, a 5% uniform import tariff was reintroduced, and an excise tax on beer followed soon after. From November 2000, the customs tariff underwent a further hike from 5% to 7%, with VAT rising to 15%.

Consequently, the Mongolian foreign trade balance has continued to fluctuate heavily since the country began its trade liberalization programs in 1990. External trade turnover declined sharply from its 1989 level until 1994, and although it started to recover in 1995, its value in 2002 remained 27.9% below the 1989 level. During the 1990s, there was initially a large deficit in the trade balance, totaling US$263.3 million in 1990, or 14.2% of GDP; the balance of trade remained negative throughout the entire period 1989-2002, apart from 1993-1995. The highest trade surplus, of US$97.7 million, was recorded in 1994. This was associated with a larger decline in imports than in exports. High inflation, a lack of foreign exchange earnings, the depreciation of the domestic currency, along with a shift from a fixed to a floating exchange rate system in 1993, contributed to this. However, after 1995, the trade balance worsened again because of massive falls in the international market price of major export commodities, such as copper and cashmere; and unfavorable external economic situations, such as the 1997 Asian financial crisis, and the 1998 Russian economic crisis (Figure 1).

2.3. Privatization

A dominant private sector is considered to be the basis for strong economic development, and the role of private sector in Mongolia has been increasing with the ongoing privatization of state assets, which started in 1991. In May

Figure 1. **Mongolia's Foreign Trade 1989-2002**



Source: Mongolian Statistical Yearbook, various issues.

[3] Namely, Mongolexport (all exports); Technikimport (machinery and equipment imports); Materialimpex (trade in construction materials); Avtoneftimport (all imports of vehicles and petroleum products); Raznoimport (consumer goods imports); Compleximport (imports and exports of goods associated with turn-key projects from the former Soviet Union); Mongolimpex (all trade made in convertible currencies).

1991, the Law of Mongolia on Privatization was adopted, setting out the legal bases for the privatization of state properties. The initial stage of the privatization process began with the equal distribution of equally valued coupons (vouchers) to all citizens of the country, to enable them to invest in a variety of enterprises, cooperatives and state-owned farm equities, based on individual choice. Every citizen of Mongolia born on or before the day on which this law took effect received a voucher worth MNT 10,000. Under this scheme, it was estimated that about MNT 20 billion of MNT 55 billion worth of fixed assets owned by the state as of 1991 would be privatized, with shares being held by 2.2 million citizens (Namjim, 2000). In 1991-1994, more than 4500 entities were privatized through this voucher system. The Securities Law of Mongolia was approved in September 1994 and the second stage of privatization began with the stock market in 1995, but its role in the economy continues to be weak. The annual volume stock trading was equal to only 3.7% of the country's GDP in 2002.

Furthermore, the State Property Committee was established in 1996, and a census of state property carried out in 1997. Based on this, the government adopted the Privatization Program for 1997-2000 and the Privatization Guidelines for 2001-2004; the former program focused on the sale of small and medium-sized enterprises and assets, while the latter focused on the privatization of Mongolia's largest or most valuable ones. The Guidelines serve as an official statement of the Government's privatization policies and define enterprise- and sector-specific objectives and priorities. Starting from 1997, state-owned enterprises and state shares in joint stock companies began to be privatized through public auctions, competitive tenders and management contracts, and they became available for purchase by foreigners as well.

However, the consequences of privatization often resulted in undesirable outcomes. Unsuitable methods of privatization and mismanagement of transitional reforms had a negative impact on domestic production capacity and conspired to bring about the failure of light industry, with the only exception being in the cashmere processing industry. Mongolian light industry had developed significant capacity for processing raw materials of livestock origin and manufacturing finished goods that were capable of competing in international markets. For example, in 1988, a new leather garment and leather haberdashery plant - the 'Uyan' factory - was started up in cooperation with Yugoslavia, using investment of more than US$11 million, 70% of which was loan financing. As all the machinery and equipment installed in this plant was purchased from Western manufacturers and used the best technology available at the time, Mongolia was able to export more than 90% of the factory's products to a diverse range of markets, including the most sensitive western markets. The factory employed more than 1,500 workers and continued operating successfully until the end of 1993. The factory managed to repay its initial loan within 3 years and planned to sell a significant amount of its products in U.S. markets, and talks about this were underway. However, following privatization and subsequent management changes, this plan failed to be realized; production then declined, ceasing completely by 1997. It is now under new ownership, with space in the plant being rented out to textile sewing companies.

