

**Press Release by IMF Mission Team  
Ulaanbaatar, Mongolia  
March 11, 2008**

An IMF mission, led by Mr. Roger Kronenberg, has been in Ulaanbaatar to conduct discussions with the Mongolian authorities for the 2008 Article IV consultation. The IMF holds these discussions with members on a regular basis to review recent economic developments, discuss the economic outlook, and assess economic and financial policies in light of the authorities' medium-term objectives. The mission benefited from discussions with Ministers and senior government officials, the Governor and staff of the Bank of Mongolia, Members of Parliament, and representatives of the private sector and civil society. On return to headquarters, the IMF staff will prepare a report that will be discussed by the IMF's Executive Board, tentatively in May.

Mongolia's economic performance in recent years has been strong. Real GDP increased by 10 percent in 2007, supported by high copper and gold prices and strong investment in the mining and construction sectors. The government budget recorded its third consecutive surplus in 2007, public debt has declined sharply, and international reserves of the Bank of Mongolia have reached record levels. Per capita income has more than doubled since 2004. With its rich mineral endowment and location between two large, fast-growing economies, Mongolia's medium-term outlook is favorable.

But booming economic conditions have also created new risks, particularly rapidly rising inflation which poses a threat to macroeconomic stability. Inflation rose from 6 percent at end-2006 to 17½ percent in January 2008. On the demand side, large increases in civil service wages, social welfare spending, broad money, and banking system credit all spurred rapid growth in spending. On the supply side, increases in import prices, particularly for food and petroleum products, and transportation bottlenecks at the borders put additional upward pressure on prices.

Therefore, the top policy priority is to reduce inflation, which distorts investment decisions and adversely affects households, particularly poor ones. In the medium term, in order to sustain strong growth, Mongolia needs to maintain high levels of investment while preserving the gains achieved in recent years in reducing public debt and keeping it on a sustainable track. There is also a clear need to establish a transparent, stable, and internationally competitive mining regime.

On fiscal policies, the mission believes that the stimulus provided under the 2008 budget is not needed and risks further aggravating inflationary pressures. To prevent high inflationary expectations from getting firmly entrenched, the mission recommended that the authorities maintain a modest budget surplus in 2008 by avoiding any further increases in civil service employment and wages, reducing overlapping social spending and improving its targeting, and curtailing low priority capital spending. The mission also recommended against the introduction of any new spending programs.

To preserve the gains from the reduction of the public debt burden in recent years, the mission recommended that the authorities move very gradually and cautiously in seeking to tap nonconcessional sources of finance. Any external borrowing strategy should not jeopardize macroeconomic stability, and nonconcessional borrowing should be considered only for highly productive projects that cannot be financed from concessional sources.

On monetary policies, the mission recommended that the authorities slow the growth of monetary aggregates to bring down inflation quickly, while recognizing that inflationary pressures also reflect supply-side factors. The mission also emphasized the importance of reintroducing greater exchange rate flexibility, in tandem with monetary policy, to help bring inflation down, facilitate adjustments to external shocks, and maintain external stability. The mission encouraged the authorities to promote the further development of a well-functioning foreign exchange market to support a flexible exchange rate regime.

Mongolia's financial system is generally sound, however some risks exist that need to be carefully managed in order to ensure its continued stability. In particular, the current rapid rate of credit growth could result in a deterioration in banks' loan quality. The Bank of Mongolia is aware of this risk and is monitoring it closely. More generally, the supervision of financial institutions by the Bank of Mongolia and the Financial Regulatory Commission needs to continue to develop to ensure ongoing financial system stability.

The mission team thanked the authorities for their excellent cooperation and the usual very high quality of the discussions.