Nevertheless, as a result of privatization and the emergence of new private assets, the private sector became the prevailing sector in the economy in 1995 and currently produces over 75% of GDP. As of 2001, the private sector share of the agriculture, hunting and forestry sector totaled 98.3%, while the shares in the mining and manufacturing sectors were 74.9% and 94.9% respectively. The private sector's share of financial mediation is increasing as well, accounting for 30.6% in 2001. Work is underway to commercialize the energy and communications sectors, and a legal framework for incorporating land into economic turnover has been constructed. In 2002, Parliament passed the Law on Allocation of Land to Mongolian Citizens. The total area of land to be allocated to citizens for private ownership is 1.2463 million ha, which constitutes 0.9% of the total area of Mongolia, which is 156.4 million ha. The process began on May 1st, 2003, with land being allocated to households and businesses. Privatization in the social and education sectors is also due to start; private sector shares in these fields were 6.5% and 8.2% in 2001. The

Table 2. **Mongolia: Private Sector Share by Industry 1999-2001, at current prices (%)**

Sectors	1999	2000	2001
Agriculture, hunting and forestry	96.4	98.0	98.3
Mining and quarrying	56.0	56.6	74.9
Manufacturing	75.0	78.7	94.9
Construction	89.1	89.2	89.5
Wholesale and retail trade, repair of motor vehicles, motorcycles, personal and household goods	80.3	88.8	90.0
Hotels and restaurants	84.3	91.7	94.6
Transport, storage and communication	41.1	57.7	58.0
Financial intermediation	28.0	31.4	30.6
Real estate, renting & business activities	77.6	82.6	78.5
Education	12.9	11.0	8.2
Health and social work	5.5	6.3	6.5
Other community, social & personal service activities	41.1	45.9	48.4
Total private sector share of GDP	**70.3**	**72.2**	**75.0**

Source: NSO, 2003.

share accounted for by the private sector in each industry is shown in Table 2.

2.4. *Financial Liberalization and Banking Sector Performance*

In line with the restructuring and liberalization taking place in real sectors, the same process is underway in the financial sector, with the aim of transforming it into a sector that supports the country's economic development. Prior to 1991, the banking sector was the only dominant type of financial mediation in the economy, apart from a few insurance organizations. During this period, the exchange rate and interest rates were under state control, and priority sectors were subsidized through government-directed credit programs. However, in October 1990, in line with free market economic reforms, the Mongolian government dissolved the state bank. In 1991, Mongolia enacted a new banking law and accordingly, the banking system was reorganized into a two-tier structure with the Bank of Mongolia acting as the central bank implementing monetary policy, and 16 other banks providing commercial services. However, the banking and financial sectors are still weak and fragile, and not entirely capable of playing a proper role in supporting and promoting economic growth. The overall capital position of the banking system worsened as a result of the deterioration of the loan portfolios of commercial banks.

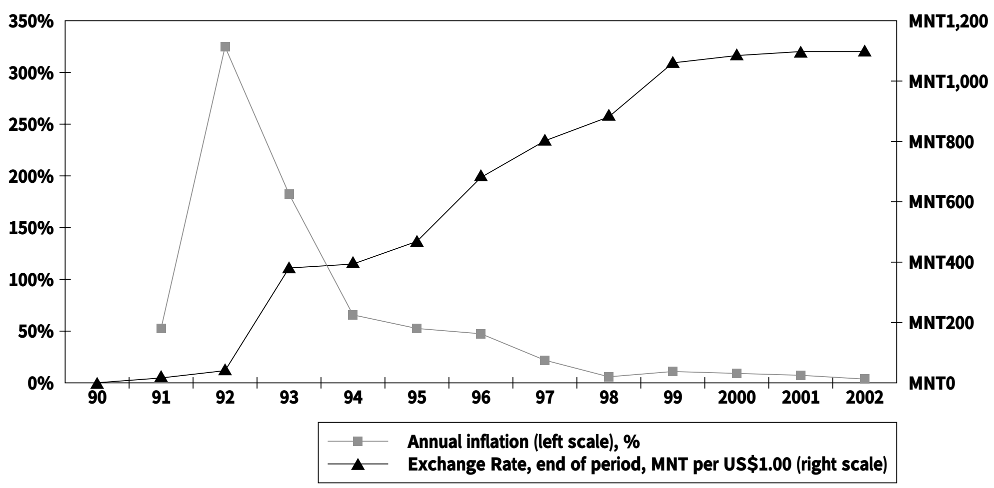
At the same time, exchange rate liberalization was considered to be an integral part of financial and trade liberalization, and this process took place progressively over the course of several devaluations and the establishment of foreign exchange markets. On May 28, 1993, Mongolia switched to a floating exchange rate system (see Box 1). Individuals and enterprises had been allowed freely to exchange the national currency into foreign currencies at the prevailing exchange rates since July 1, 1991. However, all foreign exchange centers were required to be licensed. On August 30, 1990, the first foreign currency auction was held for state enterprises and state and private cooperatives, under the brokerage of the State Bank. Although the amount of foreign currency available was tiny, this was a landmark event in the move towards a market economy (Amarjargal, 2002).

Due to the high inflation spiral in the early 1990s, the annual interest rate on loans issued by commercial banks rose to 213.1% per annum, making it impossible to use such costly financing to conduct any industrial activity. Consequently, bank loans were used only for wholesale and retail trade in imported goods. Interest on loans gradually decreased to an average of 33.3% in 2002, but this is still a high rate for financing long-term investment and production activities.

Mongolia's banking sector suffered three crises: in 1994, 1996 and 1998. The cost of the 1994 restructuring exercise was estimated at over 2% of GDP. The cost of restructuring rose to 7.8% of GDP in 1996, measured solely by the issue of government reconstruction bonds and exceptional liquidity support of about MNT 5.0 billion provided by the Bank of Mongolia to three troubled state-owned banks (the Reconstruction Bank, the Agricultural Bank and Investment and the Technological Innovation Bank). In 1998, these three banks, which held 21.4% of Mongolia's total bank assets, once again became illiquid and insolvent. The direct costs of the 1996-1998 banking crises continued to impose a burden on the budget and the direct cost to the budget was estimated at over 0.6% of GDP in 2001 (World Bank, 2002).

From 1999, individuals and economic entities were allowed to engage in some banking activities and non-bank financial institutions emerged as a new form of financial intermediary. As of 2002, Mongolia had 16 banks and 66 non-bank financial institutions: only two of the banks were state-owned, while another four had state participation in their equity funds. Furthermore, one of the state-owned banks - the Agricultural Bank of Mongolia - which is a major provider of financial services in rural areas of Mongolia, had been privatized through an international competitive tender in 2003. The Japanese company HIS Securities, part of Hideo Sawada's group of companies, became the new owner of this bank. Owing to the monetary policy carried out over the past years, financial mediation in the economy by the banking sector is increasing as

Figure 2. **Mongolia: Annual Inflation and Exchange Rate**



Source: (i) Mongolian Statistical Yearbook, various issues; Bank of Mongolia, 2003.

public confidence in the banks rises.

3. Overall Policy Outcomes: Economic Struggle, Slow Recovery and Other Consequences

3.1. Economic Contraction and Stagnation

Mongolia's transition to a market economy has not been a straightforward one, and, like other countries in transition, it faced a hard economic struggle. The sudden loss of its traditional source of economic assistance and trading partners[4], together with the introduction of a shock-therapy macroeconomic policy aimed at stabilizing the entire economy, caused major economic and social problems. The output of major economic activities, such as industrial and agricultural sectors, declined, external trade turnover fell, and the situation in the banking and financial sectors deteriorated. Massive declines in production capacity and the loss of traditional trading partners in the early 1990s have set the economy back almost 10 years. At the same time, this decade has seen the emergence of new social problems, such as unemployment, poverty and inequality.

Having been hit by a hard initial transitional shock, it took more than a decade for the Mongolian economy to find its way onto the path of economic recovery after its transition to a market economy. Following a difficult start to the transition, Mongolia has achieved some macroeconomic stability since the mid-1990s; however, recovery after the initial sharp declines in GDP in the early 1990s took 12 years, until 2002. Even so, the level in 2002 was only 2.0% above the 1989 level. Between 1990 and 1993, GDP contracted by about 20% as a result of a production decline almost in all sectors of economic activity, and unemployment reached 8.7% in 1994, the highest level recorded during the period 1989-2002. Since 1994, GDP has demonstrated continuous growth at a moderate rate of 3.0% per annum. However, due to large-scale livestock losses as a result of severe winters in 1999-2001, the GDP growth rate declined to 1.1% (Figure 3).

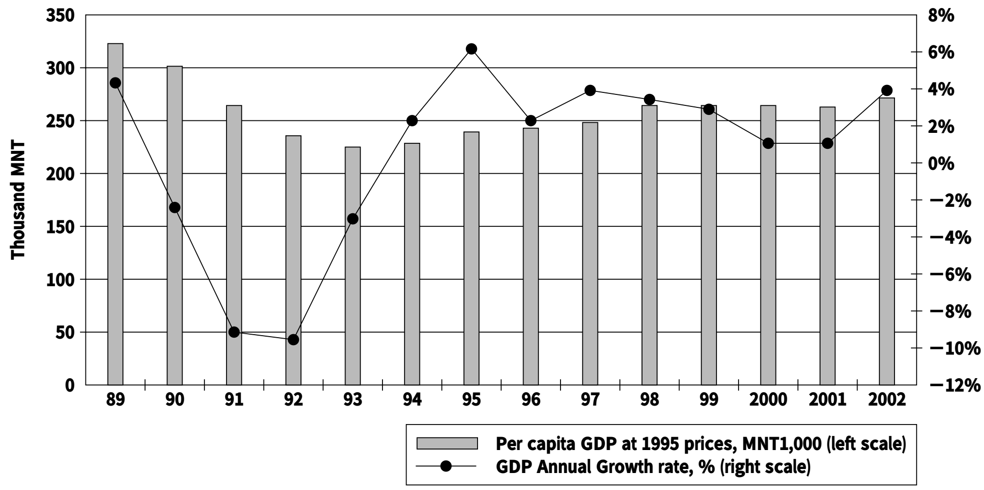
Per capita GDP, evaluated at constant 1995 prices, declined from MNT 322,000 in 1989 to MNT 225,600 in 1993, the lowest level during the period. The dynamics of per capita GDP during 1989-2002 suggest that although per capita GDP began to recover following 1994, by 2002 it still remained at 16.4% below of its level in 1989. Moderate increases in per capita GDP were mainly associated with declining rates of population growth rather than robust achievements in overall GDP growth.

Similarly to most other developing countries, the Mongolian economy is still based on the primary sector, with agricultural raw materials and raw and semi-processed materials from the mining industry dominating exports. Because all of these products are highly vulnerable to price fluctuations in world commodity markets, Mongolia's export earnings have been highly dependent on such factors. For instance, due to an increase in copper prices on the international market, Mongolian export earnings rose by 33% in 1995, thus enabling the economy to grow by 6.3% in 1995, the highest growth rate attained during the entire period 1989-2002.

3.2. External Debt

From 1991, Mongolia began to receive ODA (Official Development Assistance); average per capita ODA in the period 1991-2001 equated to US$92.8 annually, while total ODA accounted for 19.6% of GDP in 2001. Loans accounted for 52.7% of the total ODA disbursed to Mongolia in 1991-2001, with the remaining amounts disbursed as grants. The share of grants in total annual ODA disbursements increased from 14.8% in 1991 to 57.3% in 2001. However, external debt was equivalent to 49% of Mongolia's GNP in 1998 (World Bank, 2000). This signals that a proper policy is required in order to achieve better, more effective utilization of external aid and loans, thereby preventing the economy from accumulating an excessive debt burden. ODA disbursements to the government of Mongolia during 1991-2001 are shown in

Figure 3. **Mongolia: Per Capita GDP and GDP Growth Rate**



Source: Mongolian Statistical Yearbook, various issues.

[4] i.e. the former CMEA member countries.

Figure 4.

3.3. Unemployment

The contraction of the economy has resulted in an increase in unemployment, and, in the absence of income-generating asset-ownership, the unemployed have had to rely on limited public assistance and private transfers until sustained growth generates employment opportunities in the country. Prior to 1989, unemployment was not officially recorded in Mongolia, but after 1990, when the unemployment rate began to be officially recorded, unemployment ranged between 4.6% and 8.5%[5]. The unemployment rate has always been higher among women. However, due to the increased number of new entrants to the labor force in the 1990s, the rate of employment, which is defined as the share of employed persons among the working age population, remains lower. For example, the employment rate was equal to 71.0% in 1992, but declined to 60.5% in 2002 (NSO, 2001 and 2003).

During the 1990s, there were few opportunities for both laid-off workers and new entrants to the labor market to find suitable jobs in the shrinking domestic labor market, due to a massive decline in industrial activities, especially in the manufacturing sector. The Population and Housing Census of 2000 revealed that actual unemployment is much higher than the official rate, based on Employment Regulation Office records. According to the population census of 2000, the unemployment rate was estimated to be equal to 17.5% of the country's total labor force.

3.4. Increasing Poverty and Inequality

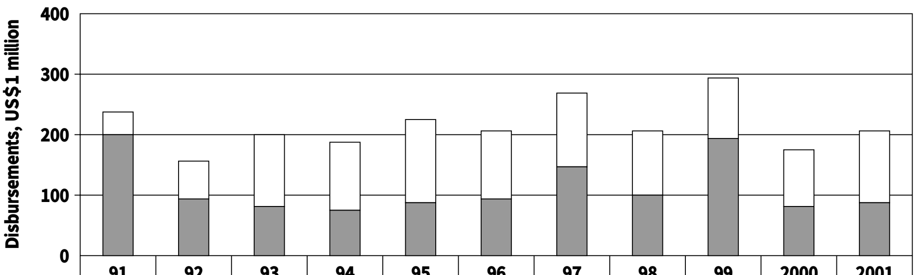
Before 1990, people's basic needs were met and a full range of social services was provided through the mechanism of central planning, therefore there was no officially registered poverty. According to the Participatory Living Standards Assessment (PLSA) made in 2000, the living standards of the population were generally similar until 1992. Between 1992-1995, newly poor and rich people emerged, and the gap between the poor and the rich increased between 1995-2000. While those with access to information and 'connections' to local officials were able to take advantage of new economic opportunities and become quite wealthy, many were less fortunate (NSO and WB, 2001). The number of poor and extremely poor households increased substantially during 1995-2000 at the expense of moderately well-off households, as more people fell into poverty than escaped from it. By the end of 1992, the government estimated that about 16% of the population lived below the poverty line, a figure that increased to 18% in 1993 and 26.5% by March 1994. According to the Living Standards Measurement Surveys (LSMS), poverty incidence increased further to 36.3% in 1995, and 35.6% in 1998. The results of these surveys revealed a strong correlation between unemployment and poverty. While 58% of the unemployed were poor in 1995, 60% were poor in 1998 (NSO, 1999).

Moreover, the PLSA reported that the polarization between the rich and the poor intensified between 1995 and 2000, and at the same time, the increase in the proportion of poor and very poor households became even more marked. By 2000, poor and very poor households were perceived to account for the majority of residents in almost all of the urban communities surveyed, whether large or small. According to Mongolian National Statistical Office estimates, the Gini index rose to 35 in 1998 from 31 in 1995.

4. Conclusion

From the foregoing discussion it can be clearly understood that the implementation of neo-liberal policies during Mongolia's transition towards a free-market economy has not been a straightforward process, and the economy initially experienced a sharp contraction. Despite the persistent stability of macroeconomic indicators, the economic recovery process is slow. Although the economy began to recover in 1993, it has failed to reach its pre-

Figure 4. **ODA Disbursements to Mongolia 1991-2001**



	91	92	93	94	95	96	97	98	99	2000	2001
Grants	34.8	65.6	121	110.3	135.4	114.2	125.2	107.3	98.5	94.5	118
Loans	200.6	92.1	79.4	78.9	90	95.6	145.9	100.4	198.3	83.7	87.8

Source: (i) Economic Cooperation Management and Coordination Department, MOFE; (ii) Treasury Department, MOFE, 2002.

Notes: 1. Following the upgrading of the debt management system in 2001-2, historical debt figures have been revised significantly, compared with previous Mongolia Consultative Group Reports.

2. Loan disbursements for balance of payments support include IMF program disbursements to Mongol Bank, which totaled US$92.6 million between 1990 and 2001.

[5] The unemployment rate is the proportion of unemployed persons, registered with the Employment Regulation Office of Mongolia, among the economically active population.

reform level, despite the passage of more than a decade. Similarly to other transitional economies, the Mongolian economy has experienced almost all forms of neo-liberal policy syndrome and transitional difficulty, such as continued negative net exports, a decline in production, increasing external debt and budget deficits, along with the emergence of other social problems, such as unemployment, poverty and inequality.

Notwithstanding the considerable support and assistance provided by donor countries and such international organizations as the World Bank, IMF and ADB, in terms of both managerial and financial aspects, the transitional mismanagement of economic policy and polarity towards neo-liberalism turned out to be too costly for the Mongolian economy. In particular, a properly thought out program for economic transition and reform was lacking, and policy measures were often introduced without prior explanation or public debate, leading to low levels of public understanding and support. In addition, the new policymakers often failed to recognize the value and support of their predecessors, and neglected almost everything built and developed under the economic system that had prevailed in Mongolia for 70 years. However, such actions may be attributed to a lack of knowledge and inexperience on the part of policymakers, with regard to the functioning of market economic mechanisms. Accordingly, policymakers had few policy options, other than to follow the proposals of external advisors, who often lacked a thorough knowledge of the workings of the Mongolian economy.

Nevertheless, Mongolia could counter that it has achieved certain positive outcomes in a decade of transition towards the diversification of its economic foundations, integration into the global economy, and, most importantly, public perceptions of the free market economy. However, if it continues without a proper strategy for economic development, this may lead to a further deepening of social and economic problems and social unease.

Therefore, any development strategy must be aimed at facilitating the transformation of the Mongolian economy from its current 'deadlocked' position towards a more advanced sustainable path, while identifying the barriers to, as well as potential catalysts for such change. It is globally acknowledged that disadvantaged parts of society are particularly severely affected by discontinuities and shocks in the economic system. Hence, sustainable development cannot be attained in the presence of large-scale poverty. Agenda 21, Poverty Reduction Growth Facility (PRGF) and other initiatives across the globe are attempting to deal with these problems; however, it is essential that these programs and policies be grounded in the reality of grassroots-level conditions, an element that has been lacking in the past.

Based on the foregoing discussion, some recommendations can be made for drafting policy options and an action plan for the development of the Mongolian economy in coming decades. These are as follows: (i) in terms of institutional capacity, the role and status of an independent think-tank that researches policies and economic development with state funding should be enhanced; (ii) with regard to investment policy, rigorous rules should be set, including a requirement that any new investment, whether public or private, domestic or foreign, be based only on the best-available practices and advanced technologies; in addition, government support is needed for investment in pollution prevention and waste removal technologies and their introduction to existing industries (e.g. the agricultural sector should be developed based on ecologically clean practices, rather than favoring the intensive use of chemicals and non-organic fertilizers); finally, marketing tools and the extensive use of Information and Communications Technology are needed in all sectors of domestic industry; (iii) financial mediation in the economy should be improved and long-term credit and development banks established immediately; moreover, experts specializing in capital markets, fund-raising, and asset-based financial engineering and project financing should be educated and re-trained in advanced countries; (iv) a sectoral development strategy and action plan should be based on the elimination of regional disparities and income inequality.

References

Amarjargal, R. (2002). Mongolia: The Early Stage of Transition. A background paper presented at the JIIA International Forum, November 26, 2002.

Bank of Mongolia (2003). *Annual Report 2002* (in Mongolian), Ulaanbaatar: Admon.

GOM (2002). *Poverty Reduction Strategy Paper*. First draft. Ulaanbaatar: Government of Mongolia.

Namjim, T. (2000). *Economy of Mongolia in Three Historical Periods*, (in Mongolian), Ulaanbaatar: Interpress.

NSO (National Statistical Office) (1999). *Living Standards Measurement Survey 1998*. Ulaanbaatar: NSO.

NSO (2001). *Mongolian Statistical Yearbook 2000*. National Statistical Office of Mongolia, Ulaanbaatar: Admon.

NSO (2001a). *Population and Housing Census 2000. Economic Activity: Analysis Based on the 2000 Census*. Ulaanbaatar: NSO.

NSO (2001b). *Population and Housing Census 2000. The Main Results*. Ulaanbaatar: NSO.

NSO (2002). *Mongolian Statistical Yearbook 2001*. National Statistical Office of Mongolia, Ulaanbaatar: Admon.

NSO (2003). *Mongolian Statistical Yearbook 2002*. National Statistical Office of Mongolia, Ulaanbaatar: Kopir Tex.

NSO and WB (2001). *Mongolia: Participatory Living Standards Assessment 2000*. Ulaanbaatar: Admon.

World Bank. (2000). *World Development Report 2000/2001: Attacking Poverty*. Oxford: Oxford University Press.

World Bank (2002). Mongolia: *Public Expenditure and Financial Management Review*. Poverty Reduction and Economic Management Sector Unit, East Asia and Pacific Region. Report No.24439-MOG.